Economic and Social Development

9th International Scientific Conference

Editors:
Ilko Vrankic, Goran Kozina and Vladimir Kovsca

Book of Proceedings

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Section 1
Globalization and Challenges of the Modern World
ENRICHING EDUCATIONAL POLICY MAKERS & EDUCATORS' INTERCULTURAL COMPETENCE VIA GLOBAL CONFERENCES: AN EXAMPLE OF A SOE GLOBAL CONFERENCE IN INDIA

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ABSTRACT

In most countries in recent years, intellectual communities, educational policy makers, as well as educators are becoming more and more confident that unifying thoughts along with strategies and policies are some of the best tools and tactics to uplift educational standards and the EFL/ESL learner’s outcome, economy of the country, and the wellbeing of individuals in every society. Therefore, intercultural competence (ICC) seems to be a vital vehicle towards international understanding of global educational issues as well as finding the appropriate and suitable solutions. Hence, the idea of sharing thoughts in the domain of education and intellectualism in addition to the integration of universally valuable cultural elements in schools worldwide is becoming a must. This paper emphasizes the necessity of investing in international educational conferences as a strategy toward the betterment of educational reform policies, as well as the impact of intercultural competence on educators, policy makers and strategic planners in the world of education.

Keywords: Culture and Learning, Education, Identity, Intercultural Competence

1. INTRODUCTION

Thousands of years ago, people used to gather in different locations in order to listen to and share new ideas, debate, or argue about new theories. In the early Greeks’ era such as the time of Socrates and his students Plato and Xenophon, gathering for intellectual and educational purposes was a common practice. In other areas of the world such as in the Arab peninsula, poets, for example, would gather in the market area called ‘Souq Oukadh’. Poets used to read their poems, and the best of those poems was selected to be hanged on the wall of Al Kaaba in Makkah. In recent years, conferences took the place of such events and are somehow becoming like a “market place” of the old times. Due to the rapid change in the means of transportation and communication, the task of organizing a conference and getting people from all over the world together is becoming much easier than ever. Complexity of issues related to education and its consequences is no more the burden of a particular society or nation. In other words, ideologies or thoughts may affect farther nations as well (and that may take place via media or immigration or by any other means). Furthermore, sharing ideas and debating new approaches, strategies, or theories in an international gathering seems more fruitful. Hence, successful nations are probably the ones investing more in intellectual educational gatherings because they are fully aware that isolation from the rest of the world brings nothing but suffering intellectually, economically, and more importantly morally.

2. NEW DELHI EXAMPLE

Just few years ago i.e., (December 16th, 2012), the School of Educators (SOE) & All India Conference of Intellectuals (AICOI) held its 31st international gathering of intellectuals from several countries (the author of this article was honored to be a guest in that conference and was awarded the award of Outstanding Higher Education Leader 2012). This unique gathering, first established by the honorable Andira Ghandi more than thirty years ago, was an
opportunity for all the participating intellectuals from different countries not only to see the ‘incredible and colorful’ India, but it was a golden opportunity to listen to the incredible concerns of the marvelous Indian educators and intellectuals from all over the world as well. What was also fascinating (besides the wonderful organization & organizers), is that we all, as educators and policy makers, felt sharing those concerns and were worried about the future of our next generations. In other words, it was obviously noticed that it is no more the concern of India alone, or any other developing country only when it comes to educational problems such as drop-outs, illiteracy in rural areas mainly, or drugs and violence in schools, but it is rather the whole world’s responsibility. In other words, illiteracy does not affect the people in rural areas of India alone, but somehow that phenomenon shall have a negative impact on other nations as well (such as through immigration).

The SOE Global gathering is a rich environment that contributes to Cross-cultural Competence (CCC) and Intercultural Competence (ICC) among intellectuals and educators. This is essential, given the nature of learning in itself, which has the chief aim of communicating with other cultures. Therefore, as mentioned in Benahnia (2012), cultural awareness imposes itself as one of the pillars to our existence as social beings. This gathering helps educators to see the benefits of being aware of the learner’s linguistic and cultural background. It also helps them employ tactics in helping teachers in various schools, universities, colleges, and institutions improve their students’ overall output in their studies and focus more on the importance of Cross-cultural Competence (CCC). The aim of the SOE international conference is very apparent from its objectives as set in its website:

- The conference aims at bringing awareness about Education in general. This year’s theme focuses on Quality in Education and Leadership issues. It would also discuss the future of education, understand Government policies and impact on edupreneurs.
- The conference and its awards encourage innovation and initiatives taken by individuals, institutions, and government in improving the teaching learning process.
- The conferences are a platform for sharing knowledge and best practices in education. It acknowledges, motivates, and commends the work of entrepreneurs and philanthropists in education.
- International leadership development
- To felicitate private sector Initiatives. (SOE Website)

This is essential, given the reality that the world of education is changing rapidly, and both educators and policy makers need to get together. They are concerned with the issues that are impeding the learning process among young learners across the glob. One of the honorable presenters at the SOE 2012 conference stressed the point that education in every school should care and incorporate the moral component in its curriculum and educational system. This seems indeed worth considering, since the absence of moral elements from the curriculum in schools had left a vacuum for other strange thoughts. In addition to that, shallow educational systems are suffering nowadays simply because the moral issue is not being objectively and seriously addressed. When moral subjects were taught in schools, most nations were living in peace and harmony with the lowest crime rate. Moreover, education with no moral foundation is like a sand castle. Not only that, but our textbooks and course materials used in language programs should be designed specifically for the learners of each country. The cultural components involved in those textbooks should reflect the learner’s Mother Tongue Culture (MTC). Therefore, an attempt should be made to use new textbooks reflecting the local customs, linguistic usages, and cultural backgrounds in their context so as to suit the psyche of the local learners and enhance their Intercultural Competence (ICC) That
includes perceptions of self, perception of others, as well as the process itself of becoming aware of the intercultural relationships in culture and identity because as stated by Willems, (2002, p.19), through an education for ICC:

a) We open up to other ways of thinking and other methods of reasoning.  
b) We find a tongue in which we can speak our humanity to each other.  
c) We learn to see that our own view of the world is just one among many.

Therefore, governments and educational policy makers should not only encourage international educational conferences such as SOE, but also financially support them in order to continue serving all nations. More importantly, the media should also focus on how to develop a better understanding of Intercultural Competence (ICC) and whatever may lead to a better understanding of the manifestation of the notion of identity, as well as the cultural components that may lead to this emphasis and especially those involved in teaching. The following part of this article will shed more light on the complexity of these notions. For example, there isn’t one singular definition of the term “Culture”, and this requires further clarification as stated in Benahnia (2012):

So, according to Chamberlain (2005), ‘culture’ represents “the values, norms, and traditions that affect how individuals of a particular group perceive, think, interact, behave, and make judgments about their world” (p197). In other words, culture is more ancient than civilization, i.e. culture began when language began, and this could have been more than a million years ago; whereas civilization began when agriculture began, probably not more than a few thousand years ago. The opposite of culture then is death and “annihilation”; while the opposite of civilization is “… savagery” (cited in Lafayette, 1976, p22).

On the other hand, O’Neil (2006) stated that the word ‘culture’ has many different meanings albeit not exclusive of the preceding comment. For some, it refers to an appreciation of good literature, music, art, and food. For a biologist, it is likely to be a colony of bacteria or other microorganisms growing in a nutrient medium in a laboratory Petri dish. However, for anthropologists and other behavioral scientists, “culture is the full range of learned human behavior patterns” (p1). We have to note here that since Tylor’s time, the concept of culture has become the central focus of anthropology. O’Neil also argues that “Applied linguistics is an interdisciplinary field of study that identifies, investigates, and offers solutions to language-related real life problems”. Some of the academic fields related to applied linguistics are education, linguistics, psychology, anthropology, and sociology. Critiques to this naturalized approach to culture includes Hall’s (2002) view that culture should be perceived socio-culturally meaning both social and cultural factors should be invoked. Socio-cultural practice is not a set of pre-defined descriptors about a group of people. Therefore, based on this argument, O’Neil believes that from this standpoint, culture “emerges in people’s social lives, and consequently particular cultural groups should not be seen as well-defined, homogeneous, and static entities whose members share fixed meanings” (ibid). Along the same lines, and as stated in Benahnia (2012), Street (1993) has claimed that ‘culture’ is a verb (i.e., it “is an active process of meaning making” (p25)) and consequently, according to O’Neil (2006), research should focus not on what culture is, but on what it does in regards to people’s ways of making sense of the world (including their perceptions of the self and others).” This also includes the process itself of becoming aware of the relationships in culture and how they are interwoven. Moreover, Williams et al (1983) admits that culture is “one of the most complicated words in the English language” (p87), especially when moving beyond the mainstream focus of culture learning as information about the other. The
meaning of culture can also be summarized in the following definition given by Nelson Brooks (1975) and stated in Lafayette (1976):

*Figure 1 - Brooks’ (1975) definition of ‘culture’ as stated in Benahnia (2012):*

<table>
<thead>
<tr>
<th>Olympian Culture:</th>
<th>BBV Culture:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Culture is defined as “the best in human life”.</td>
<td>Culture is defined as every aspect of human life. (Beliefs, Behavior and Values)</td>
</tr>
</tbody>
</table>

Brooks’ definition seems very comprehensive, but, as mentioned before, it is not the only definition that applies to EFL teaching. However, it can serve as a great guideline in structuring the distribution and frequency of the cultural elements while developing EFL textbooks or curriculum.

3. ‘INTERCULTURAL COMPETENCE’ IN RELATION TO SOCIETY

It seems that intercultural competence is becoming more apparent in the discussions among scholars in conferences and seminars. Not only that, but educators are becoming aware of its importance in the domain of teaching and learning because it has a direct impact on learners. However, scholars still tend to attribute different definitions to intercultural competence. Fantini (2000), for instance, views ‘intercultural competence’ as “transcending the limitations of one’s own world view” (p31). For some other scholars, such as Antoinette Camilleri Grima (2002) ‘cultural competence’ refers to “an ability to interact effectively with people of different cultures” (ibid).

On the other hand, other scholars tend to link intercultural competence to the notion of diversity. In other words, if we look at diversity within an organizational community, cultural competence would seem vital to every employee to ensure work continuity and survival. From the perspective of real communication among employees and administration, a diverse culture understanding would be a necessity for the entire institution. Diversity must be prevalent and valued before one may be considered ‘culturally competent’ or before we may say that we do have a diversity competent organization. We have to note also that due to the nature of the modern world and technologies we live in nowadays, cultural competence is becoming increasingly necessary for communication, workforce and integration, home comfort and long lasting relationships, as well as community social activities and networking. Historically speaking, as mentioned several research sources, it is not surprising to note that the healthcare profession was the first to promote cultural competence in its field. Poor medical procedures and prescriptions could result in bad consequences due to lack of cross-cultural misunderstanding, or miscommunication.

Diversity Training University International (DTUI) isolated four cognitive components related to intercultural competence, which in turn has direct impacts on the individual’s identity, and these are:

- *awareness,*
- *attitude,*
- *knowledge,*
- *and skills.*
Bearing in mind the above-mentioned characteristics, we can advocate that developing cultural competence leads to an ability of understanding one’s own culture and other cultures. We also tend to communicate with other people, and to effectively interact with people across cultures. Attitude as well as knowledge and skills seem to be crucial for the existence of intercultural competence. Resistance to accepting and dealing with people from other cultures will definitely impede the process of knowledge and skills acquisition. Benahnia (2012) asked the following question: What happens in case of absence of intercultural competence? This simply leads to negative consequences and impact on interlocutors at different levels. One of them is what may happen in the world of business. For example, the lack of cultural competence might damage an individual’s self-esteem and career, “but the unobservable psychological impact on the victims can go largely unnoticed until the threat of a class action suit brings them to light” (Martin & Vaughn, 2007, mentioned in Benahnia, 2012).

The above-mentioned argument can be taken further to say that not all people possess the skills and talents of how to deal with people from other cultures. By the same token, not all members of a community tend to be aware of their own identity characteristics. Yet, there might be a large segment of the population in each community that were born with this innate faculty or ability of understanding other cultures well and communicating with people across cultures, as stated by Mercedes Martin and Billy E. Vaughn:

> While a few individuals seem to be born with cultural competence, the rest of us have had to put considerable effort into developing it. This means examining our biases and prejudices, developing cross-cultural skills, searching for role models, and spending as much time as possible with other people who share a passion for cultural competence. The term multicultural competence surfaced in a mental health publication by psychologist Paul Pedersen (1988) at least a decade before the term cultural competence became popular. Most of the definitions of cultural competence shared among diverse professionals come from the healthcare industry. Their perspective is useful in the broader context of diversity work. (Martin & Vaughn, 2007, mentioned in Benahnia, 2012)

It seems evident then to admit, at this point, that there will be no culture without communication, as Ngugi (1986) advocates:

> Communication creates culture: culture is a means of communication. Language carries culture, and culture carries, particularly through speech and literature, the entire body of values by which we come to perceive ourselves and our place in the world. (pp15-16 mentioned in Benahnia 2012)

To conclude this section, let us not forget that intercultural incompetence is a severe problem that might have negative impacts on the individual’s personality, attitude, achievement, and communication with others. In the case of intercultural incompetence, the individual might face the following feelings on his behalf, or might notice it in his or her interlocutor: surprise, discomfort, irritation, shock, anger, losing face, humor, fear, and intimidation.

**4. INTERNATIONAL CONFERENCES AND THE ISSUE OF ‘IDENTITY’**

Another important factor that unifies the attendees at any conference might be the factor of identity. The term ‘Identity’ likewise is a challenging notion that may be interpreted in
different ways. In the *Merriam Webster Learner’s Dictionary*, the term ‘Identity’ reads as follows:

*The qualities, beliefs, etc., that make a particular person or group different from others. As children grow, they establish their own identities.*

The definition goes further to elaborate that we can also say that a person insisted on having his or her own *identity* [on being known for his or her own qualities, achievements, etc.]. According to Benahnia (2012), Identity is also often associated with *personality*. People who seem to lack individual identity might tend to not have a strong feeling about exactly the kind of people they are. Moreover, on various occasions, we hear people, for example, saying “his/her art reflects his/her cultural/racial identity”. Karl Perera, the owner and author of *more-selfesteeem.com* website summarizes the notion of identity in the following eight questions:

1. Who are you?
2. What makes you unique?
3. What are your values?
4. Your physical identity (what you think you look like to others) also known as body image.
5. Your internal identity (who you think you are in terms of your personality and character, values, etc.).
6. How you see yourself in relation to others?
7. How you identify yourself in terms of your job?

Additionally, another aspect of identity is what probably ties a person to his or her community, tribe, or nation. In other words, the notion of identity becomes broader once it is associated with one’s tribe, nationality, or country. Language teachers are often exposed to issues related to identity, especially when it comes to academic writing. During the early stages of EFL learning, teachers might notice the over-use of the pronoun “I” in the academic writing of their students. Literature in this regard shows that this para-linguistic phenomenon of the over-use of the pronoun “I” is much more apparent in some nations more than others, and it is more common among male learners than female, i.e., in those nations that are male dominated, such as in some countries of the Middle East (see John & Tang, 2009, for example). Moreover, we must note that identity formation is a complex process by itself, especially in target language (TL) learning situations, as it is explained by Norton (1997): “In the case of L2 learning, the identity process can be complicated by the facts that learners are under the influence of two cultural systems whose values can be extremely different from each other. Moreover, the construction of identity cannot be separated from identity negotiation in which an individual seeks for the answer to the question, ‘who am I’ and for his/her relationship to the world” (cited in Lin, 2009, p44 and stated in Benahnia 2012).

Having said that, let us see how identity might have an impact on international conferences attendees. To begin with, in large gatherings, such as international conferences, the feeling of identity is very obvious and stressed in a more public and explicit way. Presentations, talks and papers often emphasize the background of the speaker and demonstrate his or her point of origin and the community to which he or she belongs. Pride is often associated with this atmosphere. In addition to that, both the intellectual and social part of conferences, in most cases, enrich both the notion of intercultural competence and identity. Speakers often depart with vivid high spirit of pride and the willingness of getting in touch with their new
acquaintances, also willing to share and accept as well as respect of people of other cultures and beliefs.

5. CONCLUSION AND AREAS FOR FURTHER RESEARCH
Intercultural competence (ICC) is not a cognitive innate faculty or characteristic, but rather a skill that can be acquired through habit formation, as well as learning and being exposed to other cultures either via actual contact, literature and art, media, technology, or any other means of communication. However, actual or virtual exposure to other cultures and individuals from other speech communities can be considered as the most effective way in that respect. Therefore, it is very evident that international gatherings and conferences play a crucial role in enriching and polishing individuals’ intercultural competence, identity, and the willingness of accepting others.

More areas of research might concentrate on the impact of conferences on educators’ actual performance in class, and the scope of how their inter-personal communication with others might affect the outcome of their students during their learning journey.

LITERATURE
SLOVENIA’S TRADE IN GOODS AND SERVICES WITH AUSTRALIA AND NEW ZEALAND

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**ABSTRACT**  
This paper analyses Slovenia’s trade in goods and services with Australia and New Zealand, two of Slovenia’s less important trading partners. In 2012, the value of Slovenia’s trade in goods and services with Australia and New Zealand amounted to €79 million (0.2 % of the value of Slovenia’s trade in goods and services with the world) and €6.1 million (0.1 ‰ of the value of Slovenia’s trade in goods and services with the world) respectively. Therefore, a number of (additional) measures should be taken by Slovenia in order to enhance its trade in goods and services with both of these countries.  
**Keywords:** Australia, New Zealand, trade in goods and services, trading partner, Slovenia.

1. **INTRODUCTION**  
Between 2008 and 2012, the number of companies that export goods from Slovenia to other countries and that of companies that import goods from other countries to Slovenia increased by 49.4 % and 23.1 % respectively. There were many reasons for this, such as Slovenia’s financial, economic and social crisis, which has had a negative impact on Slovenia’s financial, economic and social situation. As a result, many companies from Slovenia have taken a number of cost-cutting and other measures in order to survive. One of these measures has been their (further) internationalization, which has already had some positive effects on Slovenia’s economy.

2. **SLOVENIA’S TRADE IN GOODS AND SERVICES WITH THE WORLD**  
This section deals with Slovenia’s trade in goods and services with the world. In 2012, the value of Slovenia’s trade in goods and services with the world amounted to €51,646.4 million, an increase of 0.4 % over the previous year. In the same year, the value of Slovenia’s exports of goods and services to the world amounted to €26,217.6 million, an increase of 2.3 % over the previous year, while the value of Slovenia’s imports of goods and services from the world amounted to €25,428.8 million, a decrease of 1.4 % over the previous year.  
In order to enhance its trade in goods and services with the world, notably Asia and some other regions, Slovenia should take a number of cost-cutting and other measures in order to become more competitive in comparison to some other countries in Central and Eastern
Europe (CEE), or any other region. In addition, Slovenia should also take a number of measures in order to become more attractive to foreign people and companies.

2.1. Slovenia’s trade in goods with the world
Slovenia is dependent on its trade in goods with the world. There are many reasons for this, such as the small size of Slovenia’s domestic market for goods. In 2012, the value of Slovenia’s trade in goods with the world amounted to €43,125.2 million, 83.5 % of the value of Slovenia’s trade in goods and services with the world and a decrease of 0.3 % over the previous year. In the same year, the value of Slovenia’s exports of goods to the world amounted to €21,056.2 million, 80.3 % of the value of Slovenia’s exports of goods and services to the world and an increase of 1.2 % over the previous year, while the value of Slovenia’s imports of goods from the world amounted to €22,069 million, 86.8 % of the value of Slovenia’s imports of goods and services from the world and a decrease of 1.6 % over the previous year.

Europe is Slovenia’s most important foreign market for goods. There are many reasons for this, such as the relatively small distance between Slovenia and other countries in the region, notably CEE, and, consequently, relatively low logistics costs. In 2012, the value of Slovenia’s trade in goods with Europe amounted to €36,449.2 million (see Table 1), 84.5 % of the value of Slovenia’s trade in goods with the world and a decrease of 1.6 % over the previous year. In the same year, the value of Slovenia’s exports of goods to Europe amounted to €18,936.1 million (see Table 2), 89.9 % of the value of Slovenia’s exports of goods to the world and a decrease of 0.3 % over the previous year, while the value of Slovenia’s imports of goods from Europe amounted to €17,513.1 million (see Table 3), 79.4 % of the value of Slovenia’s imports of goods from the world and a decrease of 2.9 % over the previous year.

Table 1: Slovenia’s trade in goods by region, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>Value in million €</th>
<th>Percentage of the total value</th>
<th>Value in million €</th>
<th>Percentage of the total value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Africa</td>
<td>497.3</td>
<td>1.2</td>
<td>664.8</td>
<td>1.5</td>
</tr>
<tr>
<td>America</td>
<td>1,671.0</td>
<td>3.9</td>
<td>1,501.6</td>
<td>3.5</td>
</tr>
<tr>
<td>Asia</td>
<td>3,704.1</td>
<td>8.6</td>
<td>4,046.3</td>
<td>9.4</td>
</tr>
<tr>
<td>Europe</td>
<td>37,031.4</td>
<td>85.6</td>
<td>36,449.2</td>
<td>84.5</td>
</tr>
<tr>
<td>Oceania</td>
<td>52.4</td>
<td>0.1</td>
<td>78.4</td>
<td>0.2</td>
</tr>
<tr>
<td>Other</td>
<td>280.1</td>
<td>0.6</td>
<td>384.8</td>
<td>0.9</td>
</tr>
<tr>
<td>Total</td>
<td>43,236.3</td>
<td>100.0</td>
<td>43,125.2</td>
<td>100.0</td>
</tr>
</tbody>
</table>

### Table 2: Slovenia’s exports of goods by region, 2011–2012

<table>
<thead>
<tr>
<th>Region</th>
<th>Value in million € 2011</th>
<th>Percentage of the total value 2011</th>
<th>Value in million € 2012</th>
<th>Percentage of the total value 2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Africa</td>
<td>256.5</td>
<td>1.2</td>
<td>424.7</td>
<td>2.0</td>
</tr>
<tr>
<td>America</td>
<td>528.7</td>
<td>2.5</td>
<td>561.7</td>
<td>2.7</td>
</tr>
<tr>
<td>Asia</td>
<td>964.7</td>
<td>4.6</td>
<td>1,044.8</td>
<td>5.0</td>
</tr>
<tr>
<td>Europe</td>
<td>18,999.6</td>
<td>91.3</td>
<td>18,936.1</td>
<td>89.9</td>
</tr>
<tr>
<td>Oceania</td>
<td>40.1</td>
<td>0.2</td>
<td>69.2</td>
<td>0.3</td>
</tr>
<tr>
<td>Other</td>
<td>19.8</td>
<td>0.1</td>
<td>19.7</td>
<td>0.1</td>
</tr>
<tr>
<td>Total</td>
<td>20,809.5</td>
<td>100.0</td>
<td>21,056.2</td>
<td>100.0</td>
</tr>
</tbody>
</table>


### Table 3: Slovenia’s imports of goods by region, 2011–2012

<table>
<thead>
<tr>
<th>Region</th>
<th>Value in million € 2011</th>
<th>Percentage of the total value 2011</th>
<th>Value in million € 2012</th>
<th>Percentage of the total value 2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Africa</td>
<td>240.8</td>
<td>1.1</td>
<td>240.1</td>
<td>1.1</td>
</tr>
<tr>
<td>America</td>
<td>1,142.3</td>
<td>5.1</td>
<td>939.9</td>
<td>4.3</td>
</tr>
<tr>
<td>Asia</td>
<td>2,739.3</td>
<td>12.2</td>
<td>3,001.5</td>
<td>13.6</td>
</tr>
<tr>
<td>Europe</td>
<td>18,031.8</td>
<td>80.4</td>
<td>17,513.1</td>
<td>79.4</td>
</tr>
<tr>
<td>Oceania</td>
<td>12.3</td>
<td>0.1</td>
<td>9.2</td>
<td>0.0</td>
</tr>
<tr>
<td>Other</td>
<td>260.3</td>
<td>1.2</td>
<td>365.2</td>
<td>1.7</td>
</tr>
<tr>
<td>Total</td>
<td>22,426.8</td>
<td>100.0</td>
<td>22,069.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>


Asia, notably Eastern and South-eastern Asia, is Slovenia’s second most important foreign market for goods. There are many reasons for this, such as its large size. In 2012, the value of Slovenia’s trade in goods with Asia amounted to €4,046.3 million, 9.4 % of the value of Slovenia’s trade in goods with the world and an increase of 9.2 % over the previous year. In the same year, the value of Slovenia’s exports of goods to Asia amounted to €1,044.8 million, 5 % of the value of Slovenia’s exports of goods to the world and an increase of 8.3 % over the previous year, while the value of Slovenia’s imports of goods from Asia amounted to €3,001.5 million, 13.6 % of the value of Slovenia’s imports of goods from the world and an increase of 9.6 % over the previous year. America, notably North America, is Slovenia’s third most important foreign market for goods. In 2012, the value of Slovenia’s trade in goods with America amounted to €1,501.6 million, 3.5 % of the value of Slovenia’s trade in goods with the world and a decrease of 10.1 % over the previous year. In the same year, the value of Slovenia’s exports of goods to America amounted to €561.7 million, 2.7 % of the value of Slovenia’s exports of goods to the world and an increase of 6.2 % over the previous year, while the value of Slovenia’s imports of goods to America amounted to €939.9 million, 4.3 % of the value of Slovenia’s imports of goods to the world and a decrease of 17.7 % over the previous year. Other regions (for example, Oceania) are Slovenia’s less important foreign markets for goods. There are many reasons for this. In the case of Oceania, these reasons include the relatively large distance between Slovenia and Oceanian countries (for example, Australia and New Zealand) and the relatively high logistics costs as a consequence.
2.2. Slovenia’s trade in services with the world

In 2012, the value of Slovenia’s trade in services with the world amounted to €8,521.3 million, 16.5 % of the value of Slovenia’s trade in goods and services with the world and an increase of 4.1 % over the previous year. In the same year, the value of Slovenia’s exports of services to the world amounted to €5,161.4, 19.7 % of the value of Slovenia’s exports of goods and services to the world and an increase of 7 % over the previous year, while the value of Slovenia’s imports of services from the world amounted to €3,359.8 million, 13.2 % of the value of Slovenia’s imports of goods and services from the world and an increase of 0.3 %.

Europe is Slovenia’s most important foreign market for services. In 2012, the value of Slovenia’s trade in services with Europe amounted to €7,972 million, 93.6 % of the value of Slovenia’s trade in services with the world and an increase of 3.8 % over the previous year. In the same year, the value of Slovenia’s exports of services to Europe amounted to €4,839.2 million, 93.8 % of the value of Slovenia’s exports of services to the world and an increase of 6.3 % over the previous year, while the value of Slovenia’s imports of services from Europe amounted to €3,132.9 million, 93.2 % of the value of Slovenia’s imports of services from the world and an increase of 0.1 % over the previous year.

3. SLOVENIA’S TRADE IN GOODS AND SERVICES WITH AUSTRALIA AND NEW ZEALAND

This section deals with Slovenia’s trade in goods and services with Australia and New Zealand, two of Slovenia’s less important trading partners. In 2012, the value of Slovenia’s trade in goods and services with Australia and New Zealand amounted to €85.1 million (see Table 4), 0.2 % of the value of Slovenia’s trade in goods and services with the world and an increase of 46.3 % over the previous year. In the same year, the value of Slovenia’s exports of goods and services to Australia and New Zealand amounted to €74.9 million (see Table 5), 0.3 % of the value of Slovenia’s exports of goods and services to the world and an increase of 69.2 % over the previous year, while the value of Slovenia’s imports of goods and services from Australia and New Zealand amounted to €10.2 million (see Table 6), 0.4 % of the value of Slovenia’s imports of goods and services from the world and a decrease of 26.8 % over the previous year.

Table 4: Slovenia’s trade in goods and services with Australia and New Zealand, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>Percentage of the total value</th>
<th>2012</th>
<th>Percentage of the total value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value in million €</td>
<td></td>
<td>Value in million €</td>
<td></td>
</tr>
<tr>
<td>Australia</td>
<td>53.3</td>
<td>91.6</td>
<td>79.0</td>
<td>92.9</td>
</tr>
<tr>
<td>New Zealand</td>
<td>4.9</td>
<td>8.4</td>
<td>6.1</td>
<td>7.1</td>
</tr>
<tr>
<td>Total</td>
<td>58.2</td>
<td>100.0</td>
<td>85.1</td>
<td>100.0</td>
</tr>
</tbody>
</table>


Table 5: Slovenia’s exports of goods and services to Australia and New Zealand, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>Percentage of the total value</th>
<th>2012</th>
<th>Percentage of the total value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value in million €</td>
<td></td>
<td>Value in million €</td>
<td></td>
</tr>
<tr>
<td>Australia</td>
<td>40.8</td>
<td>92.1</td>
<td>70.0</td>
<td>93.5</td>
</tr>
<tr>
<td>New Zealand</td>
<td>3.5</td>
<td>7.9</td>
<td>4.9</td>
<td>6.5</td>
</tr>
<tr>
<td>Total</td>
<td>44.3</td>
<td>100.0</td>
<td>74.9</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Table 6: Slovenia’s imports of goods and services from Australia and New Zealand, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>2011 Value in million €</th>
<th>Percentage of the total value</th>
<th>2012 Value in million €</th>
<th>Percentage of the total value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>12.5</td>
<td>90.1</td>
<td>9.0</td>
<td>88.2</td>
</tr>
<tr>
<td>New Zealand</td>
<td>1.4</td>
<td>9.9</td>
<td>1.2</td>
<td>11.8</td>
</tr>
<tr>
<td>Total</td>
<td>13.9</td>
<td>100.0</td>
<td>10.2</td>
<td>100.0</td>
</tr>
</tbody>
</table>


3.1. Slovenia’s trade in goods and services with Australia

Australia is the largest island country by area and population in Oceania. In 2012, the value of Slovenia’s trade in goods and services with Australia amounted to €79 million, 0.2 % of the value of Slovenia’s trade in goods and services with the world and an increase of 48.2 % over the previous year. In the same year, the value of Slovenia’s exports of goods and services to Australia amounted to €70 million, 0.3 % of the value of Slovenia’s exports of goods and services with the world and an increase of 71.7 % over the previous year, while the value of Slovenia’s imports of goods and services from Australia amounted to €9 million, 0.5 ‰ of the value of Slovenia’s imports of goods and services from the world and a decrease of 28.4 % over the previous year.

3.1.1. Slovenia’s trade in goods with Australia

In 2012, the value of Slovenia’s trade in goods with Australia amounted to €68.9 million, 87.2 % of the value of Slovenia’s trade in goods and services with Australia and an increase of 53.4 % over the previous year. In the same year, the value of Slovenia’s exports of goods to Australia amounted to €62.4 million, 89.1 % of the value of Slovenia’s exports of goods and services with Australia and an increase of 81.2 % over the previous year, while the value of Slovenia’s imports of goods from Australia amounted to €6.5 million, 81.9 % of the value of Slovenia’s imports of goods and services from Australia and a decrease of 37.9 % over the previous year.

3.1.2. Slovenia’s trade in services with Australia

In 2012, the value of Slovenia’s trade in services with Australia amounted to €10.1 million, 12.8 % of the value of Slovenia’s trade in goods and services with Australia and an increase of 20.2 % over the previous year. In the same year, the value of Slovenia’s exports of services to Australia amounted to €7.6 million, 10.9 % of the value of Slovenia’s exports of goods and services with Australia and an increase of 20.2 % over the previous year, while the value of Slovenia’s imports of services from Australia amounted to €2.5 million, 18.1 % of the value of Slovenia’s imports of goods and services from Australia and an increase of 20.1 % over the previous year.

3.2. Slovenia’s trade in goods and services with New Zealand

New Zealand is the third largest island country by area and population in Oceania. It consists of two islands (the North Island and the South Island) separated by Cook Strait, and many small islands. In 2012, the value of Slovenia’s trade in goods and services with New Zealand amounted to €6.1 million, 0.1 ‰ of the value of Slovenia’s trade in goods and services with the world and an increase of 24.9 % over the previous year. In the same year, the value of Slovenia’s exports of goods and services to New Zealand amounted to €4.9 million, 0.2 ‰ of the value of Slovenia’s exports of goods and services to the world and an increase of 39.7 %

over the previous year, while the value of Slovenia’s imports of goods and services from New Zealand amounted to €1.2 million, 0.1 \% of the value of Slovenia’s imports of goods and services from the world and a decrease of 12.6 \% over the previous year.

3.2.1. Slovenia’s trade in goods with New Zealand
In 2012, the value of Slovenia’s trade in goods with New Zealand amounted to €5 million, 82.2 \% of the value of Slovenia’s trade in goods and services with New Zealand and an increase of 35.5 \% over the previous year. In the same year, the value of Slovenia’s exports of goods to New Zealand amounted to €4 million, 81.9\% of the value of Slovenia’s exports of goods and services to New Zealand and an increase of 54 \% over the previous year, while the value of Slovenia’s imports of goods from New Zealand amounted to €1 million, 83.2 \% of the value of Slovenia’s imports of goods and services from New Zealand and a decrease of 8.6 \% over the previous year.

3.2.2. Slovenia’s trade in services with New Zealand
In 2012, the value of Slovenia’s trade in services with New Zealand amounted to €1.1 million, 17.8 \% of the value of Slovenia’s trade in goods and services with New Zealand and a decrease of 8.1 \% over the previous year. In the same year, the value of Slovenia’s exports of services to New Zealand amounted to €0.9 million, 18.1 \% of the value of Slovenia’s exports of goods and services to New Zealand and a decrease of 1.8 \% over the previous year, while the value of Slovenia’s imports of services from New Zealand amounted to €0.2 million, 16.8 \% of the value of Slovenia’s imports of goods and services from New Zealand and a decrease of 28.2 \% over the previous year.

3.3. Some measures to enhance Slovenia’s trade in goods and services with Australia and New Zealand
Australia and New Zealand are increasingly dependent on their trade in goods and services with Asia (notably Eastern and South-eastern Asia), which is, according to Walsh (2014), ”the world’s most dynamic region” (p. 18). In 2012, the value of Australia’s and New Zealand’s trade in goods with Asia amounted to €266,803.6 million, an increase of 8.6 \% over the previous year, and €29,483 million, an increase of 17.9 \% over the previous year, respectively. As a result, the financial, economic and social situation in both countries is relatively good (in the case of Australia, see International Monetary Fund, 2014a; while in the case of New Zealand, see International Monetary Fund, 2014b), which is an important reason why both are increasingly attractive to foreign people and companies.

- In order to enhance its trade in goods and services with Australia and New Zealand, Slovenia should:
  - increase cooperation between companies that export goods and/or services from Slovenia to Australia and/or New Zealand;
  - increase cooperation between companies that import goods and/or services from Australia and/or New Zealand to Slovenia;
  - increase cooperation between companies that do not export goods and/or services from Slovenia to Australia and/or New Zealand, but would like to;
  - increase cooperation between companies that do not import goods and/or services from Australia and/or New Zealand to Slovenia, but would like to;
increase cooperation between companies that export goods and/or services from Slovenia to Australia and/or New Zealand, and companies that do not export goods and/or services from Slovenia to Australia and/or New Zealand, but would like to;

increase cooperation between companies that import goods and/or services from Australia and/or New Zealand to Slovenia, and companies that do not import goods and/or services from Australia and/or New Zealand to Slovenia, but would like to;

increase cooperation between people and/or companies from Slovenia on the one hand, and people and/or companies from Australia and/or New Zealand on the other hand;

remove unnecessary barriers to trade in goods and services between Slovenia on the one hand, and Australia and/or New Zealand on the other hand;

etc.

4. EU’S TRADE POLICY TOWARDS AUSTRALIA AND NEW ZEALAND

This section deals with the EU’s trade policy towards Australia and New Zealand. The EU’s trade policy is set out in Articles 206 and 207 of the Treaty on the Functioning of the European Union. Trade policy is the exclusive competence of the EU, which means that only the EU, and not the Member States (including Slovenia, which joined the EU on 1 May 2004), can legislate on trade matters and conclude international trade agreements. There are three institutions involved in making the trade policy decisions. The European Commission proposes trade legislation. The legislation is then adopted in co-decision by the Council of the European Union and the European Parliament. The adopted decisions are published in the Official Journal of the European Union and are binding in their entirety and directly applicable in all Member States (including Slovenia). The EU does not have a trade agreement with either Australia or New Zealand. Trade relations between the EU and Australia are set out in the European Union – Australia Partnership Framework, which in 2008 replaced the Agenda for Cooperation and the Joint Declaration on Relations between Australia and the European Union, while trade relations between the EU and New Zealand are set out in the Joint Declaration on Relations and Cooperation between the European Union and New Zealand, which in 2007 replaced the Priorities for Future Cooperation and the Joint Declaration on Relations between the European Union and New Zealand.

Australia and New Zealand are two of the EU’s less important trading partners. In 2012, the value of the EU’s trade in goods with Australia and New Zealand amounted to €46,096 million (0.5 % of the value of the EU’s trade in goods with the world and an increase of 5.1 % over the previous year) and €7,018.9 million (0.1 % of the value of the EU’s trade in goods with the world and an increase of 0.3 % over the previous year) respectively (see Table 7). In the same year, the value of the EU’s exports of goods to Australia and New Zealand amounted to €33,717.6 million (0.8 % of the value of the EU’s exports of goods to the world and an increase of 9.5 % over the previous year) and €3,560.1 million (0.1 % of the value of the EU’s exports of goods to the world and an increase of 6 % over the previous year) respectively (see Table 8), while the value of the EU’s imports of goods from Australia and New Zealand amounted to €14,721.2 million (0.3 % of the value of the EU’s imports of goods from the world and a decrease of 3.9 % over the previous year) and €3,458.9 million (0.1 % of the value of the EU’s imports of goods from the world and a decrease of 4.9 % over the previous year) respectively (see Table 9).
### Table 7: EU’s trade in goods with Australia and New Zealand, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value in million €</td>
<td>Percentage of the total value</td>
</tr>
<tr>
<td>Australia</td>
<td>46,096.0</td>
<td>86.8</td>
</tr>
<tr>
<td>New Zealand</td>
<td>6,998.1</td>
<td>13.2</td>
</tr>
<tr>
<td>Total</td>
<td>53,094.1</td>
<td>100.0</td>
</tr>
</tbody>
</table>


### Table 8: EU’s exports of goods to Australia and New Zealand, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value in million €</td>
<td>Percentage of the total value</td>
</tr>
<tr>
<td>Australia</td>
<td>30,784.2</td>
<td>90.2</td>
</tr>
<tr>
<td>New Zealand</td>
<td>3,359.4</td>
<td>9.8</td>
</tr>
<tr>
<td>Total</td>
<td>34,143.6</td>
<td>100.0</td>
</tr>
</tbody>
</table>


### Table 9: EU’s imports of goods from Australia and New Zealand, 2011–2012

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value in million €</td>
<td>Percentage of the total value</td>
</tr>
<tr>
<td>Australia</td>
<td>15,311.8</td>
<td>80.8</td>
</tr>
<tr>
<td>New Zealand</td>
<td>3,638.7</td>
<td>19.2</td>
</tr>
<tr>
<td>Total</td>
<td>18,950.5</td>
<td>100.0</td>
</tr>
</tbody>
</table>


In 2012, Slovenia accounted for 1.4 % of the value of the EU’s trade in goods with Australia and 0.7 % of the value of EU’s trade in goods with New Zealand. In the same year, Slovenia accounted for 1.9 % of the value of the EU’s exports of goods to Australia and 1.1 % of the value of the EU’s exports of goods to New Zealand. In the same year, too, Slovenia accounted for 0.4 % of the value of EU’s imports of goods from Australia and 0.3 % of the value of EU’s imports of goods from New Zealand.

In order to enhance its and its Member States’ trade in goods and services with Australia and New Zealand, the EU should change its trade policy towards these two countries and take a number of other measures, such as increasing the cooperation between companies that export goods and/or services from the EU to Australia and/or New Zealand.

### 5. CONCLUSION

Australia and New Zealand are two of Slovenia’s less important trading partners. There are many reasons for this, such as the relatively large distance between Slovenia, on the one hand, and Australia and New Zealand, on the other. In 2012, the value of Slovenia’s trade in goods and services with these two countries amounted to €85.1 million, 0.2 % of the value of Slovenia’s trade in goods and services with the world. This means that there is considerable scope for enhancing Slovenia’s trade in goods and services with both of these two countries.
LITERATURE
USAGE OF SERVQUAL FOR ASSESSMENT OF CUSTOMERS` SATISFACTION WITH SERVICES OF PRIMARY HEALTHCARE PUBLIC INSTITUTIONS IN THE CITY OF SIBENIK

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ABSTRACT
This paper presents results of an empirical research of quality of services provided in primary healthcare public institutions in the city of Sibenik (with special emphasis on family clinics) by applying SERVQUAL instrument. The research was conducted in December 2014 and January 2015 on a sample of 218 examinees and it tried to establish whether there was a difference between customers` expectation and their satisfaction with the received services in primary healthcare public institutions in Sibenik, what is the level of their overall satisfaction, what is the level of satisfaction with certain elements of services and, finally, whether specific determinants such as employment status, frequency in usage of services and usage of services (also) in private institutions significantly influence examinees` contentment with primary healthcare services in public institutions. The results have shown that there is a significant difference between expectations and satisfaction of examinees with received medical services according to all observed variables in SERVQUAL model, which leads to the conclusion that quality of services in primary healthcare public institutions in Sibenik is not satisfactory. When it comes to satisfaction with specific elements of medical services, it has been concluded that the examinees are least pleased with the duration of time necessary to have physical check-ups and with insufficiently modern medical equipment. Moreover, it has been established that the frequency in usage of services significantly influences the overall contentment of the examinees whereas those who use mentioned services quite often are actually those who are the least satisfied.

Keywords: city of Sibenik, primary healthcare, service quality, SERVQUAL gap

1. INTRODUCTION
Ever since the beginning of the 1990s health sector in the Republic of Croatia has experienced significant reforms, primarily with the intention of extending life expectancy and „improving quality of public healthcare services and protection“ (Ministry of Finance, 2014). It is therefore essential to constantly monitor and analyze attitudes, expectations and opinions of health services users in order to establish if they match with, and to what extent, those of healthcare providers“(Ozretic Dosen et al., 2009, p. 28).
There is no agreement between scientists on definition of quality in total healthcare systems, among population or in the separate healthcare services. Different cultures have different values and priorities; for some “good” is the very existence of medical staff and facilities,
whereas for some it means equity and empathy, and for developed countries it means optimal clinical outcomes (Tipurić, 2014). Moreover, there is no agreement on methods of measuring quality of medical services. The greatest reason for that is the fact that medical or healthcare organizations are service companies and thus have their own specific qualities related to products and these are namely the lack of substantial properties, transience and heterogeneity (Trbusic; 2005; Sisko Kulis, Grubisic, 2010) while some other authors stress the problem of possession (eg Pupovac, 1999; Ozretić Dosen; 2002; Kotler et al., 2006; Kotler, Keller, 2008). Besides already mentioned characteristics, the process of measuring medical services is a complex one for following reasons: impossibility of controlling and rejecting services that do not correspond to a certain standard before their administering (Ozretić Dosen et al., 2010, p. 32); it is more difficult to distinguish level of quality in medical than in other services, primarily because they imply human beings and connect their welfare directly to quality; users always want more and their expectations of quality are different from quality offered; only practice, careful listening and attention can lead to a more or less truthful idea (Kolanović, 2007, pp. 214-215).

The main problem of this research is: measuring service quality of primary healthcare in the city of Sibenik. With this research several questions have been addressed:
1. Is there a difference between users expectations and their satisfaction with given medical care in institutions of primary healthcare?
2. What is the level of satisfaction with specific elements of healthcare services in Sibenik?
3. What is the level of overall satisfaction with primary healthcare services?
4. Whether some characteristics of respondents, such as employment status, frequency in usage of services and usage of services (also) in private institutions, significantly influence examinees’ contentment with primary healthcare services in public institutions?

It is expected that the results of this research will expand common notion about clients’ pleasure with primary healthcare services and thus contribute to scientists and practitioners in solving problems and discovering possibilities in reaching contentment in this sector.

2. THEORETICAL FRAME
This paper analyzes quality of medical service from the viewpoint of users (patients) and quality of service measurements in the empirical research has been conducted by method of assessing users’ satisfaction. This suggests that quality and satisfaction have been used as synonyms as it was already stated in some of the available empirical studies (Zeithaml et al., 1993; Iacobucci et al., 1996). Emphasis should be made that in some studies there is a distinction between these two concepts and Bolton and Drew (1991) state that quality of service is an attitude about the service company whereas clients’ satisfaction refers to individual service encounters, according to Boulding et al (1993) the term “customers satisfaction” is a cumulative measure but it is not the same as quality of service.
There are two key elements in measurements of service quality: customers expectations (Brown and Swartz, 1989) and perceived quality that reflects customers opinion about the excellence of service (Zeithaml, 1988). In the light of these factors Parasuraman et al. developed SERVQUAL model in 1985 which identified ten dimensions for measurement of service quality. With further improvements of this process, the same authors developed a new model of dimensions in 1988 where the previous ten dimensions were reduced to five as follows: reliability, responsiveness, empathy, assurance and tangibles. From the listed dimensions it is perfectly clear that services possess less tangible elements and the research therefore needs to focus more on intangible ones. The mentioned criterions have been
established as “relevant for many services” (Johnson, 2002). Nevertheless, research into different service policies with the aim of adjusting to specific characteristics of services emphasised the need to omit, add or change the list of dimensions according to SERVQUAL and the original model and its scale have been modified several times (e.g. Carman, 1990; Headley and Miller, 1993, Engelland et al., 2000).

SERVQUAL model has been subjected to criticism by numerous scientists (e.g. Lewis and Mitchell, 1990, p. 15; Cronin and Taylor; 1992, pp. 55-56; Teas; 1993, p. 29). These critical comments have largely been directed towards theoretical base of the model and its operational mode (measurement principles). The most frequent criticism is related towards validity and reliability of the model, measurements of expectations and structure of dimensions.

“However, due to its positive elements – simplicity of use and ability of instruments to provide quantitative assessment, the model has been accepted and applied for measuring quality of different types of services” (Ozretic Dosen et al., 2010, p. 33) and therefore medical services as well. There is a general attitude that results in SERVQUAL model predict the overall quality of services in a very reliable way (Khan, 2003, p. 121). This model has been accepted as the key instrument for measuring immediate service quality in the medical sector and due to this reason ever increasing number of researchers have been using it in their work (e.g. Anderson, 1995; Sohail, 2000; Andaleb, 2001; Kilbourne et al., 2004). However, in Croatia there have been only a few researches on quality of medical service by applying the SERVQUAL model: in 2005 on primary healthcare services in Osijek (Verner, 2005) and in 2010 on primary healthcare services and their users in Zagreb and the Zagreb County (Ozretic Dosen et al., 2010). Bajto and Kondic measured customers’ satisfaction with the Public municipal hospital in Nasice.

The lack of available research indicates the conclusion that there are still not enough relevant data in Croatia which could identify the level of contentment of medical services’ users and this, consequently, justifies this paper and the analysis that was conducted.

3. RESEARCH METHODOLOGY

A questionnaire has been prepared according to dimensions from the SERVQUAL model and has been adjusted to specific characteristics of medical services. After pre-testing conducted on 8 examinees, the range of the questionnaire has been reduced from the initial 22 to 20 claims. Two items of the original SERVQUAL instrument were deleted because of their unsuitability for the research context and due to the lack of understanding by the respondents. The final questionnaire consisted of two sets of 20 items, representing the modified SERVQUAL scale.

The questionnaire consisted of three parts. In the first part there were measured expectations of examinees about the quality of primary healthcare services in general, while the second one contained measured perception of customers about the services provided. The third part contained questions regarding gender, age, employment status, frequency of using services in primary healthcare public institutions and use of medical services in private institutions of primary healthcare. At the end of the questionnaire examinees were asked to express their satisfaction with the quality of services in primary healthcare institutions by giving a single evaluation mark.

A Likert scale of five degrees was used in measuring quality of expected and given services. The main population in this survey consisted of all users of services in primary healthcare public institutions in Sibenik above 16. The questionnaire was not intended for children younger than 16 since parents’ consent would have been necessary, which would complicate the research. In addition, it was assumed that some of the concepts and terms may not have been fully comprehended on their part. The sample thus consisted of persons of eligible age
who were users of services in primary healthcare public institutions in Sibenik and were willing to participate. The research was conducted in December 2014 and January 2015. Input and data processing were finalised by using statistical package IBM SPSS Statistics 21. To enable ease of data entry, questions were precoded beforehand.

12 examinees out of 230 haven’t completed the questionnaire. Their answers were excluded from the following analysis and the final results of empirical research were obtained by analyzing 218 questionnaires.

The classical approach of applying Cronbach criterion was used for empirical validation of the model that surveyed quality of services in primary medical health care. The total value for coefficient of reliability that refers to expectations is 0.885 whereas for real satisfaction is 0.953. When analyzing specific values for each variable, everything surpasses the recommended level of 0.5 ranging from 0.875 to 0.955. This implies that coefficient of reliability while using characteristics of SERVQUAL instruments in health care sector does not distinguish itself significantly from other service branches.

4. RESEARCH RESULTS

Table 1 shows the results of research with regard to the characteristics of the respondents.

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Modality</th>
<th>Absolute frequency</th>
<th>Relative frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>gender</td>
<td>male</td>
<td>110</td>
<td>50.5</td>
</tr>
<tr>
<td></td>
<td>female</td>
<td>108</td>
<td>49.5</td>
</tr>
<tr>
<td>age</td>
<td>16-29</td>
<td>71</td>
<td>32.6</td>
</tr>
<tr>
<td></td>
<td>30-49</td>
<td>76</td>
<td>34.9</td>
</tr>
<tr>
<td></td>
<td>50 and more</td>
<td>71</td>
<td>32.6</td>
</tr>
<tr>
<td>employment status</td>
<td>student</td>
<td>31</td>
<td>14.2</td>
</tr>
<tr>
<td></td>
<td>employed</td>
<td>101</td>
<td>46.3</td>
</tr>
<tr>
<td></td>
<td>unemployed</td>
<td>53</td>
<td>24.3</td>
</tr>
<tr>
<td></td>
<td>retiree</td>
<td>33</td>
<td>15.1</td>
</tr>
<tr>
<td>frequency in usage of services</td>
<td>often</td>
<td>52</td>
<td>23.9</td>
</tr>
<tr>
<td></td>
<td>several times a year</td>
<td>145</td>
<td>66.5</td>
</tr>
<tr>
<td></td>
<td>rarely</td>
<td>21</td>
<td>9.6</td>
</tr>
<tr>
<td>usage of services also in private institutions</td>
<td>yes</td>
<td>87</td>
<td>39.9</td>
</tr>
<tr>
<td></td>
<td>no</td>
<td>131</td>
<td>60.1</td>
</tr>
</tbody>
</table>

As shown in table 1, the sample included almost equal number of male (50.5%) and female (49.5%) examinees. The majority of those examined belong to the age group between 30 and 49 (34.9%). According to employment status the largest portion are employed persons (46.3%). The greatest number of examinees (66.5%) uses services of primary healthcare institutions several times per year. It is extremely interesting that 39.9% examinees along with services in primary healthcare public sector, use services of private institutions of primary health care.

The total rating of satisfaction with quality of services in primary healthcare institutions in Sibenik is 3.33 with average deviation of 0.843. The results of One-Way MANOVA analysis have shown that there is statistically significant dis(satisfaction) with the overall quality of services regarding frequency of their usage in primary healthcare institutions (p=0.017). The examinees that use these services most often are in fact those who are the least satisfied. They rated the total quality with 3.10. The rating of examinees who use services several times a
year is 3.37 while those who use services rarely evaluated them as being quite satisfactory and quality assessment was 3.62.

The impact of characteristics employment status and usage of services (also) in private institutions on overall satisfaction is not significant (p=0.194 and p=0.842). The paper will therefore now analyze average ratings of expected and real satisfaction of examinees with services of primary healthcare institutions in the city of Sibenik.

Table 2: Average values of expectation and real satisfaction of examinees and the test of relevance of differences

<table>
<thead>
<tr>
<th>Dimension</th>
<th>Variable</th>
<th>Expectations</th>
<th>Perception</th>
<th>Gap</th>
<th>t-test</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td>4.62</td>
<td>3.09</td>
<td>-1.53</td>
<td>20.258</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>4.37</td>
<td>3.25</td>
<td>-1.12</td>
<td>14.683</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>4.65</td>
<td>4.02</td>
<td>-0.63</td>
<td>9.398</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>4.84</td>
<td>3.83</td>
<td>-1.01</td>
<td>16.126</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>4.61</td>
<td>3.19</td>
<td>-1.42</td>
<td>16.455</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>4.60</td>
<td>3.25</td>
<td>-1.35</td>
<td>17.595</td>
<td>.000</td>
</tr>
<tr>
<td>Tangibles</td>
<td>7</td>
<td>4.64</td>
<td>3.45</td>
<td>-1.19</td>
<td>15.299</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>4.62</td>
<td>3.21</td>
<td>-1.41</td>
<td>16.793</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>9</td>
<td>4.61</td>
<td>3.29</td>
<td>-1.32</td>
<td>16.676</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>10</td>
<td>4.47</td>
<td>3.24</td>
<td>-1.23</td>
<td>15.808</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>11</td>
<td>4.49</td>
<td>2.90</td>
<td>-1.59</td>
<td>18.865</td>
<td>.000</td>
</tr>
<tr>
<td>Reliability</td>
<td>12</td>
<td>4.64</td>
<td>3.47</td>
<td>-1.17</td>
<td>15.185</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>13</td>
<td>4.31</td>
<td>3.06</td>
<td>-1.25</td>
<td>13.491</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>14</td>
<td>4.65</td>
<td>3.32</td>
<td>-1.33</td>
<td>18.076</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>15</td>
<td>4.71</td>
<td>3.49</td>
<td>-1.22</td>
<td>15.832</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>16</td>
<td>4.54</td>
<td>3.46</td>
<td>-1.08</td>
<td>12.065</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>17</td>
<td>4.56</td>
<td>3.25</td>
<td>-1.31</td>
<td>17.969</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>18</td>
<td>4.16</td>
<td>3.17</td>
<td>-0.99</td>
<td>11.254</td>
<td>.000</td>
</tr>
<tr>
<td>Responsiveness</td>
<td>19</td>
<td>4.09</td>
<td>3.72</td>
<td>-0.37</td>
<td>3.977</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>20</td>
<td>4.15</td>
<td>3.27</td>
<td>-0.88</td>
<td>10.598</td>
<td>.000</td>
</tr>
</tbody>
</table>

When we analyze results of research shown in Table 2, which are based on answers about expectations and perceptions of characteristics of service quality in primary healthcare public institutions, visibly suggests that expectations are considerably high. Average values of expectations considered through notions range between 4.09 and 4.84. The majority of examinees have the highest expectations regarding cleanliness and tidiness of medical equipment and instruments (variable 4 from the questionnaire) followed by the wish to feel secure and “in good hands” during examinations (variable 15). Furthermore, when we observe real satisfaction, average marks range from extremely low 2.90 (it refers to speed of providing a service) to 4.02 (refers to tidiness and cleanliness of the staff).

Based on ratings of expectations and perception, a gap has been calculated and it represents a very good indicator of the overall quality of services in primary health care in Sibenik. All 20 variables have a negative gap which means that perceptions are lower than expectations and the quality of services in primary healthcare institutions is not satisfactory. These results lead to conclusion that there is definitely the need to improve quality of services that institutions of primary healthcare in the city of Sibenik provide to their patients and specifically the speed of providing the mentioned services since the greatest gap (-1.59) is recorded for this variable. We should also emphasise variable 1 from the questionnaire which related to the modernity of
equipment in primary healthcare institutions and which also had a relatively high gap (1.53). Examinees are most satisfied with working hours of institutions (variable 19) but this result cannot be considered as satisfactory since this question also reveals higher expectations than actual satisfaction. The results of Paired-Samples t test showed that for examinees there is a statistically significant difference between expected and perceived assessment for all analysed characteristics of services in primary health care in Sibenik.

5. CONCLUSION AND DISCUSSION
Empirical research has concluded that the level of overall satisfaction of users of primary healthcare services in Sibenik is not satisfactory since the average rate of satisfaction is 3.33. Furthermore, it has been determined that there is statistically considerable dissatisfaction of users with the overall service quality regarding frequency in service usage. The examinees who use services often rated the quality with the lowest average of 3.10.

It has been defined that there is statistically significant difference between examinees` expectation and their satisfaction with received medical services and that expectations are statistically higher than realized satisfaction which, again, leads to conclusion that quality of medical services in primary healthcare institutions in Sibenik is not satisfactory and that enough effort has not been made in order to increase patients` contentment.

When it comes to satisfaction with specific elements of medical services, it has been concluded that the examinees are least pleased with the duration of time necessary to have physical check-ups and with insufficiently modern medical equipment. We should definitely emphasize that the research has recorded the way in which the examinees had the highest expectations from tangible elements of medical services whereas in similar studies conducted in banking or tourism sector the participants had the lowest expectations from tangible dimension. This may be explained with a well known fact that cleanliness and tidiness are generally associated with good health.

The results cannot be generalized on all primary health care services since the research was primarily oriented towards services provided in general practice clinics excluding in this way dental practices, emergency services, occupational services and gynaecological clinics which all have unmistakable importance in the selection of primary healthcare system.

Ultimately, it can be concluded that this research should be conducted in regular periodical intervals in the future in order to reach a relevant judgement about trends in quality of services in primary healthcare institutions in Sibenik and its influence on patient satisfaction.

Despite the fact that in contemporary scientific literature in the field of quality there is strong emphasis on crucial importance of users` demands as the main criterion of quality, these demands should not be based solely on the patient perspective. Consequently, future studies should include perceptions of employees in primary healthcare institutions allowing them to be compared with attitudes of patients which would certainly help identify differences.

LITERATURE


25.
STOCK MARKET TRADING ANALYSIS BEFORE WORLD FINANCIAL CRISES AND NOWADAYS: ZAGREB STOCK EXCHANGE CASE

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ABSTRACT

In 2013, Croatia became a member of the European Union but it is still considered as a part of emerging and developing markets. Croatian stock market is known as Zagreb Stock Exchange (ZSE). It is an electronic market where stocks and bonds are traded since 1991. Among numerous economic indicators, general stock market situation also shows positive or negative trends and/or movements in the country. This paper will present two way analysis: CROBEX (main ZSE index) movement and daily turnover movement in period between 2007 and 2015. It will also be shown which corporations are market leaders according to the trading volume in past ten (10) years. The main objective of this paper is to provide general information on ZSE condition before global crises and nowadays with purpose to encourage worldwide readers to use this paper as a basic tool to acquaint themselves with the situation on stock market trading in Croatia. Data used for the analysis will be taken out from the historic data at Zagreb Stock Exchange website which represents fully open access archive. Important note regarding this work is that it shouldn't be taken as an initiative to buy or sell securities – the only purpose is to make a review of ZSE trading before the world crises to date.

Keywords: Croatian Stock Market, CROBEX, Securities trading, World financial crises, Zagreb Stock Exchange

1. INTRODUCTION

The capital market in Croatia stands as a developing and emerging market. Capital market participants in the Republic of Croatia are:

- investors (in financial instruments),
- intermediaries (investment firms, credit institutions, etc.),
- issuers of securities and other financial instruments,
- Zagreb Stock Exchange (market and multilateral trading facility operator),
- Central Depository and Clearing Company (depository of dematerialized securities, register and ownership, clearing and settlement system) (Croatian Financial Services Supervisory Agency 2015).

Zagreb Stock Exchange (ZSE) is a central place of securities trading in the Republic of Croatia and it was founded on the initiative of twenty five (25) initial members - brokerage companies (Zagreb Stock Exchange 2015). Stocks and bonds are traded there since 1991, shortly after the declaration of Croatian independence. Most common indicators of general condition at any stock market are stock exchange indices.
Main official ZSE stock index is called CROBEX, calculated since September the 1st 1997, consisting of twenty five (25) stock issuers - mainly based on the criterion of free float market capitalization (Limun.hr 2015). The paper represents a short review of daily regular turnover amount in period of eight years (2007 to 2015), as well as CROBEX movement in the same period. Represented data are taken from the ZSE archive on their official website.

2. ZSE - REGULAR TURNOVER 2007-2015

In this analysis, daily turnover or in other words trading volume will refer to the sum of all traded stocks turnover in each trading day for an observed period. Each stock turnover is calculated as multiplication of daily average stock price and number of traded stocks. Analysis starts in 2007, just few months before the worst global financial crises since Great Depression of the 1930s (Yale Global Online 2015) has started. Figure 1 represents all collected data of ZSE trading volume in mentioned period.

Beginning of the 2007 shows regular turnover rising as foreign and domestic investors started to find this type of investment much more attractive than for example savings in bank, which is not only being considered as most common and safest type of investment but also mostly recommended by financial advisors (Berg & Green 2012, p.22). Higher risk level, closely connected with investing on the stock market, also includes possibility of higher profit realization.
Higher turnover in that period occurred as a result of the higher demand and this will be shown later in the paper. In late 2007 and early 2008, when world financial crisis has already started, the positive trend ends yet higher trading volumes are still visible. By the end of 2009 trading volumes were practically constantly decreasing to stagnation at very low level. Stagnation is visible up to 2015 with a few extreme and rare exceptions. Opposite of the period of trading volume growth in this period trading was accompanied by an increase of offer or in other words "selling out" which will also be shown later in the paper.

3. CROBEX – MAIN ZSE STOCK PRICE INDEX

Stock market indices use base period (set value) and are merely a weighted or unweighted arithmetic mean of group of stocks (Teweles & Bradely 1998, p. 380). Main ZSE stock index is called CROBEX and described as follows:

- price index, dividends are not accounted for calculation
- selection criteria: more than 80% trading days
- consisting of 25 issuers
- weighted on free float market capitalization (maximum weight 10%)
- revised semi-annually
- base value 1000 (Zagreb Stock Exchange 2015).

Free float market capitalization is defined as that proportion of total shares issued by the company that is ready to be available on the market for trading (Bhat 2008, p.118). Proportion of total shares that is not ready to be available on the market is usually in the possession of the company management, state institutions, majority owners or strategic partners etc. If the security meets all necessary index requirements it is considered to be one among best representatives that will serve as an indicator of the general trends on the market – in this specific situation, stock prices situation and pricing trends on ZSE.

3.1. CROBEX movement 2007-2015

Considering the fact that higher trading volume can be achieved both as a result of a large demand as well as a result of a large offer and lower trading volume can be achieved both as a result of a low demand as well as a result of a small offer, main ZSE index analysis will serve as an indicator which one of just mentioned situations has happened in which period. CROBEX movement is shown in Figure 2 and data presented describe the same period that is covered with trading volume movement in previous chapter.
As ZSE trading volume increased at the beginning of 2007, CROBEX is also showing the same positive trend. That would actually mean that the demand overpowered the offer at that time of higher turnovers. Although the high trading volumes continued to hold until beginning of 2009, stock prices started their rapid drop at the beginning of 2008, pulling CROBEX back to low values. That would mean just the opposite – in 2008 higher turnovers were achieved because large offer overpowered low demand. People started to lose money on their investments, so they started to resort to safer ways of keeping their money and different types of investments. Massively they began to sell shares causing both turnover and CROBEX movement negative trend at first, then long term stagnation which is lasting until 2015, with a difference that CROBEX stagnation logically shows less extreme exceptions. Since stock market index represents relevant indication of general market situation, extreme turnover and extreme price volatility of some shares will never have significant influence on its value change. Figure 2 also shows that world financial crises had such a big impact on the Croatian stock market that the last visible value of CROBEX is much closer to its initial or base value then to its all time high value, at the time of this paper.

4. TOP TRADED COMPANIES ON ZSE
It is proved in previous chapters that world financial crises has left deep scars on the Croatian stock market, and small turnovers in past six years have caused almost complete lack of liquidity of a large number of listed shares. However, some companies have managed to maintain solid interest of private and institutional investors and speculators, who are considered to be less of investors and more of market liquidity providers. This section will present top traded companies on ZSE and their share price change in past ten years (in Croatian currency kuna – HRK). Table 1 shows top ten companies according to the achieved total turnover in period of 2005-2015.
<table>
<thead>
<tr>
<th>Issuer/Company Name</th>
<th>Turnover in HRK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hrvatski Telekom d.d.</td>
<td>9.994.345.518</td>
</tr>
<tr>
<td>INA-Industrija nafte d.d.</td>
<td>6.113.017.991</td>
</tr>
<tr>
<td>Adris grupa d.d.</td>
<td>5.514.948.568</td>
</tr>
<tr>
<td>Pliva d.d.</td>
<td>4.742.184.915</td>
</tr>
<tr>
<td>Atlantska plovidba d.d.</td>
<td>4.669.244.334</td>
</tr>
<tr>
<td>Ericsson Nikola Tesla d.d.</td>
<td>3.900.771.801</td>
</tr>
<tr>
<td>Dalekovod d.d.</td>
<td>2.881.137.064</td>
</tr>
<tr>
<td>Institut IGH d.d.</td>
<td>2.869.198.395</td>
</tr>
<tr>
<td>Podravka d.d.</td>
<td>2.753.612.033</td>
</tr>
<tr>
<td>Ingra d.d.</td>
<td>2.166.777.690</td>
</tr>
</tbody>
</table>

Table 1. – Top 10 stocks on ZSE, according to the total trading volume in period of 01-01-2005 to 31-12-2014

Source: ZSE Archive; Interpretation: Author

1. By far most traded company on ZSE is Hrvatski Telekom d.d. It is a leading telecommunication services provider in Croatia, a joint stock company in the majority ownership of CMobil B.V. which is 100% owned by T-Mobile Global Holding Nr. 2 GmbH - which is 100% owned by Deutsche Telekom AG (Hrvatski Telekom 2015). Total turnover in observed period of ten years was almost ten billion HRK – with emphasize on the fact that initial public offer (IPO) was at the end of 2007.

2. Runner up is Croatian leader in oil business and medium-sized European oil company INA-Industrija nafte d.d., having MOL Plc. and the Republic of Croatia as its biggest shareholders (INA-Industrija nafte 2015). In period of ten years (2005-2015) total turnover amounts to little above than six billion HRK - with emphasize on the fact that (IPO) was at the end of 2006.

3. In third place is Adris grupa d.d., that operates twenty companies in two strategic business units: tobacco industry and tourism, plus becoming a regional insurance industry leader in 2014 by acquiring Croatia osiguranje – biggest Croatian insurance company (Adris grupa 2015). This company share has achieved around five and a half billion HRK total turnover in period 2005-2015.

The rest of the list belongs to companies from pharmacy, shipping transport, telecommunication, construction and food sector. Share prices of each mentioned company in the Table 1, back in 2005 and then at the end of 2014 are shown in Table 2.
Table 2. – Share Prices of top 10 stocks on ZSE, according to the total trading volume in period of 01-01-2005 to 31-12-2014

Source: www.mojedionice.com; Interpretation: Author

Disregarding the fact that some of the companies have not been listed on ZSE yet when observed period started, further disregarding the fact that some of them were split (stock split) at one moment (Ingra d.d. for example), it is visible that some of the mentioned shares have not suffered irreparable damage in period of past ten years. Still, all time high values are also presented because in period between 2005 and beginning of the world financial crises, Croatian stock market almost continuously grew – like most other world markets at that time. Real consequences of the crises can only be visible if nowadays prices are compared to ATH values, or at least ATH values have been taken into consideration. Construction sector has suffered the worst consequences in this specific case with three representatives: Dalekovod, Institut IGH and Ingra.

5. CONCLUSION
Croatian stock market, like all other world markets, has suffered real damage after the world financial crises. Further analysis of other European, world developed and emerging markets as well as detailed comparison of all mentioned should be done to conclude whether recovery time on ZSE is already late or normally delayed. Small turnovers are still ZSE reality and long term market growth is still not possible. Croatian economy does not represent good foundation or solid support to the stock market – it is not realistic to expect construction sector, for example, to recover if bankruptcy threats to most of biggest Croatian construction companies. On the other hand, there are more than few examples of the companies that operate well and make profit, still their share price is not even near ATH values. So it is lack of the good economy condition on the one hand (to support recovery of struggling companies) and lack of private and institutional investors on the other (to support companies that operate well) that inhibits long term return of the over passed higher trading volumes on ZSE. Without constant higher turnovers supported by the strong demand it is not likely to happen CROBEX will get close to its all time high.
LITERATURE
12. www.mojedionice.com (All Time High values accessed on 9 March 2015)
COMPARISON OF DETERMINANTS OF EXPORT COMPETITIVENESS OF CROATIA IN RELATION TO CHOSEN COUNTRIES IN THE ENVIRONMENT

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ABSTRACT
This paper analyses facts connected to the export-competitiveness of Croatia in context of chosen countries in the environment, to evaluate the relative aspect of Croatian production aiming on export. The countries for comparison are chosen by key of experience in socialistic, planned economy and relatively late access to the European Union. In the analysis data is used from the period before the crisis which began in 2008, on incoming foreign investments, size of labour cost, movement of productivity of labour-force and importance of European Union market in the structure of export. By size of incoming foreign investments and especially by size of labour cost and growth of productivity rate and their correlation, Croatia is among the chosen countries in the most unfavourable position to realize growth of production meant for export. Decrease of share of export to developed markets of European Union countries from the year 2000 until now witness on the inadequate export-structure and on its increasing mismatch wit import demand of EU countries, opposite to the scenario favourable for Croatia.

Keywords: competitiveness, foreign direct investments, exports

1. INTRODUCTION
One country’ competitiveness can be looked at as its position in the international market in comparison to the position of other countries with a similar grade of economic development. The state and national conditions are important factor for international competitiveness. Michael Porter discloses four attributes of a national economy which influence the creation of competitiveness of the country and companies acting within: factorial attribute, attribute of demand, strategy and structure of competition and supporting and connected industry. (Grgic, Bilas, Franc, 2010, p. 90). The process of economic development influences the changes of intensity of influence of the single growth factor.

With regard to the importance of the single growth factors Porter recognizes three groups of countries. The first group comprehends countries that compete with labour force and natural resources, so their companies compete with low prices and generally sell primary products and low-tech products. These countries are depending on import of higher technologies and belong to underdeveloped countries. The second group of countries are middle developed countries which are characterized by a higher grade of investment efficiency, and as such they are selling products of middle developed technology. The third group of countries bases its growth on innovations and their companies compete with high technologies, new and unique
products. We are talking about high developed countries which are dominated by the service sector, developed scientific-investigative work and global orientation, and with higher salaries than in the two other groups of countries (Grgic, Bilas, Franc, 2010, p. 91). In the past 50 years important changes concerning the importance of factors of economic development took place. While 50 years ago competition was based on product development to achieve competitive advantage, today it is of prime importance to understand the market position for increasing competitiveness and market share on international markets, so we speak about collaborative and adaptive advantage. New factors of competitiveness are flexibility, integration, co-ordination and innovations. The world economic forum united these two indexes to the index of global competitiveness and defined competitiveness as aggregation of institutions, factors and politics which determine the grade of productivity of a country.

2. BASIC CHARACTERISTICS OF INTERNATIONAL COMPETITIVENESS OF CROATIAN ECONOMY

If we would rank the columns that make the global index of competitiveness, we would see that the most unfavourable places are taken in this order by: efficiency of labour market, efficiency of market of goods, institutions, business sophistication, development of financial market and macroeconomic environment. Concluding based only on the ranking of columns of competitiveness that make the index of global competitiveness of the World economic forum, Croatia is at most marked by being part of the first group of countries which are orientated on factors and build their competitiveness on institutional framework, infrastructure, macroeconomic stability healthcare and basic education, and partially in the second group , group of medium developed countries which build growth on higher efficiency of investments and taking technology of more developed countries. For analysing it is interesting to take a look also the most problematic factors for doing business in Croatia, given by the forum. Within 15 most problematic factors the first five in the ranking are in this order: inefficient state bureaucracy, corruption, political instability, tax rates and restrictive regulation of labour market. (http://reports.weforum.org/global-competitiveness-2014-2015/31.1.2015)

3. COMPARATIVE ANALYSIS OF FOREIGN-TRADE FLOW OF SELECTED COUNTRIES IN THE ENVIRONMENT

Summarized one can state that the basic condition for increasing export is competitiveness on international markets, and the structure of production for export aligned with the demand on international market (Kersan – Skabić, 2005, p. 82). For the sake of a comparative analysis of export competitiveness of Croatian economy countries are selected in the environment which went or are going to a transition phase like Croatia, except the war and war damages: Bulgaria, Czech Republic, Hungary, Romania, Slovakia and Slovenia. The observed countries generally export more than half of their export to countries in the European Union, that means to the market of developed countries. The analysis of their export-structure will show that Hungary has the biggest share of capital-intensive technological products in its export, while Croatia leads in labour-intensive products and low-technology products according to OECD classification. (Hatzichronoglou, 1997, p. 6).

From the data on size of imports, exports, their growth rates in the five-year period from 2003 to 2008, the size of the balance of exchange of goods and balance of current transaction account in table 1. we can see that, except Hungary and Czech Republic, all countries have a deficit in exchange of goods, and Croatia takes the third place by deficit of exchange of goods. Higher deficit of exchange of goods have Poland, 16,65 and Romania, 18,34. But taking into consideration that the deficit of exchange of goods in this countries is taking
“only” 13,86% (Poland) and 54,65% (Romania) of the total export, while the Croatian deficit of exchange of goods exceeds total export by more than a billion EUR, the situation of Croatian exchange of goods is by far the worst. At the same time Croatia is the only country with a coverage ratio of import by export less than 50%. The second worse position as per coverage rate import by export share Romania and Bulgaria with about 64%. According to the share of deficit of balance of current transactions in overall GDP, Croatia with 9,4 % is ranked third, behind Bulgaria (25,4%) and Romania (12,2%). The best ranks concerning this criteria are taken by Czech Republic (3,1%), Poland (5,4%) and Slovenia (5,5%) and Slovakia (6,6%). Croatia meanwhile registers the lowest export growth-rate, 11,92% in the five year period from 2003 to 2008. A somewhat higher growth rate record Slovenia (12,06%) and Hungary (13,86%) while Slovakia with 19,98% registers the highest export growth-rate. For the sake of rightful interpretation, this data has to be completed with the data that also by the growth of import Croatia takes the lowest rank with 10,46%, which talks about the general “slowing” of Croatian economy. A somewhat higher import growth-rate is recorded for Hungary with 12,14% and Slovenia with 13,72%, while the other countries register from 15% to 21% import-growth. Here definitely the most unfavourable position is taken by Romania, where the growth rate of import I by 5 percentage points higher than the export-rate.

Table 1: Indicators of exchange of goods in Croatia and selected countries in the environment in 2008, in billions EUR (Source: Wiener Institut für Internationale Wirtschaftsvergleiche (WIIW), Handbook of Statistics 2009, II Structural Indicators, Table II/1.13, Croatia: Main Economic Indicators, str. 63, 65, 69, 75, 77, 79, 81 i 86)

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<tbody>
<tr>
<td>Bulgaria</td>
<td>15,2</td>
<td>23,8</td>
<td>-8,6</td>
<td>-25,4</td>
<td>18,04</td>
<td>21,34</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>98,82</td>
<td>94,67</td>
<td>4,15</td>
<td>-3,1</td>
<td>18,2</td>
<td>15,98</td>
</tr>
<tr>
<td>Hungary</td>
<td>72,26</td>
<td>72,16</td>
<td>0,1</td>
<td>-8,7</td>
<td>13,86</td>
<td>12,14</td>
</tr>
<tr>
<td>Poland</td>
<td>120,15</td>
<td>136,8</td>
<td>-16,65</td>
<td>-5,4</td>
<td>17,48</td>
<td>18,42</td>
</tr>
<tr>
<td>Romania</td>
<td>33,56</td>
<td>51,9</td>
<td>-18,34</td>
<td>-12,2</td>
<td>16,56</td>
<td>21,7</td>
</tr>
<tr>
<td>Slovak Republic</td>
<td>47,72</td>
<td>48,43</td>
<td>-0,71</td>
<td>-6,6</td>
<td>19,98</td>
<td>19,98</td>
</tr>
<tr>
<td>Slovenia</td>
<td>20,03</td>
<td>22,66</td>
<td>-2,63</td>
<td>-5,5</td>
<td>12,06</td>
<td>13,72</td>
</tr>
<tr>
<td>Croatia</td>
<td>9,74</td>
<td>20,61</td>
<td>-10,87</td>
<td>-9,4</td>
<td>11,92</td>
<td>10,46</td>
</tr>
</tbody>
</table>

For the sake of this analysis we will limit to the absolute amount of direct foreign investments. As is visible from picture 1, international investors in the relevant period were attracted most by Hungary, whose incoming investments had accelerated growth until 2007. Croatia entered significant investments only in 2004, while in other years the amounts are on the level of investments in Slovakia. Less foreign investments than Croatia and Slovakia received only Slovenia, while all other countries record significantly higher income of investments than Croatia, even ten times the amount.

Beside the stated facts connected to the size of incoming foreign investments, it is important to take also the structure of the industries into consideration that registered most investments. The biggest share of direct foreign investments was in the banking industry, in connection with privatisation, rehabilitation and sales of banks, and telecommunication, connected with Deutsche Telekom becoming a shareholder, and pharmaceutical industry. After receiving direct foreign investments, these industries did not have significant impact on the increase of competitive competence of the exporting sector. The main reason is the lack of influence direct foreign investments on the export potential, type of industries that received investments: we are talking about so called local, internationally not tradable sectors, by this thinking of telecommunication and banking sector. In pharmaceutical industry there was acquisition of existing companies or acquisition of shares of existing companies, with undisturbed continuing of business, so that it did not come to new production, income or employment. The motive of the investor was hidden in taking market position and existing business and technology. Positive experience with foreign direct investment can be shown on the example of consolidating the banking sector, which manifested in improving quality and stability. The mentioned three sectors where receiving 62,1% of all direct foreign investments. The remainder is spread over many other industries. In internationally tradable sectors we lose the influence of foreign currency exchange rate on level of prices and production cost, that is why some authors consider the overvalued kuna partially reason for such structure of incoming of foreign investments, where non-production industries dominate, without export potential (Majic, 2012, p. 128)

4. COMPARATIVE ANALYSIS OF BASIC INDICATORS OF EXPORT COMPETITIVNESS OF CROATIA AND SELECTED COUNTRIES

For comparative analysis of export competitiveness of Croatian economy and the economy of selected countries the following indicators are used: productivity of labour, level of wages and importance of market of developed countries.
4.1. Productivity of labour

Productivity of labour is the indicator of the level of GDP per one employee. Growth of productivity of labour can be reached by growth of GDP by same level of employment, growth of GDB faster than growth of employment or decrease of employment and same GDP. In case of Croatia we can talk about decreasing employment at same level of (Kersan – Skabic, 2005, p. 92), which lead to undeserved optimistic picture of growth of employment in some periods in the early nineties. Growth of employment was reached by laying off workers. The same thing happened with countries in transition, which we compare with Croatia, but only at the begin of transition, later growth of employment followed.


Data from picture 2 will show that Slovakia, Czech Republic, Hungary and Poland show high growth-rates of employment. Croatia records in the contemplated period lowest average rates of all other contemplated countries, without major oscillations, which some countries record (Hungary, Slovakia, Slovenia) in 2008, showing negative values. The highest growth-rate Croatia records in 2005, 8%, when growth is higher only in two countries: Bulgaria and Hungary. After 2005 the growth rate settles at about 2%. Romania and Bulgaria as youngest members of the EU within the selected countries record relatively high productivity growth rates, multiply exceeding the growth rates in Croatia, except in year 2005.

4.2. Wages

From the data on development of gross salaries in the manufacturing industry in the period 2005 – 2008 in picture 3, we see that Croatia is with respect to these criteria similar to the most developed countries or countries which record by far higher rates of productivity growth, Slovenia and Czech Republic.

As per size of monthly gross salary multiply surpasses Rumania and Bulgaria, which, on the other hand, record multiple growth rates of productivity.
For example, in 2007 the average salary in Croatia of 863 EUR exceeds four times the average salary in Bulgaria, and more than two times the average salary in Romania. As low labour cost is one of the motives of foreign investors to invest in countries in transition, as generally for start production, one can conclude that by these criteria, Croatia has low competitiveness.

Looking at the size of total labour cost (picture 4) in 2008, this relation is even higher. With average 1.126 EUR labour cost Croatia is only somewhat lower than Czech Republic with 1.250 EUR, the second of the selected countries.
4.3. Significance of EU market for export of selected countries in the environment

From all selected countries Croatia records the lowest share of export to EU countries in total export, especially to EU-15, old members, except Bulgaria in 2000 (picture 5 and 6). Comparing 2000 and 2008, almost all countries decreased the share of export to EU countries, but only in the case of Croatia we can speak about a significant decrease, which can be explained by the renewal of so called “soft markets” of former Yugoslavia. So Croatian export to EU decreased from 69,5% in 2000 to 61 % in 2008. The decrease of Croatia to EU-15 countries, old EU members, amounts in more than 10. Somewhat less decrease of share of export to EU countries records Hungary, from 83,6% in 2000 to 78% in 2008, no here we are talking about a country which is, after Slovakia and the Czech Republic, the third country as per share of export to the EU. The best positioned countries in that respect, Slovakia and the Czech Republic, show high convergence of export structure and demand of EU, realizing 85% (Czech Republic) and 85,3% (Slovakia) of its export to EU countries. From the structure of total export to EU and other countries, we see the increase of share of export of Croatia to other countries from 30,6 % in 2000 to 39,1 % in 2008, whereas other countries mark countries of ex- Yugoslavia and Russia.

Picture 5: Significance of EU markets for Croatian export and selected countries in 2000 in % of total export (Source: Wiener Institut für Internationale Wirtschaftsvergleiche (WIIW), Handbook of Statistics, II.7 Manufacturing Industry, Table II/7.2, p. 231-241)

We can conclude that Croatia is in a phase of redirecting to soft markets of Ex-Yugoslavia, where it is easier to place Croatian products, and Russia, instead of the expected scenario of increased export to developed markets of the European Union, respectively we can speak on returning to the position before 1992. Liberalization of trade through joining the World Trade Organisation and bilateral contracts did not realize the wanted effects for Croatian exporters.
5. CONCLUSIVE CONSIDERATION

Looking according to the index of global competitiveness of the World Economic Forum, Croatia is marked a member of a group of countries directed by factors, which base their competitiveness on institutional framework, infrastructure, economic stability, healthcare and basic education, rather than medium developed countries which are aiming on realizing effectiveness and which base competitiveness on a system of high level education, efficient markets of goods and labour, developed financial markets, technological facilities and market–size. Croatia is significantly lacking behind in respect of sophisticated business and innovation, which are base of competitiveness of developed countries. Amongst the selected group of countries in the environment, Croatia is on high third place regarding labour-cost, and on second place, behind Slovenia, by size of gross-salary. Looking at growth rates of labour productivity, Croatia is amongst a group of three countries with the most unfavourable growth of productivity, not taking into consideration 2008, the year of recession when Croatia’s position improved, as result of strong effect of recession on the majority of selected countries in the environment, than on Croatia. By size of inflow of foreign investments, and especially by size of labour-cost and growth-rates of productivity and their correlation, Croatia is amongst the selected countries in the environment in the most unfavourable positions as far realization of growth of production for export is concerned. Decrease of share of export to developed markets of countries that are members of the European Union from 2000 until today witness an inadequate structure of export, respectively of growing miss-match with the import demand of EU countries, opposite to the scenario which would be favourable for Croatia. This fact is especially unfavourable, given that Croatia, expect ship-building, leads in export of labour-intensive products (textile industry), and resource-intensive products (mineral-oil and grease), instead of favourable capital-intensive products. At this place it is important to add that ship-building itself generates high import due to lack of fitted components, respectively un-developed supporting industry. Growth of share of export to countries outside the EU shows that Croatia returns to the position before 1992, respectively again directs to so-called soft markets of Ex-Yugoslavia.
and Russia. Movement of size and structure of export of the Republic of Croatia from independence until now shows that the economic policy in this part is not successfully established according to the challenges of transition and liberation of trade. Joining the contracts of free-trade and World Trade Organisation did not result in the expected respective increase of export and improvement of its structure but rather in increase of import due to growth of domestic consumption and increase of competition for the sector of domestic manufacturers which are anyway not strong enough.

LITERATURE

Treatise

Articles

Reports
1. Wiener Institut für Internationale Wirtschaftsvergleiche (WIIW), Handbook of Statistics 2009
POSSIBLE IMPACT OF G20 ON THE RESOLUTION OF THE FINANCIAL CRISIS

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ABSTRACT
This paper will present the history of the Group of Twenty (G20), and analyze the goals, main determinants and challenges facing the Group. Furthermore, by analyzing the role of the Financial Stability Board, the paper will try to explain the causes and consequences of the financial crisis, and how it unfolded. The role of the G20 in resolving the financial crisis is analyzed in detail, followed by a description of the BRICS countries and the new economic order. The paper does not strive to put forward concrete solutions or discuss academic proposals on how to improve G20 activities. Nevertheless, the paper will present a systematic analysis of key deficiencies in the system's operations, and thus contribute to the ongoing discussion of the G20's role in the world.

Keywords: G20, financial crisis, BRICS, Bretton Woods, new economic order

1. INTRODUCTION
Twenty major world economies have gathered into the Group of Twenty and the primary goal of this group is to ensure strong and sustainable growth all over the world. Twenty finance ministers and central bank governors (19 national economies and the EU) openly discuss problems concerning global economic stability. The G20 started in Berlin in 1999 as a meeting of finance ministers and central bank governors and now the group consists of eight member states of the G8 group (USA, Japan, Germany, France, the United Kingdom, Italy, Canada and Russia), Australia, ten large emerging markets (China, India, Brazil, Indonesia, Mexico, Korea, Turkey, Saudi Arabia, South Africa and Argentina) and the European Union. The G20 Summit was established in November of 2008 at the beginning of the global financial crisis and involved nineteen countries and the EU. The G20 Summit has become an important platform for global economic governance, international coordination of policies, and, most importantly, the reform of the international monetary system. The G20 members account for 85 percent of the global wealth.
One of the important items on the G20 agenda is regulation of financial markets. Mike Callaghan, from the Institute for International Policy in Sidney, also agrees that this group is more than a phrase in resolving problems. He points out that in 2008 there was a general psychosis for the fear that the crisis might turn into the Great Depression of the 1930-ies, and the G20 summit in London in 2009 prevented this from happening. The Financial Stability Board (FSB) also plays an important role. The board consists of regulators from the G20 group of major world economies and it was established at the Pittsburgh summit in 2009. Foundation of this board is considered to be one of the most important moves of the G20.
With the aim of resolving the financial crisis, FSB suggested that the major world banks should have a particular bond portfolio to protect themselves in case of collapse and to avoid the need to be saved by tax payers. It should be pointed out that many challenges lie ahead of the G20 as the G20 mechanism still remains an informal institution with the problem of balancing among the national interests of member states.

This paper aims to achieve two goals: firstly, to present and explain the complex structure and action of the involved states in the decision-making process by providing a definition of the term and a historical overview; and secondly, to analyze the key situation that determines not only the long-term importance of the G20 for the stability of global economy, but also its legitimacy as an international economic regime, and that is the 2008 global recession. Therefore, the synthesis of the analysis presented in this paper is that the G20, due to its non-institutional form which allows, for example, the BRICS countries to oppose the interests of western countries, is not and cannot become in the near future what it is expected to be: a functional international economic regime. The aim of the paper is not to put forward what “should” be done to make the G20 more functional, but to show the situation “as it is”, pointing to the key limitations of the organization itself. Based on the quantitative processing of both source and data, dependent variable of this research is the structure of the G20 activity. Independent variable used to determine non-functionality of the G20 is the “2008 global recession”.

2. DEVELOPMENT OF THE G20
The name of so-called “Group” as the name used for a forum of the most powerful countries of the world was first used in the early 1970-ies, when Bretton Woods was brought to an end by the US abandoning the gold standard. Therefore, “the 1973 oil shock forced them (the most powerful countries of the Western world) to organize themselves in an informal way and to establish a forum where they would agree on a common strategy. Thus the Group of five most influential countries of the Western world was formed, namely, the USA, the United Kingdom, France, Germany and Japan, known as the G5. Institutions such as Bretton-Woods, MMF and World Bank as well as other formal international economic organizations, such as the World Trade Organization, became instruments for implementation of economic policies based on decisions made within an informal group of the most powerful countries of the world” (Popovic, 2014: 138).

The G20 was established in 1999 and it started its activity as a forum of finance ministers and central bank governors whose goal was to meet once a year, typically in late autumn, to discuss international economic issues. With the onset of the global economic crisis in 2008, the G20 evolved into the premier leaders’ forum for international economic cooperation. Annual meetings of finance ministers and central bank governors continue to take place. The G20 has no permanent secretariat and much of the preparation for the summit is completed by G20 leaders’ personal representatives, known as Sherpas. Sherpas maintain contact with each other over the course of the year to discuss agenda items for the summit and coordinate the work of the G20 (http://www.international.gc.ca/g20/history-histore.aspx?lang=eng).

According to Kirton (2014), finance ministers and central bank governors from 19 important countries of the world and the European Union (EU) gathered in Berlin on December 15-16, 1999 to initiate the G20 meeting. The G20 was started by two finance ministers, Paul Martin from Canada and Lawrence Summers from the US. According to Kirton (2014), the G20 was established in response to the Asian financial crisis which broke out in Thailand in June 1997. The crisis spread to Indonesia and Korea and by the end of the year it affected Russia, Brazil and the USA. In addition, the hedge fund Long Term Capital Management collapsed. The first meeting of the G20 members was held on November 14-15, 2008, in Washington, DC.
One of the most important events in this meeting was that France suggested a summit, *G20 Leaders Summit on Financial Markets and the World Economy*. The G20 should provide financial stability through financial regulations, ensure economic growth and work on trade liberalization and development. Working groups and expert groups are established when needed to support the work of leaders, finance ministers, central bank governors and Sherpas. Currently there are following working groups and expert groups (http://www.international.gc.ca/g20/history-histoire.aspx?lang=eng).

Working groups:
- Framework for Strong, Sustainable and Balanced Growth
- Anti-Corruption (established at the G20 Toronto Summit)
- Development (established at the G20 Toronto Summit)
- International Monetary Fund Quota and Governance Reform

Expert groups
- Financial Safety Nets
- Financial Inclusion
- Energy

The G20’s work is supported by international organizations such as the World Bank, the IMF, the Organization for Economic Co-operation and Development, the International Labor Organization, the World Trade Organization and the United Nations. The G20 calls upon experts from these institutions for technical advice and it also works with the Financial Stability Board to develop financial stability and eliminate weaknesses. They also monitor regulatory and supervisory policies.

(http://www.international.gc.ca/g20/history-histoire.aspx?lang=eng)

### Table 1: The G20 member states (www.g20.org)

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<th>Argentina</th>
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<td>Australia</td>
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The idea of international financial organizations agreeing on relations and trade dates back to the 18th century and liberal tradition of Europe in the Age of Enlightenment. Theoretical development of the concept of “international organization” reached its peak in the 20th century: in the first half under the influence of theoretical thinking of David Mitrany. His functional approach advocated the theory that countries should cooperate in the fields outside of the state policy: trade, telecommunications, transport, banking system, etc. To regulate these relations, it was necessary to establish international organizations as bodies that would regulate relations between states (Mitrany, 1975). In the second half of the 20th century, the idea of liberal institutionalism, i.e. the idea that relations between states are fully regulated in agreement with international organizations reached its peak, with foundation of various international organizations, from the United Nations and Bretton Woods institutions, to military organizations such as NATO (Keohane, 1988; Stein, 2008).
2.1. Goals and determinants of the G20
The G20 aims to achieve various goals, but the main goal that is always emphasized at the group meetings is to improve global economic governance. By means of information technologies, globalization has created better connections and interdependence on a financial plan, leaving the countries weak in this context (Held et al., 1999; Beck, 2004). Further, stronger coordination of international economic policy and resolving the unemployment issues and trade imbalance through structural reforms is emphasized. Tiberghien and Xu (2013) claim that it is important to accelerate the reforms of the international financial system and to achieve this, international community must insist on the development of international reserve currencies. One of the goals is a better international supervision of the financial framework, which includes stronger supervision of hedge funds, over-the-counter derivatives and credit rating agencies. It is of particular importance to give the voting right to developing countries and emerging countries in international financial institutions. Important work is done on further trade and investment liberalization. Global poverty should be reduced and more development goals and support for education and social security improvement in developing countries should be offered. The gap between developed and undeveloped economies should be reduced and the G20 mechanisms should encourage international trade and investment. Economic growth should be encouraged as well as job creation in developed economies. The G20 should protect mutual interests of nations with different economic structures. There should be more responsibility, and countries having problems with fiscal deficit should carry out structural reforms. Their macro-economic policy should be focused on encouraging long-term assets and human capital, and not on speculative investments on securities market and unsustainable, excessive spending, as pointed out by Tiberghien and Xu (2013).

2.2. Challenges ahead of the G20
Financial crisis was somehow resolved through global recovery. However, the G20 is still facing the general feeling of economic insecurity and solidarity. European debt crisis creates additional insecurity and the trade protectionism threat continues to affect global economy. According to various analysts, the G20 policy lacks authority. Further, there is a conflict between “big” and “small” countries and an inadequate process of the monetary system reform. One of the greatest challenges ahead of the G20 is to deal with imbalance in the international monetary system and the global economic governance mechanisms. Different countries should participate in finding solutions to the problem, thus promoting the win-win approach. Big countries sometimes put their interests in front of “small” countries, which often leads to a conflict (Tiberghien and Xu, 2013). It should be mentioned that Payne (2014) thinks that the G20 today is like a big vessel waiting to be filled up. The author compares the G20 with a car parked in a car park and between meetings it is waiting for a new driver to take over the wheel. According to Payne (2014), the key challenge ahead of the G20 is the underlying lack of continuity (2014).

3. FINANCIAL CRISIS
According to Mlikotic (2010), roots of the global financial crisis should be sought in negative effects resulting from an array of neoliberal reforms that have dominated economic policy of the western countries since the 80-ies of the past century. Particular emphasis is put on the responsibility of the USA and unsustainable development concept based on spending and economy of “financialization”. Another problem was deregulation of the financial market favoring introduction of an array of risky innovations, reduction in the rate of progressive tax
burden and policy of low interest rates. These are some of the most frequently mentioned misjudgments in the US economic policy, Mlikotic said (2010).

Global economic crisis was caused by poor financial regulation in the United States, global macro-economic imbalance and high deficits in current accounts in the USA and some other advanced industrial countries. There was poor American financial regulation, poorly organized risk management, and excessive risk taking is emphasized as a particular problem (Guerrieri, 2010). Mlikotic (2010) points out that many sophisticated financial mechanisms were developed while seeking profit, i.e. new “products” were launched, such as futures or forwards contracts. An array of innovations was introduced (futures, swaps, options, etc.), and development of futures market was most strongly encouraged through securities purchased by using borrowed funds or at a margin (the share that buyer must pay in cash when buying securities, whereas broker keeps a deposited security as a collateral), Mlikotic points out (2010). In this way speculators could (by means of a financial leverage) with a particular amount (depending on the margin) acquire securities of a multiple value. Tett (2009) was among the few ones who predicted crisis. Her opinion about the three wrong assumptions on which the 21st century finances were based should be emphasized. Firstly, there was an opinion that modern capital markets had became so advanced that it would always be possible to sell the risk further.

Secondly, investors relied on risk assessment agencies, which proved to be totally unreliable. Thirdly, and most importantly, it was believed that the process of slicing and dicing of debt made financial system more stable. It (allegedly) distributed the default risk among millions of investors and the system became more capable of amortization of potential shocks. Blog PositiveMoney.org explains that UK banks created too much money. Every time a bank makes a loan, new money is created. In just seven years, they doubled the amount of money and debt in economy. Banks used this money to push up house prices and speculate on financial markets. Trillion pounds that banks created in the period 2000-2007 went to residential property (31%), commercial real estate (20 %), financial sector (32%), and just 8% went to businesses outside the financial sector. A further 8% went into personal loans. Lending large sums of money into the property market pushes up the price of houses along with the level of personal debt. Interest has to be paid on all the loans that banks make, and with the debt rising quicker than incomes, eventually some people became unable to keep up with repayments. They stopped repaying their loans, and banks found themselves in danger of going bankrupt.

3.1. The course of the crisis
Description of the course of the financial crisis can begin with house prices on the US market reaching the peak in 2006, which was followed by a sharp fall, leading to a collapse of subprime mortgage market in August 2007. After that default risk started to spread on other mortgage classes and problems in trade between banks (Mlikotic, 2010). Further fall of 17% in house prices followed, and, by the second half of 2008, 40% of subprime mortgages from 2006 became troublesome, the author adds. During 2008 the crisis spread very quickly in the USA, Japan and Europe and caught the global financial market. The first serious warning was the bankruptcy of Bear Stearns, the fifth largest investment bank in the USA. Dramatic proportions take place in September 2008 when heavy credit contraction occurs, along with dropping of value on stock exchanges all over the world and collapse of some of the largest financial institutions (Mlikotic, 2010).

On Friday, March 13, Bear Stearns faced a shocking discovery – they ran out of money. Lenders and clients started to withdraw money, worried about poor financial situation, and the
company suddenly had less than 3 billion dollar on accounts, which was insufficient to restart business. This caused loss of trust in credit ability of partners, fall in securities prices, and in September and October interest rates on interbank loans and state securities reached the highest levels in the past few decades. At the end of September and during October, further loss of investor trust combined with declining results of the real sector resulted in new panic selling of securities all over the world. The fall in the securities value at the global level only in the first ten days of October was more than $10,000 billion, and total fall recorded in 2008 amounted to 40%. The Us financial institutions could not avoid bankruptcy - Fannie Mae and Freddie Mac24 (“government-sponsored enterprises”, having half of the mortgage loans in the USA, worth $5,000 billion), then American International Group (AIG; one of the largest insurance companies in the world, with assets worth more than $1,000 billion), Citigroup, Lehman Brothers, Washington Mutual, etc. (Mlikotic, 2010).

Not long after that, Lehman Brothers and Washington Mutual also declared bankruptcy – the first being the largest company in the American history, the second being the largest company that had ever failed. These events marked the end of independent investment banking in the US, i.e. institutions that profited the most from deregulation of the financial system in the past decades. Japanese and European financial systems were not immune to crisis either, so only in December of 2007 the European Central Bank loaned $500 billion to European merchant banks. Various other financial institutions also could not avoid bankruptcy: Dutch-Belgian Fortis, French-Belgian Dexia, British Bradford & Bingley and Northern Rock, German Hypo Real Estate, Dutch ING and Aegon, and others (Mlikotic, 2010). Benic (2012) emphasizes that the crisis caused problems also in the European banking sector. For example, Germany had to save its Hypo Real Estate holding company; the United Kingdom recapitalized big banks such as Royal Bank of Scotland, HBOS, Barclays; France had to deal with BNP and Societe Generale, and Holland with ING. All this led to a rise in interest rates and reduced offer of favorable loans, i.e. money, which directly affects reduced personal spending and investments. Benic emphasizes that selling, particularly of goods purchased with borrowed funds (cars), sharply fell. There was a growth of inventory and share prices were falling down. To reduce this effect, the Federal Reserve (the US Central Bank), followed by the European Central Bank and seven leading banks, reduced the interest rate to 3.25% already toward the end of 2008, Benic continues (2012).

We should bear in mind that the crisis did not emerge in 2007 or 2008. It was created through decades of great changes in the share of work and capital, for the benefit of capital, in the GDP, i.e. national revenue (whereas the share of work in developed countries toward the end of the 1960-ies and at the beginning of the 1970-ies was around 75%, at the beginning of the 21st century in Europe it was 65-68%), according to Benic (2012). This resulted in disproportion between supply and demand which was resolved with loans for years without a crisis, until living above one’s means simply was not possible any more, Benic concludes (2012). Toward the end of 2008 the global financial system was facing collapse and it had to be saved by means of further government interventions. In an effort to restart the financial system, developed countries provided government guarantees covering savings accounts and interbank loans, recapitalized banks with public funds and took over risky investments, approved fiscal reliefs, influenced the interest rates and undertook a set of other measures amounting to approximately $4,000 billion, Mlikotic concludes (2010). For information about the extent to which the housing loan market had effect on the crisis outbreak, see: (IMF, 2012).
3.2. Consequences of the crisis

The financial sector crisis and disturbances it caused in loan supply, with increased savings rates, resulted in reduced investments in fixed capital and consumer goods, which explains the sharp fall in the global demand. Consequently, global industrial production recorded a 13% decline in the period from September 2008 to March 2009. There were signs of demand stabilization, particularly of consumer goods, as results of the government measures and reduced inflation rates, but the level of savings remained high. Unemployment became the greatest problem, at least in the US (Mlikotic, 2010). Obadić (2011) emphasizes that financial crisis brought about reduction in aggregate demand, leading to a reduced production volume (primarily due to reduced demand for export products and FDI inflow), thus leading to reduced demand for labor. The author emphasizes that the crisis spread all over the world, deteriorating economies, reducing business capacities and leaving millions of people without a job. The global GDP in 2009 fell by 1.1% (Figure 5), and this fall in developed countries and the EU amounted to 3.5%.

It should be noted, according to the author, that many workers entered various forms of vulnerable employment groups; the number of decent jobs decreased, insecure employment rate increased as well as the number of low-wage workers. As the crisis was deepening, government incentive measures started to slow down the decline in economic activities and reduced the initial impact in the circumstances of job destruction at global level, Obadić concludes (2011). Mlikotic (2010) further emphasizes that the US economy was mostly affected by the fall in the property market and collapse of the financial system, which again caused worry, after initial signs of recovery. The government’s anti-recession package worth almost $800 billion did not achieve the expected results, state revenues decreased due to a lower level of economic activity, and the President Barack Obama’s ambitious healthcare reform plan should also be mentioned here as well as the planned increase in military expenses, leading the state finances to serious problems – the federal deficit increased to 12% of GDP. It is also noted that Europe and East Asia, having the same problems, but of a lesser volume, were also facing difficulties arising from stagnation of international trade. Developing countries, to which crisis spread through the financial system and trade, were facing various problems. Large exporters like China and India were trying to compensate for a fall in exports by encouraging home spending, with the government leading the way, whereas most of the remaining developing countries were mostly affected by a decrease in foreign investments and exports of industrial products. Mlikotic (2010) concludes that the fall in economic activities, the fall in demand and growth of unemployment have led to a general decrease in inflation rates, but fears of deflation, it seems, will not come true, Mlikotic concludes (2010).

4. THE ROLE OF THE G20 IN THE RESOLUTION OF THE FINANCIAL CRISIS

The G20 summits made great progress in stopping the financial crisis in the world and results achieved are based on the four key roles played by the G20. First, a higher level of international coordination and cooperation was achieved among the major world economies. In this way it was possible to achieve a coordinated response to the global financial crisis, fight against trade protectionism, coordinate fiscal incentives and achieve a gradual fall in fiscal deficits in developed economies. Second, the role of the IMF was particularly pronounced in assessing the influence of particular policies on other states and work was done on the reform of the governance over international financial institutions. The G20 played an important role in the shifting of voting rights (The IMF and the World Bank) to developing countries to increase the level of their participation in accordance with their GDP growth.
Third, the G20 played a very important role in strengthening the international financial supervision and establishment of the Financial Stability Board. Fourth, particular attention was given to the reform of the management fees for management of financial institutions, and also Basel Capital Accord III (Basel III) was established. The G20 summit was also established as a regulatory mechanism (Tiberghien & Hongcai, 2013).

The second G20 summit was held in London on April 1-2, 2009, and this summit is considered to be a turning point in resolution of the global financial crisis. It is interesting that the US agreed to include French and German proposals as well as requests for radical strengthening of the role of financial regulation and control in global financial system in the declaration. The Chinese request was to significantly increase the influence of those countries that had made progress in both economic and financial aspect. The G20 made the following conclusions: We face the greatest challenge to the world economy in modern times; a crisis which has deepened since we last met, which affects lives of women, men and children in every country, and which all countries must join together to resolve. A global crisis requires a global solution. We start from the belief that prosperity is indivisible; that growth, to be sustained, has to be shared; and that our global plan for recovery must have at its heart the needs and jobs of hard-working families, not just in developed countries, but also in emerging markets and the poorest countries of the world too; and must reflect the interests, not just of today’s population, but of future generations too. We believe that the only sure foundation for sustainable globalization and rising prosperity for all is an open world economy based on market principles, effective regulation, and strong global institutions. We have today therefore pledged to do whatever is necessary! By acting together to fulfill these pledges we will bring the world economy out of recession.

The agreement we have reached today, to treble resources available to the IMF to $750 billion, to support a new SDR allocation of $250 billion, to support at least $100 billion of additional lending by the MDBs, to ensure $250 billion of support for trade finance, and to use the additional resources from agreed IMF gold sales for concessional finance for the poorest countries, constitute an additional $1.1 trillion program of support to restore credit, growth and jobs in the world economy.

4.1. Restoring growth and jobs
The G20 made the following conclusions: We are undertaking an unprecedented and concerted fiscal expansion, which will save or create millions of jobs which would otherwise have been destroyed, and that will, by the end of next year, amount to $5 trillion, raise output by 4 per cent, and accelerate the transition to a green economy. We are committed to deliver the scale of sustained fiscal effort necessary to restore growth. Our central banks have also taken exceptional action. Interest rates have been cut aggressively in most countries, and our central banks have pledged to maintain expansionary policies for as long as needed and to use the full range of monetary policy instruments, consistent with price stability.

Our actions to restore growth cannot be effective until we restore domestic lending and international capital flows. We have provided significant and comprehensive support to our banking systems to provide liquidity, recapitalize financial institutions, and address decisively the problem of impaired assets. We are committed to take all necessary actions to restore the normal flow of credit through the financial system and ensure the soundness of systemically important institutions, implementing our policies in line with the agreed G20 framework for restoring lending and repairing the financial sector. Taken together, these actions will constitute the largest fiscal and monetary stimulus and the most comprehensive support program for the financial sector in modern times. Acting together strengthens the impact and
the exceptional policy actions announced so far must be implemented without delay. Today, we have further agreed over $1 trillion of additional resources for the world economy through our international financial institutions and trade finance. We are confident that the actions we have agreed today, and our unshakeable commitment to work together to restore growth and jobs, while preserving long-term fiscal sustainability, will accelerate the return to trend growth. We commit today to taking whatever action is necessary to secure that outcome, and we call on the IMF to assess regularly the actions taken and the global actions required. We are resolved to ensure long-term fiscal sustainability and price stability and will put in place credible exit strategies from the measures that need to be taken now to support the financial sector and restore global demand. We are convinced that by implementing our agreed policies we will limit the longer-term costs to our economies, thereby reducing the scale of the fiscal consolidation necessary over the longer term. We will conduct all our economic policies cooperatively and responsibly with regard to the impact on other countries and will refrain from competitive devaluation of our currencies and promote a stable and well-functioning international monetary system. We will support, now and in the future, to candid, even-handed, and independent IMF surveillance of our economies and financial sectors, of the impact of our policies on others, and of risks facing the global economy.

4.2. Strengthening financial supervision

Major failures in the financial sector and in financial regulation and supervision were fundamental causes of the crisis. Confidence will not be restored until we rebuild trust in our financial system. We will take action to build a stronger, more globally consistent, supervisory and regulatory framework for the future financial sector, which will support sustainable global growth and serve the needs of business and citizens. We each agree to ensure our domestic regulatory systems are strong. But we also agree to establish the much greater consistency and systematic cooperation between countries, and the framework of internationally agreed high standards that a global financial system requires. Strengthened regulation and supervision must promote:

a.) propriety, integrity and transparency;

b.) guard against risk across the financial system;

c.) dampen rather than amplify the financial and economic cycle;

d.) Reduce reliance on inappropriately risky sources of financing; and discourage excessive risk-taking.

e.) Regulators and supervisors must protect consumers and investors, support market discipline, avoid adverse impacts on other countries, reduce the scope for regulatory arbitrage, support competition and dynamism, and keep pace with innovation in the marketplace.

To this end we are implementing the Action Plan agreed at our last meeting, as set out in the attached progress report. We have today also issued a Declaration, Strengthening the Financial System. In particular we agree: 1. to establish a new Financial Stability Board (FSB) with a strengthened mandate, as a successor to the Financial Stability Forum (FSF), including all G20 countries, FSF members, Spain, and the European Commission; 2. that the FSB should collaborate with the IMF to provide early warning of macroeconomic and financial risks and the actions needed to address them; 3. to reshape our regulatory systems so that our authorities are able to identify and take account of macro-prudential risks; 4. to extend regulation and oversight to all systemically important financial institutions,
instruments and markets. This will include, for the first time, systemically important hedge funds; 5. to endorse and implement the FSF’s tough new principles on pay and compensation and to support sustainable compensation schemes and the corporate social responsibility of all firms; 6. to take action, once recovery is assured, to improve the quality, quantity, and international consistency of capital in the banking system. In future, regulation must prevent excessive leverage and require buffers of resources to be built up in good times; 7. to take action against non-cooperative jurisdictions, including tax havens. We stand ready to deploy sanctions to protect our public finances and financial systems. The era of banking secrecy is over. We note that the OECD has today published a list of countries assessed by the Global Forum against the international standard for exchange of tax information; 8. to call on the accounting standard setters to work urgently with supervisors and regulators to improve standards on valuation and provisioning and achieve a single set of high-quality global accounting standards; and; 9. to extend regulatory oversight and registration to Credit Rating Agencies to ensure they meet the international code of good practice, particularly to prevent unacceptable conflicts of interest.

We instruct our Finance Ministers to complete the implementation of these decisions in line with the timetable set out in the Action Plan. We have asked the FSB and the IMF to monitor progress, working with the Financial Action Taskforce and other relevant bodies.

4.3. Strengthening global financial institutions

Emerging markets and developing countries, which have been the engine of recent world growth, are also now facing challenges which are adding to the current downturn in the global economy. It is imperative for global confidence and economic recovery that capital continues to flow to them. This will require a substantial strengthening of the international financial institutions, particularly the IMF. We have therefore agreed today to make available an additional $850 billion of resources through the global financial institutions to support growth in emerging market and developing countries by helping to finance counter-cyclical spending, bank recapitalization, infrastructure, trade finance, balance of payments support, debt rollover, and social support. To this end: 1. we have agreed to increase the resources available to the IMF through immediate financing from members of $250 billion, subsequently incorporated into an expanded and more flexible New Arrangements to Borrow, increased by up to $500 billion, and to consider market borrowing if necessary; 2. we support a substantial increase in lending of at least $100 billion by the Multilateral Development Banks (MDBs), including to low income countries, and ensure that all MDBs, including have the appropriate capital.

It is essential that these resources can be used effectively and flexibly to support growth. We welcome in this respect the progress made by the IMF with its new Flexible Credit Line (FCL) and its reformed lending and conditionality framework which will enable the IMF to ensure that its facilities address effectively the underlying causes of countries’ balance of payments financing needs, particularly the withdrawal of external capital flows to the banking and corporate sectors. We support Mexico’s decision to seek an FCL arrangement. We have agreed to support a general SDR allocation which will inject $250 billion into the world economy and increase global liquidity, and urgent ratification of the Fourth Amendment.

In order for our financial institutions to help manage the crisis and prevent future crises we must strengthen their longer term relevance, effectiveness and legitimacy. So alongside the significant increase in resources agreed today we are determined to reform and modernize the international financial institutions to ensure they can assist members and shareholders effectively in the new challenges they face. We will reform their mandates, scope and governance to reflect changes in the world economy and the new challenges of globalization, and that emerging and developing economies, including the poorest, must have greater voice
and representation. This must be accompanied by action to increase the credibility and accountability of the institutions through better strategic oversight and decision making. To this end: 1. we commit to implementing the package of IMF quota and voice reforms agreed in April 2008 and call on the IMF to complete the next review of quotas by January 2011; 2. we agree that, alongside this, consideration should be given to greater involvement of the Fund’s Governors in providing strategic direction to the IMF and increasing its accountability; 3. we commit to implementing the World Bank reforms agreed in October 2008. We look forward to further recommendations, at the next meetings, on voice and representation reforms on an accelerated timescale, to be agreed by the 2010 Spring Meetings; 4. we agree that the heads and senior leadership of the international financial institutions should be appointed through an open, transparent, and merit-based selection process; 5. building on the current reviews of the IMF and World Bank we asked the Chairman, working with the G20 Finance Ministers, to consult widely in an inclusive process and report back to the next meeting with proposals for further reforms to improve the responsiveness and adaptability of the IFIs.

In addition to reforming our international financial institutions for the new challenges of globalization we agreed on the desirability of a new global consensus on the key values and principles that will promote sustainable economic activity. We support discussion on such a charter for sustainable economic activity with a view to further discussion at our next meeting. We take note of the work started in other fora in this regard and look forward to further discussion of this charter for sustainable economic activity.

4.4. New economic order

According to Nikolić (2010), from the Institute for Peace Studies, the goal of the BRICS and most of the G20 countries is to create a new world order based on being less US-centered, with more regulated financial sector, reduced use of the US dollar and a greater role of developing countries. The statement of Robert Zoellick, the World Bank president, drew attention. He invited all the world’s centers of power to put different geopolitical interests aside and work on strengthening of multilateralism whose significance was just accentuated by the global economic crisis. Nikolić (2010) explains that, owing to a strong growth of many developing countries, Zoellick envisages creation of a new global system where “the North” and “the South”, “the East” and “the West” are now directions of a compass and not determinants of economic destiny. The following question arises: Is it already possible to see an outline of a new multipolar, global financial (and to an extent also geopolitical) order? It should be emphasized that political, social, economic, cultural and religious diversity of the G20 and BRICS countries is a paradigm of the modern world, unlike relative homogeneity of the western world, painted through the G7. Nikolić (2010) says that it is encouraging that major emerging economies, since they intensely use globalization advantages, have strong interest in providing conditions in which transition toward the multipolar system will not be followed by financial instability or aggravated international trade, international capital and investment flows. Of particular importance is the economic relation between China and the US, which will face great challenges. Potential political and economic blockade of China, due to alleged currency manipulation, would drive China to great troubles, whereas negative effects for the US in form of growing interest rates and weakening of the dollar would be less pronounced, Nikolić concludes (2010).

Nikolić (2010) emphasizes that the most likely scenario is that the US would remain the leader, but in a multipolar world. The role of China would be significant due to its economic expansion and the EU would maintain a significant level of influence, also owing to the alliance with the US. Emerging economies such as the Indian, Brazilian and Russian economy
would slowly strengthen their role in the new order. Petrovic and Nikolic (2011) also add that global governing structure was defined in the post-war era under the dominant role of the US, through liberalism and support to multilateralism as well as the monetary system that gave developing countries a peripheral role in the process of creating international financial architecture, under pressure of great changes. The authors also claim that the US economic model has come into question and that the Chinese model of strong government influence on the economy is increasingly gaining on importance. The authors also point out, that, in addition to having positive effects, Chinese use of strong fiscal stimulations directed at Chinese companies, i.e. literally redirecting to the home market also implies growth of protectionism and creates risk of erosion of the world economic interdependence.

The 2007-2010 crisis, according to Petrovic and Nikolic (2011), only accelerated reconfiguration of the world financial order, which has been taking place since the end of the 20th century. It is indicative that the share of the processing industry in the US GDP in the 1970-ies was 24% and in 2010 it was only 11%, whereas financial sector or virtual economy doubled and reached as much as 8% of GDP just before the crisis, authors add. The share of the Euro-bonds has already exceeded the dollar bonds at the global level. However, this still does not indicate who could be a relative winner in financial reconfiguration. At the beginning of the 21st century financial power shifted toward the countries with non-convertible currencies (China, India, Russia and Brazil). Consequently, developing countries are emerging into markets that are desirable for investments. However, according to authors, the crisis strongly affected the reputation of the West, particularly the US, where the crisis started. Petrovic and Nikolic (2011) emphasize that the beginning of use of the ruble and the Yuan in mutual trade since the end of 2010 shows a symbolic and potentially historical event reflecting tectonic changes in the world economy and politics and it promises transformation of the global financial architecture. As developed countries are overloaded with debt, the time after the crisis will be challenging for them as it will require high fiscal transfers to service debts, whereas reprivatization of the banks that became state-owned also demands political effort. In a bad scenario these countries can slip into a long recession and the “convertible” currencies are the ones posing a threat to stability, according to authors.

The position of the dollar, which is still the currency in which two thirds of the global foreign exchange reserves are held, is in danger. Additional threats are bilateral and multilateral barter schemes. The question arises whether global financial system is shifting toward a polycentric configuration. One should bear in mind that it is not only the liquidity level or currency functionality that matters, where the dollar, euro, yen or pound still hold the primary position, but how stability and strength of economies, which are at the root of power of every currency, consequently lead to strengthening of the role of alternative currencies (Yuan, rupee, ruble...). Multitude of actors on the international scene might strengthen international system in the way that they will fill empty spaces in institutions established after 1945, but monetary system can also be fragmented and it can further disable instruments of international cooperation.

The current financial crisis, in absence of strong multilateral intervention, leads toward fragmented and non-functional international monetary system. Michael Maloney emphasizes that after the classic gold standard 1871–1914, gold exchange standard 1918–1940, Bretton-Woods system 1944–1971 and practically dollar monetary standard 1971–2007, currently we have a new global monetary system, which rapidly shows its outlines, Petrovic and Nikolic conclude (2011). The crisis is present at two levels: the first level is inability of powerful countries within the G 20 (West vs. BRICS) to establish equilibrium in the balance of payments, but also in various interests (for example, China is not developing its own consumer market, but it is flooding the world market with its products and its exports.
continuously exceed imports) (Helleiner, 1994; Nye, 2011; Madhur, 2012). The second level that certainly should be mentioned is that the G20 is not only burdened with finding consensus among economic powers, but also with how to overcome vertical imbalance in the proportion of the world poverty (almost 60%) and the wealthiest people (about 5%), (Goldsmith, 2001; Wade, 2001; Held, 2004).

4.5. The role of the BRIC countries in the resolution of the crisis

In 2012, in Los Cabos, Mexico, the BRICS countries (Brazil, Russia, India, China and South Africa) showed their readiness to resolve the financial crisis by promising high contributions to the global crisis fund of the International Monetary Fund in order to support its efforts to raise $456 billion in the circumstances of debt crisis escalation in the eurozone. Their contribution is based on providing support in amount of $95.5 billion for the IMF’s crisis fund. China offered $43 billion, whereas Brazil, Russia, India and Mexico offered $10 billion each. It is interesting that Chinese contribution is lower only than the Japanese and German one, amounting to $60 and 54.7 billion, respectively. What was most interesting in Los Cabos is the fact that the BRICS countries warned about the need for changes in the IMF as it had been dominated by economic powers from Europe and the US for years, and they were not willing to provide their own contribution to the crisis fund.

It is particularly important that contributions will be paid only after all agreed reforms are implemented, including the comprehensive reform of voting rights and quotas. The BRICS countries were very clear and exact and they particularly cautioned that the crisis in the Eurozone might have far reaching consequences for their economies. The BRICS countries took one more step toward strengthening of economic power of their community as they agreed on the procedure for establishing a mutual fund of foreign exchange reserves and capital in their own development bank, Kuzmin says (2013) in Rossijskaja gazeta. The BRICS countries meeting opening the leader summit of that community was held at the beginning of September 2013 in St. Petersburg during the G20 summit. Kuzmin (2013) says that the decision about the amount of funds available in the mutual fund ($100 billion) was made already at the BRICS summit in Durban, South Africa. On this occasion the leaders of the group achieved a preliminary agreement on the share of each country in the mutual fund. China participates with $41 billion, Brazil, India and Russia with $18 billion each, and South Africa participates with $5 billion, says Kuzmin (2013).

The BRICS members reached an agreement to perform draft swaps when needed. “Each member will be able to obtain the US dollars for its national currency, i.e. the Central bank of the Russian Federation should, at certain conditions (determined interest rate and repayment terms) provide dollars for the country requiring them. Mutual fund is created to be able to react fast to the changes in foreign exchange markets”, explained the Russian officer, and his words were repeated by Kuzmin (2013) in Rossijskaja gazeta. This idea of leaders of developing countries about establishing some kind of their own World Bank and IMF was created based on growing criticism of these countries and general capital outflow from emerging markets. For example, for the G20 summit the IMF experts prepared a report saying that growth of the world economy in the near future will be mostly encouraged by the US, Kuzmin says (2013). Experts and economic analysts generally approve of the idea for establishing a mutual currency fund, but they also point out that its proportions are obviously insufficient to be used to solve great problems.

“This level of funding might be sufficient to mitigate short-term negative effects of capital outflow and to allow national regulatory institutions to react more efficiently. In this case there would be no such sharp fall in the value of the rupee and the real”, says analyst Vladimir
Lupenko, a partner in the FCG company. However, these reserves, according to his estimates, would not be sufficient to maintain currencies in the long-term period, Kuzmin says (2013). “These funds could be sufficient to reduce the pressure on national currencies during the campaign ‘quantitative easing’ which would obviously influence sudden strengthening of the dollar. But it should not be forgotten that this is not only about the volume of reserves, but also about that the US Federal Reserve should “step out” of the stimulation program”. In the event of wrong estimates, control over such a complex and unique process could be lost”, Vladimir Lupenko points out.

According to Prange (2014), the bank will be seated in Shanghai, unlike the World Bank whose management is in Washington. The new institution will try to act as counterbalance to the International Monetary Fund and the World Bank. “In the World Bank the US has the right of veto, whereas all shareholders among the BRICS countries are equal”, says Guido Mantega, the Brazilian finance minister. In addition, the World Bank is traditionally managed by an American, and the IMF by a European. The BRICS countries organized this in a different way – the first president of the bank will come from India, and representatives of the five founding countries will rotate in this function every five years, according to Prange (2014). In addition, an agreement was signed on CRA (Contingent Reserve Arrangement), IMF type fund. The purpose of this $100 billion currency fund is to increase financial stability of all member states. According to Prange, this institution provides an opportunity for the BRICS countries, which currently have the highest foreign exchange reserves in the world, to use their funds in a feasible way. She also points out that initial investments in the CRA differ from country to country. For example, China has provided $41 billion; India, Brazil and Russia 18 billion each; and South Africa $5 billion, which will affect the planned process of taking a loan, depending on the member state.

5. CONCLUSION

Seven years ago the global financial crisis hit the world. Company decline, unemployment growth rate and reduced production levels urgently required great efforts to find a way out of the crisis. In November 2008, the countries that account for around 90% of the world wealth gathered and thus the G20 was established. The G20 summits proved to be important in the sense that the G20 became an important platform for global economic governance and the reform of the international monetary system. Of particular importance is the establishment of the Financial Stability Board (FSB), which was officially founded in April 2009 in Pittsburgh as a successor of the Financial Stability Forum. What is important about the FSB is that its role is to eliminate the lack of transparency in the financial sector, spread regulatory mechanisms and supervise financial institutions, instruments and markets.

The G20 countries allowed for a fiscal stimulus that helped prevent the world economy from collapsing. Also, there are agreements about establishing a global infrastructural initiative. Employment growth has been another important issue. It was of greatest importance to build a financial sector that is resistant to various crises, and particular attention was given to measures taken to ensure fairness of the international monetary system. One of the goals of the G20 is to strengthen international economic institutions as a response to changes in the world economy and to facilitate trade. Nowadays the G20 is facing the dilemma whether to reintroduce a system where gold was used to measure the value of goods and services in order to rectify fiscal and monetary imbalance and to stop uncontrolled production of new dollars. Robert Zoellick, the World Bank president, asked to consider the option of introducing gold as a foundation or a reference point in relation to market expectations related to inflation, deflation and future exchange rate values. Another challenge that the G20 is facing is how to
maintain the group homogeneity as the BRICKS members have started “separating” from the G20, as they have formed alternative institutions to the World Bank and the IMF.

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OIL PRICES – ANALYSES OF ORIGINS AND IMPLICATIONS OF CURRENT DEVELOPMENT

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ABSTRACT

Oil prices slump that began in June 2014 led to decrease in the average monthly prices of oil by 60% and got lots of attention as oil is still integral part of world energy mix with many countries’ economies crucially dependent on import or export of this commodity. Fall of oil prices was surprising as it came during the period of multiple geopolitical tensions. As our article describes this was primarily caused by discrepancies between supply and demand on oil market. However we argue that market factors only created environment and provided first impetus but geopolitics inherently bound to this subject played its role in further development. We believe that Saudis decision that led to decline in oil prices was intended to help to fulfill multiple of its own goals as well as some of that of Saudis allies. With respect to EU we assume positive but differentiated impact of oil prices on economic development, with largest members benefiting less. We conclude that long run effects of current low oil prices will greatly depend on the way policymakers will be able to use low oil price environment.

Keywords: Energy markets, Geopolitics, Oil prices

1. INTRODUCTION

Average yearly oil prices have oscillated relatively stable around $100/bbl during last four years. This previously unimaginable level of oil prices resulted from a combination of several factors, starting with the weak dollar, growing share of costlier types of oil (oil sands, tight oil, deep-sea drilling) on overall production, political unrests, and growing Chinese energy demand. As most of these factors were present also in previous period a prime reason of such high oil prices seems to be the outbreak of geopolitical unrest known as the Arab Spring that followed the previous slump in oil prices in the wake of financial crisis. The revolutions in the MENA region destabilized several oil-producing countries and caused interruptions of commodity flows on world markets. The high oil price was additionally influenced by the FED’s quantitative easing undermining the value of US dollar aimed at supporting the fragile economic recovery.

Period of high oil prices was also joined by quickly rising reserves of recoverable oil, and therefore it might be surprising that oil companies did not use the this favorable environment to more pronounced increase of production and profits (the incremental supply originated largely from relatively smaller companies producing from unconventional resources). The answer to this question provide Economy and Levi (2014) who claim it was the consequence of oil markets structure, which is dominated by national oil companies as their goal is not the profit, but to ensure required revenue for the state budget. These companies are not incentivized to increase production during the period of high oil prices because they are able to deliver required funds at a lower volume of extraction, which further creates conditions for maintaining high oil prices. The incremental demand for oil pulled by Chinese thirst was therefore more and more covered by producers from NOPEC countries, which led to the
creation of conditions favorable for price war after the market began to shrink, when slowdown in Chinese demand and temporary improvement of the situation in the countries affected by the events of the Arab Spring created primary impetus for recognition of the changing trend on the oil market.

2. OIL PRICES DEVELOPMENT

After the slump in oil prices in 2009, OPEC eventually managed to reduce production and the price of commodity started to rise. The sharp increase in prices of this energy commodity was subsequently preceded by protests in MENA region that led to revolutions and destabilization of oil producing countries, which resulted into 32% growth of oil prices to yearly average of $104/bbl in 2011. Subsequently, in 2012 the basket of crude oil markers averaged on $105/bbl, which was again attributed to geopolitical factors in large extent - sanctions against Iran due to its nuclear program and growing violence in Syria, but also to more positive economic outlook of USA and EU. Yet, at that point increased US oil production reaching some 7 mil. bbl/d, representing so the highest level of production since 1992, was already recognized as a major factor. The most of the oil production growth originated from the shale and tight oil formations in North Dakota and Texas (Obadi, 2013). The combination of military conflicts in the Middle East, growing production in North America that overreached 10 mil. bbl/d, optimistic expectations about US economy but also technical outages of some refineries, uncertainty about American involvement in Syria and ongoing violence in multiple countries of MENA region resulted repeatedly into average price around $104/bbl in 2013. Moreover, conflict zones were joined by Ukraine at the end of 2013 after the outburst of protests known as Euromaidan which were followed by Crimea annexation and outbreak of violent conflict in eastern part of Ukraine in 2014. The world has also become aware of military activities of terroristic organization ISIS, which started to threaten the oil production in Iraq and Kurdistan, when they finally started to deliver raising volumes of oil onto the world markets. Chinese economy that represented the key determinant of oil demand in recent years has slowed down although combined with the positive news from USA and Japan basically it altogether did not result into any significant changes in oil prices over the first months of 2014 as USA kept increasing the oil production and after overtaking Russia and Saudi Arabia, becoming the world largest oil producer.

Despite all the listed geopolitical conflicts, graph 1 clearly suggests that since 2011 the oil price was significantly determined by the interaction of supply and demand. Between 2011-2014 the oil market recorded only two significant oil price drops while both were preceded by period of excess supply of oil in the market. The decline of average monthly oil prices by $17/bbl which occurred between January and June 2012 was accompanied by 2 mil. bbl/d oil oversupply. On the contrary, during subsequent period of high oil prices has demand outpaced supply by approximately 350 000 bbl/d. This again changed to excess supply in December 2013 and during the following twelve months average supply exceeded demand by 800 000 bbl/d on average during with highs of +1.43 mil. bbl/d in May 2014 and lows of 65 000 bbl/d in November 2014.
The explanation why the oil price fall began only in June as the oversupply already lasted for several months offers Berman (2015) who claims the primary impetus for oil prices to fall was the end of quantitative easing in the United States. In similar vein argues Pflüger (2015) who concluded, that despite all the theoretical considerations, the drop in oil prices can be simply explained by the combination of three factors: a sharp increase in oil production in the US and slower than expected growth of oil demand due to the slowdown of world economy, speculations on international stock markets and unfulfilled positive expectations that induced massive sale of long contracts, and cessation of quantitative easing in the US and the opposite policy within EU, which strengthened the US dollar and decreased the nominal prices of oil. The EIA (2015) prognosis expects continuing state of oil oversupply, which will lower only gradually resulting in prices increase. Although those should not exceed 80 USD/bbl, however this whole development is to a large extent depended on ongoing military conflicts in oil producing countries.

3. THE ROLE OF OPEC

After oil prices began to fall in mid-2014, in the wake of production overcapacity a great attention was drawn to the OPEC meeting in Vienna, which took place at the end of November 2014. Contrary to expectations OPEC did not change the production quotas, which remained at 30 million bbl/d and sent the oil prices to fall below $70/bbl, almost approaching the level of $40/bbl in January. This decision of OPEC was subject to multiple theories seeking to explain it.

Anyway, before any further analysis, it is necessary to emphasize that the decision to maintain production quotas at the level that even according to own OPECs estimates was larger than the demand for the cartel’s oil was not unanimous or easy, and was mainly supported by Saudi Arabia, which has sufficient foreign exchange reserves, greatest possibilities to limit the output and moreover – many reasons for such action.

Venezuela, along with Algeria, on the other side allegedly demanded 2 mil. bbl/d cut in production¹, however were not able to arrange such production decline by themselves so final decision was to keep quotas unchanged. It also should not be forgotten that prior the OPEC meeting there were unsuccessful negotiations with NOPEC countries. Those as we already suggested are responsible for supplying of ever growing share of market.

¹ During previous oil price slump in 2009 OPEC managed to agree on actual production decrease of 3 mil. bbl/d, 2 mil. bbl/d of which was pulled out of the market by Saudi Arabia.
This non-agreement resulted in oil prices below $50/bbl at the beginning of 2015. As original estimates of oil prices trough were in range $60-$70, it is questionable whether such deep fall was not more than OPEC (even Saudi Arabia) initially expected from this strategy, although it needs to be admitted Saudi Arabia has benefited from such development in several cases. Firstly, the fight for market become less competitive and OPEC can easier hold its market share. Since 2008 when the importance of US unconventional oil production started to be fully recognized has the output of USA risen by 47% (3,2 mil. bbl/d), which was reflected in lower need for imports – those decreased by 4,3 mil. bbl/d while the possibility of US oil exports has become a discussed topic. For OPEC this would mean not only loss of export market but also new competitor at their existing customers. This risk has been reduced by low oil prices since the cost profile of American oil production is undoubtedly much higher than that of Saudi Arabia and other generic OPEC members. Two largest plays (Eagle Ford and Barnett), where the significant share of production come from are profitable only with prices starting at $50-$60/bbl. Despite that, current prices have not automatically led to massive production cuts as multiple producers have reportedly hedged their production for several months in advance and at the same time many producers have taken lot of credit and therefore it can be assumed they are ready to continue with production in order repay their debts. When analyzing American market of unconventional oil production it needs to be noted there exists many different companies and therefore different cost curves, with respect to volume of taken credit and oil well profile. The information on drilling rigs usage which is taken as a primary real time indicator of oil production activity and renting of new production sites clearly suggests slowdown of drilling activities. Therefore after expiring of existing hedging contracts and under current low oil prices, a more rapid decline of oil production can be expected considering the characteristics of this type production when flow rates are diminishing in much faster pace. American producers were moreover hit by Saudis offering discount prices for American customers. However the fight for market cannot be seen only as OPEC vs. North America. As we already stated the decision not to reduce oil production was not welcomed unanimously by all the cartel’s members and even more, it did not solve the actual situation of oversupply which led to price war between OPEC members on Asian market (Reuters, 2015), indicating so existence of other frictions influencing current situation. In February OPEC (2015) report has already anticipated lowering production of NOPEC countries by 420 000 bbl/d and increase demand for oil produced by the cartel. According to IEA (2015), it should be Russia not USA that will suffer the most. Russia impacted by both low oil prices, western sanctions and weaker Rubble is predicted to lower oil output by 560 000 bbl/d by 2020 to 10,4 mil. bbl/d. On the other hand, unconventional oil production in US should after temporary slowdown continue growing in the same period reaching 14 mil. bbl/d in 2020. Such development would actually support the second narrative that tries to explain the reasons behind the OPECs decision not to reduce quotas and production. It simply claims that US collude with Saudi Arabia in order to weaken Russian position. This theory, despite its conspiracy nature can actually have at least partially sound foundations. Indeed, one has to realize that weaken Russian economic and military forces is in the interest of Saudi Arabia itself. However, it is not connected to current conflict in Ukraine but rather originates from the long term strategic battle to gain the dominance over Arab peninsula, where Russia repeatedly acted contrary to Saudi Arabia’s interest. The cases in the point are support of Iran in the field of energetic and military equipment or Russian support of Assad’s regime in the Syrian civil war. Saudi Arabia has actually tried to win over Russian support already in past with signing contract for supply of Russian arms. Fact, that the Russian arms are reportedly not compatible with majority of Saudi weapons supplied by is traditional western allies only emphasizes that arms itself were not the most important subject of that deal. The sale itself
has never realized though. Wikileaks documents claim it was due to Russian reluctance to spend its political leverage over USA (gained through supporting regime in Iran and blocking the sanctions against Syria) over pure economic benefit of arms deal. In 2013 Saudi Arabia repeatedly tried to purchase Russian weapon systems for $15 billion, supposedly under condition of Russia pulling back its support for al-Asad, but this contract has neither come into existence. The willingness of Saudi Arabia to bear the losses can really be related with its political goals (those are however shaped by its own interests, not only those of USA). Some analysts even stated that, power battle between Saudi Arabia and Iran in Persian Gulf might be the reason why Saudi Arabia accepts billion losses in oil revenues. Another aspect that cannot be forgotten in current geopolitical environment is losses that suffer ISIS, which used to earn $1 mil.-$2mil./d by selling oil on black market, and which has already in December 2014 aired its intention to conquer Saudi Arabia, after a minor armed skirmish on its borders. Apart from above mentioned pragmatic theories seeking to explain the steps of Saudi Arabia, another, more visionary one, attracted attention. According to Hinkley (2015) Saudi Arabia acts in this way because it realizes all the oil reserves cannot be extracted and current battle over market shares is interpreted as an effort to maximize the economic benefits with respect to future loss of value of oil. Basically this is an extension of concept of “stranded assets” developed by Carbon Tracker Initiative think tank, according to which the huge investments into fossil fuels will become worthless as they become redundant in the less fossil fuels dependent future world. After both USA and China confirmed their commitment to reduce greenhouse gases emissions last year and 2015’s Paris climate agreement looks more realistic the scenario of decreasing demand for oil is becoming more realistic. Under such scenario, keeping price low could be understood as an attempt to increase interfuel competition and alternative costs of renewable energy sources and an effort to optimize oil rent in the long run. Even if low oil prices might act as an enabler for prolongation of oil usage era, according to multiple observers it will not stop the momentum that RES is ridden on. The history of 1980s when oil prices drop brought to halt the initiatives aimed at increasing roles of RES will not repeat according to Mathews (2015), who argued that Chinese commitment to lower the air pollution in their cities and demand for energy security via increasing usage of indigenous renewable resources are moving forces that will prevent such development. We find it highly questionable, whether prolonged period of low oil prices would really not cause any distortion to that scenario. However we do not consider to be likely scenario as compared to 1986 and antishock of that time, a great difference exists nowadays. Then period of low oil prices that lasted over decade was caused by increased production of low cost conventional sources coming on stream in NOPEC countries in reaction to previous oil shocks and low demand for oil resulting from disintegration of Soviet Union. In the absence of further technological breakthrough such scenario can hardly be expected with respect to fact current oversupply was driven by unconventional sources and quickly exhaustible oil wells. Generally, return of higher oil prices is expected and only question is when it is going to happen and how high the prices will be - in other words market expectations are uncertain, which is not an ideal situation for changing the direction of energy policy. That is being oriented in still growing number of countries towards low carbon sources. Moreover IEA as well as many other institutions encourages countries to use current period of low oil prices to enforce measures aimed at lowering fossil fuels consumption via removing fossil fuels subsidies (worldwide reaching $550 billions, introducing carbon pricing schemes or additional taxation, that would not represents any major burden for customers and more importantly would support energy efficient behavior of citizens and incremental financial resources so collected could be directed in the energy related research.
The reasons of recent oil price development still remain ambiguous. We believe, that impetus in form of market factors, that struck the market – oversupply, lower demand, change in monetary policy of main economic powers or speculations on stock markets served as a prime mover for price change. Explanation of following oil price path however cannot omit geopolitical factors. We suppose, that Saudi Arabia follows the wide range of its own goals and oil price fall served her as an (expensive) ultimate tool for its fulfillment, while US concerns likely play less important part than is generally attributed by some western medias.

4. THE IMPLICATION OF LOW OIL PRICES FOR GLOBAL ECONOMY

Lower oil prices serve an instrument of wealth transfer from oil exporting to oil importing countries. Since income elasticity is undoubtedly greater on consumer side (as there are much more oil consumers than people earning from oil), lower oil prices should necessarily mean faster growth of global economy. Often cited estimate is that 10% oil price decline leads to 0.1-0.2% growth of economy, in current environment that would mean positive economic incremental growth of 0.5-1%. Although, according to IMF’s (2015) revision of economic outlook for 2015, this assumption will not be valid this time and positive aspects of lower oil prices will not have power to offset the impact of events that had make them happened. Economic growth in 2015 should reach 3.5%, which represents decline of 0.3% compared to previous prognosis. The reasons behind that are lower economic growth of China, Russia, EU, Japan and oil exporting countries, while only large economy where the growth was reassessed upwards is US.

Overall it can be said, that primary beneficiaries of low oil prices should be net importing countries and on the other side stand net oil exporters. According to Arezki – Blanchard (2014) the impacts are not homogenous and in each group significant differences exist. Essentially, there exist three channels, through which oil prices influence countries importing oil: by increasing the real income of consumers, lowering production costs of goods and through inflation rate. Magnitude of these impacts logically varies across different countries with respect to its economic profile, infrastructure and importance of oil in economy. For instance, positive influence for US is likely to be smaller than one for Europe or Japan, as US is also large producer and lower oil prices will be reflected in lower revenues of oil producing companies and tightening the labor market in this sector. On the contrary, the economy of India and China with their higher energy intensity profile will benefit more, as real terms of trade of this type of countries should improve. Lower oil prices will at the same decrease inflation, which can be an issue in the advanced economies, although developing countries suffering from high inflation and consequential high interest rates that are curbing economic growth can greatly benefit. Lower oil prices will also allow developing countries to remove some of existing subventions of fuels and through that lower the pressure on public deficit, therefore ease the access to international financial market, strengthening so the foundations for economic growth (for instance, India spent $41 billion in fuels and food subventions which represents 14% of governmental expenditures and 2.5% of GDP).

4.1. EU implications of low oil prices

Consequences for EU economy are not very clear so far. European Commission in its winter economic prognosis suppose that favorable combination of low oil prices and weakened EUR represents combination that will lead to growth of all the EU member countries first time since 2007. At the same time it stresses the risks of geopolitical development and threat of deflation influenced by low oil prices. On the other side we would like to remind that high energy costs were considered to be major threat to EU competitiveness in recent period so their decline can be anything but welcome. As table below illustrates the magnitude of oil
importance in European countries varies significantly. When we consider energy intensity, trade balance, volume of oil related trade in GDP and position of oil energy mix as a key indicators determining the importance of oil for economy, we found out that lower oil prices should mainly improve situation for Lithuania, Malta, Cyprus and Greece. On the other hand, economies of largest EU members United Kingdom, France and Germany as well as Austria are likely to be impacted in smaller range as oil plays less important role in their economies.

Another issue is influence of low oil prices on natural gas market especially strategy of Russian Federation. Current custom of indexing natural gas prices to those of oil will automatically lead to lowering natural gas prices which is confirmed by Russian ministry of economic development estimating 35% decline of prices of exported natural gas (from $341/tcm in 2014 to $222/tcm in 2015). Lower price will however inevitably lead to
increasing competitiveness of Russian gas on European market, therefore the volume of exported gas is estimated to jump from 146.6 bcm to 160 bcm, which will not compensate the prices decline and Gazprom would lose €14.3 billion in revenues. Current circumstances so create an environment suitable for reopening the negotiations on natural gas pricing and from the longer point of view also strengthen the position of natural gas in European energy mix via its higher competitiveness. However the question that must follow is the impact of such development on energy security, as higher market share of Gazprom on EU market would be integral part of such development.

4.2. Consequences of low oil prices for oil exporters
As we already stated, low oil prices are not good news especially for oil exporting countries dependent on related revenues. As was the case of importers, the consequences for individual economies are different based on the role of oil in their economies. Considering the geopolitical allocation of oil resources, one cannot find it surprising that dependency on oil prices is much higher in case of oil exporters than oil importers. For instance energy business is responsible for as much as 25% of GDP, 70% of exports and 50% of state revenues of Russian Federation. In Middle East the share of oil reaches as much as 22.5% GDP and even 63.6% for countries belonging into GCC group. In Africa the oil export stands for 40-50% of GDP in case of Gabon, Angola and Congo and 80% of GDP of Equatorial Guinea. The oil revenues also create 75% of governmental revenues in Angola, Congo and Equatorial Guinea. In Latin America oil contributes 30% resp. 46% revenues of public sector and 55% resp. 94% of exports in Ecuador and Venezuela (Arezki – Blanchard, 2014). These examples only highlight the magnitude of challenges faced by oil exporting countries. Since the outburst of oil prices decline many estimates of so called breakeven oil prices (prices of oil ensuring balanced budget for oil exporting countries).

Table 2: Basic characteristics of major oil exporters (EIA, SWFI, WSJ, Nationsonline.org)

<table>
<thead>
<tr>
<th>Countries</th>
<th>Net export (000' bbl/d)</th>
<th>„Breakeven“ oil price ($/bbl)</th>
<th>Sovereign fund (bil. USD)</th>
<th>Population (mil.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Saudi Arabia</td>
<td>8 733</td>
<td>106.0</td>
<td>762.5</td>
<td>21.1</td>
</tr>
<tr>
<td>Russia</td>
<td>7 249</td>
<td>98.0</td>
<td>181.8</td>
<td>143.1</td>
</tr>
<tr>
<td>UAE</td>
<td>2 743</td>
<td>77.3</td>
<td>1 078.5</td>
<td>8.3</td>
</tr>
<tr>
<td>Kuwait</td>
<td>2 345</td>
<td>54.0</td>
<td>548.0</td>
<td>3.3</td>
</tr>
<tr>
<td>Iraq</td>
<td>2 289</td>
<td>100.6</td>
<td>18.0</td>
<td>33.3</td>
</tr>
<tr>
<td>Nigeria</td>
<td>207</td>
<td>122.7</td>
<td>1.4</td>
<td>177.5</td>
</tr>
<tr>
<td>Venezuela</td>
<td>1 905</td>
<td>117.5</td>
<td>0.8</td>
<td>27.2</td>
</tr>
<tr>
<td>Qatar</td>
<td>1 847</td>
<td>60.0</td>
<td>256.0</td>
<td>1.8</td>
</tr>
<tr>
<td>Angola</td>
<td>1 756</td>
<td>n.a.</td>
<td>5.0</td>
<td>20.6</td>
</tr>
<tr>
<td>Canada</td>
<td>1 643</td>
<td>n.a.</td>
<td>391.9</td>
<td>35.0</td>
</tr>
</tbody>
</table>

These figures need to be read cautiously. The budget of each country is always based on certain assumptions, which are not unalterable and in case of exogenous shocks can government always take adapting measures, as was the case of most of the countries in the wake of Great recession in 2009. The same procedure is valid for oil exporting countries. and in many cases no severe cuts are needed, as national sovereign funds managing the past oil revenues offers them the comfort of gradual adaptation to changed conditions. As table 2 reflects, not all the countries have the same maneuvering space and those who are going to
suffer mostly are countries without largest population and smallest reserves – Venezuela and Nigeria. Their cases are even more critical as the oil related wealth distribution was reportedly not transparent, which can lead to struggle for power between fractions of ruling groups and this way even more spikes the civil unrests already happening in these countries. As was also pointed out by multiple observers changes can be expected in the “backyards” of countries suffering from lower oil incomes. Regimes and organizations supported by them could soon find themselves lacking the sponsorship as eventual persistence of low oil prices would demand prioritization of governmental policies. Current situation will therefore most likely impact regimes in central Asia supported by Russian Federation or those closely bound to it, Iranian support of Hezbollah movement and other Shiite allies will lower, as well as Venezuelan space to support its regional allies.

4.3. Future development of prices
Predictions of oil prices cover extremely wide range and will be essentially determined by the duration of current low oil prices. OPEC warned that low oil prices will lead companies to halt investments into development of new oil fields and future oil prices can jump as high as $200/bbl. The warning sign in this field is the volume of newly discovered reserves, which in 2014 were the lowest since 1995 even though exploration budgets were intact that year (on the other hand it needs to be said that after previous reserves additions from recent years the oil peak fears are not currently any issue). Citigroup, on the other hand claims that oil prices can fall to $20/bbl for a certain time during 2015 during the process of balancing. At the present time (spring, 2015) oil prices seems to stabilize and started to slowly rise due to combination of unstable situation in Libya, stock market speculations and optimizing of international oil flows.

Even if the elasticity of oil market is extremely small, current oil prices will certainly influence the demand and supply. According to OECD study, short run elasticity of demand (1-2 years) represents 0.02 and middle to long run 0.17. Juel (2015) estimated that this would translate into 0.75 mil. bbl/d growth of demand in short run and even 8 mil. bbl/d in the long run. At the same time, higher elasticity of supply (0.05 in short run and 0.2 in long run) would translate into 2.2 mil. bbl/d and 9.5 mil. bbl/d lower supply in short run respectively long run. This means that even in this hypothetical case where no other factor played any role the supply demand balance would be restored within 1-2 years bringing the price back to higher levels. Fair price nowadays is estimated to be around $80/bbl, with US being in the position of new swing producer since prices above $80/bbl would lead more shale producers to start drilling and push prices back.

5. CONCLUSION
Events that led fall of oil prices are still not fully explained and duration of their persistence and the path of its recovery is not clear. The OPEC reaction, that immediately preceded their fall emphasized that OPEC is increasingly heterogenic organization dominated by Saudi Arabia that is able to assert its specific goals. Without any doubts, the first impetus for oil prices drop resulted from the discrepancies between supply and demand on oil market. However, integral part of the oil price determinants are also geopolitical interests, and Saudis decision undoubtedly helped to fulfill multiple of its own goals as well as some of that of Saudis allies. Therefore, analysis of future development of oil prices cannot omit the geopolitical aspects. In the long run, critical issue that resonates more than oil price itself are implications of current development. On one side there are threats from inadequate investments and growth of tensions in oil producing countries that will repeatedly lead to oil shocks or complicates the transition towards low carbon sources. On the other, there exist
positive predictions that focus on benefits for countries importing oil, or sees current situation as an opportunity to launch carbon tax that would enable more effective solution of climate change issue. The final effects will surely depend on ability of politicians to seize the opportunities that low oil price environment created. This is especially true for EU, where oil prices determine also natural gas prices with all the related effects for energy security. So far it seems low oil prices would need to stay here for much longer period to bring some actual long run positive effects as current policy activity is focused more in different areas.

LITERATURE
THE EFFECTIVENESS FUNDS PROGRAM OF SCHOOL OPERATIONAL ASSISTANCE AT THE ELEMENTARY SCHOOL IN SUMBA BARAT DAYA DISTRICT OF NUSA TENGGARA TIMUR PROVINCE - INDONESIA

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ABSTRACT
The funds Program of School Operational Assistance at the elementary school is the policies adopted by the government of Indonesia to improve the accessibility and participation rate of primary education for the poor. Through this program, the government provides funding to schools elementary and junior high school that is willing to comply with the provisions stipulated in the terms of the program participants. The urgency of this program is to reduce the burden on the poor so that they earn adequate educational services and quality. Implementation of the funds program in the School Operational Assistance in Sumba Barat Daya District of Nusa Tenggara Timur Province began in 2008 with funding is IDR 2,300,450,200, while for the year 2011 of the School Operational Assistance fund budget amounted to IDR.3,090,148,750. Funding for these programs has cost the government large enough, but what degree of its effectiveness is not known with certainty. The research problem is how to rate the effectiveness fund program of School Operational Assistance in Sumba Barat Daya District of Nusa Tenggara Timur Province. While the goal of the study was to find out the effectiveness of the funds program of the School Operational Assistance at Sumba Barat Daya District of Nusa Tenggara Timur Province. This study used a qualitative design, the data collected through interviews and documentation. While the technique of data analysis is descriptive qualitative analysis technique, namely to provide a qualitative description of the facts of the research findings. Based on the results of the study show that the effectiveness of funds program of the School Operational Assistance do not maximized to improve the accessibility and public participation rate at primary education for poor communities in Sumba Barat Daya District of Nusa Tenggara Timur Province. Effectiveness is measured by the precision dimension, all of which indicates the category is not precise in terms of time, the precision of the number, target precise and precision in terms of administration. The study recommends that to improve the effectiveness of fund program of the School Operational Assistance needs to be increased control and improvement standard operating procedures mechanism of funds to implement the program.

Keywords: Effectiveness, Public Policy, the School Operational Assistance.

1. INTRODUCTION
One indicator of the the progress of development of a nation is the level of achievement of the development of human resources, primarily on the education sector. The education sector is a key sector for any country that wants to acquire and master advanced technology.
The Constitution of the Republic of Indonesia Year 1945 in Article 31 paragraph (1) has mandated that every citizen has the right to get an education and develop their potential optimally. Along with efforts to implement the mandate of the law then the government issued a policy through Act No. 20 of 2003 on National Education System. The government attempted improve the quality of education in Indonesia are taken through a variety of strategies, but the results of the development of education in Indonesia is still not achieve maximum results.

Under the performance index of Human Development in Indonesia is still cause for concern, namely in 2004 was ranked 110 out of 173 countries. This means that Indonesia lagged behind other ASEAN countries such as Malaysia (59), Thailand (70) and the Philippines (77). Indonesia is ranked even below Vietnam, a country emerging from war-torn prolonged (UNESCO 2004).

The Achievement in the field of education Indonesia is evidence of the development of the education sector has not been successful. Therefore, the government is continuously trying to make efforts, including through the completion of the handling of the Compulsory Basic Education 9 Year. The policy of education development in the period 2004 - 2009 priority on increasing of public access to more the quality basic education, through Improved Implementation of Compulsory Basic Education 9 Years and giving greater access to community groups that have felt less able to reach basic education services.

One of the programs in the field of education that get a large budget allocation is the funds Program of School Operational Assistance. Through this program, the central government provides funds to schools at the primary and secondary are willing to comply with the provisions stipulated in the requirements for program participants.

The implementation of the program, in Sumba Barat Daya District began in 2008, budget school operational funds are disbursed IDR. 3,090,148,750.. Urgency given the funds Program of School Operational Assistance is to reduce the burden on society, especially the poor or unable to support their educational services Compulsory adequate and quality.

The implementation of the funds Program of School Operational Assistance apparently not as expected, there are schools that charge money enrollment at the elementary level and contributions pay for educational Development. Results of interviews the author of some of the teachers, showed that the use of the funds by the school, not done in consultation with all components of the school, including parents/ guardians of the pupil. The engagement of parents at each meeting at school just to talk about the contribution of the parents of the students to the school budget shortfalls.

2. THE RESEARCH PROBLEM
The research problems are how is the effectiveness of the funds Program of School Operational Assistance at the elementary school in elementary school in Sumba Barat Daya District of Nusa Tenggara Timur Province?

3. THE RESEARCH OBJECTIVE
This study aims to find out the effectiveness of the implementation of the funds Program of School Operational Assistance at the elementary school in elementary school in Sumba Barat Daya District of Nusa Tenggara Timur Province?

4. THEORETICAL FRAMEWORK
4.1. The Concept of Program Effectiveness.
The effectiveness of the program is the goal to be achieved in any policy implementation, the programs are not successfully implemented in the program indicates that there is something of
a problem. Implementation study has given us an understanding of why a well-executed program and why there are programs also fail (Pressman and Wildavsky, 1978; Anderson, 1978; Jones, 1984).

The factors effective or not an implementation can be viewed from three perspectives, namely, the first, of the initiator of policy / decision makers, namely the efforts made by officials at a lower level in changing public attitudes / target groups. Second, efforts made by the implementers in the field. Finally, the target group, the those who will enjoy the results of a program, extent of services that have been provided may change the pattern of his life, can have a positive impact in the long term to improve the quality of life including their income (Wahab, 2000)

While Hogwood and Gunn (1984), noted that to implement the policy completely, the necessary requirements are:

a. The external condition of the executing agency does not become limiting freedom of movement of the implementing agencies.

b. There is sufficient time and resources to implement the policy.

c. The various resources needed really available.

d. The policy will be implemented based on the theory valid.

e. The relationship between cause and effect is straightforward and only a few are related indirectly.

f. The dependency relationship is only a little.

g. There is an understanding and agreement will be goals to be achieved.

h. The tasks specified in the proper order.

i. There is a perfect communication and coordination.

j. Those who have the authority can do the demands and demands are met completely.

Furthermore, Ripley and Franklin (1986), argues that there are three main way of thinking for the successful implementation of the program, namely:

” (1) Some argue that success should be measured by the degree of compliance on part of bureaucratic underlings to their bureaucratic superior or by the degree of compliance on the part of bureaucracies in general with specific mandates contained the statute; (2) Perspective argue that successful implementation is characterized by smoothly functioning routines and absence of problem; (3) There is no way around the fact that desirable is not objective, neutral concept. The desirability relates to value held by one or more people “.

According to Dunn (1981), to assess the success of the implementation of the program based on the dimensions, namely: (1) effectiveness; (2) efficiency; (3) adequacy; (4) equity; (5) responsiveness; (6) appropriateness.

4.2. THE FUNDS PROGRAM OF SCHOOL OPERATIONAL ASSISTANCE

The Purpose of funds Program of School Operational Assistance is to free of payout for poor pupils and relieve for pupils, so that they acquire the services of Education

The provision of assistance funds are:

1. The primary schools was IDR.254.000 per year

2. The secondary school was IDR.354 per year

This program was initiated in an effort to improve public access, especially the pupils from poor families to quality education in the context of compulsory nine years. Schools that receive funds Program of School Operational Assistance the are required to follow all rules set by the program manager, both about how to the management, use, accountability funds have been received.
5. METHODS
This study used a qualitative research method that is research that produces descriptive data in the form of written words or refers to the process and meaning that are not tested or measured strictly. The main emphasis on the qualitative approach in this study is based on consideration that the focus of this study reveal the effectiveness of funds Program of School Operational Assistance. To see the empirical facts, the necessary interpretation of the meaning and interpretation of the action. Disclosure process and interpretation of the qualitative approach is more relevant (Creswell; 1994). The focus of research are on the effectiveness of funds Program of School Operational Assistance at Sumba Barat Daya District of Nusa Tenggara Timur Province, which includes dimensions: (1) efficiency; (2) adequacy; (3) equity; (4) responsiveness. The data collection techniques, namely observation, documentation, and in-depth interviews. The collected data were then analyzed using qualitative descriptive analysis. Qualitative data collected will be interpreted by triangulation.

6. RESULTS AND DISCUSSION
6.1. The Implementation funds Program of School Operational Assistance
The results of audit from Representative financial Control Agency and Development Nusa Tenggara Province showed some findings include: (1) There are surplus of payment of funds received 7 elementary schools, IDR. 21.6975 million; (2) There is a shortage of payment of funds received 20 elementary schools with value IDR.115.257.000; (3) Tax on the taxable salary has not been submitted to the State Treasury, IDR.8.301.775; (4) there is a difference of funds that must be accounted for, should at IRD.108.328.343.

Realization of payment from fund for each quarterly also appears to not function properly. There was delay in each quarter, shown in the table 1.

<table>
<thead>
<tr>
<th>Quarterly</th>
<th>Realization at</th>
<th>Supposed to</th>
<th>Delays</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>25th april 2011</td>
<td>January 2011</td>
<td>3 months</td>
</tr>
<tr>
<td>II</td>
<td>6th June 2011</td>
<td>April 2011</td>
<td>2 months</td>
</tr>
<tr>
<td>III</td>
<td>19th september 2011</td>
<td>July 2011</td>
<td>2.5 months</td>
</tr>
<tr>
<td>IV</td>
<td>19th January 2011</td>
<td>October 2011</td>
<td>3 months</td>
</tr>
</tbody>
</table>


While the program performance assessment in 2011 considered less successful because achievement scores showed only 56.77% of the maximum value of 100%. These results were obtained from measurements of performance indicators targeting accuracy, precision number, timing, and accuracy of fund management and administration accuracy.

In terms of targeting accuracy program management in 2012 was considered successful because all elementary schools are being targeted all received fund program. From the the accuracy of the amount, considered less successful because still some schools that receive funds exceed the target and also there are many schools that receive less than that stipulated. The effectiveness of the management of funds program can also be viewed from the appropriate usage designation. The funds intended for financing component 13 as mentioned in the technical guidance funds program in 2011. The use of the funds for the 13 components of the six schools of the case can be seen in table 2.
### Table 2 Use of BOS Quarterly I - IV Fiscal Year 2012

<table>
<thead>
<tr>
<th>Item</th>
<th>Component Financing</th>
<th>Quarterly I</th>
<th>Quarterly II</th>
<th>Quarterly III</th>
<th>Quarterly IV</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Purchase / doubling of textbooks</td>
<td>3.562.450</td>
<td>-</td>
<td>1.484.000</td>
<td>-</td>
<td>5.046.450</td>
</tr>
<tr>
<td>2</td>
<td>Financing activities in the context of new admissions</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>3</td>
<td>Financing remedial learning activities.</td>
<td>7.929.500</td>
<td>7.606.050</td>
<td>6.242.250</td>
<td>2.182.000</td>
<td>23.959.800</td>
</tr>
<tr>
<td>4</td>
<td>Costs of daily tests, general tests, etc.</td>
<td>9.559.400</td>
<td>9.608.700</td>
<td>3.350.000</td>
<td>2.320.000</td>
<td>24.838.100</td>
</tr>
<tr>
<td>5</td>
<td>The procurement of consumable materials</td>
<td>1.639.500</td>
<td>4.477.500</td>
<td>16.489.750</td>
<td>5.995.000</td>
<td>28.601.750</td>
</tr>
<tr>
<td>6</td>
<td>Paying bills and services</td>
<td>370.400</td>
<td>200.000</td>
<td>754.500</td>
<td>559.100</td>
<td>1.884.000</td>
</tr>
<tr>
<td>7</td>
<td>Financing of School Care</td>
<td>900.000</td>
<td>1.035.000</td>
<td>1.240.000</td>
<td>2.719.000</td>
<td>5.894.000</td>
</tr>
<tr>
<td>8</td>
<td>Payment of monthly salary honorary teachers</td>
<td>7.350.000</td>
<td>7.350.000</td>
<td>7.350.000</td>
<td>7.350.000</td>
<td>29.400.000</td>
</tr>
<tr>
<td>9</td>
<td>The Teacher professional development such as training, etc.</td>
<td>3.946.250</td>
<td>2.193.000</td>
<td>862.500</td>
<td>1.048.750</td>
<td>8.050.500</td>
</tr>
<tr>
<td>10</td>
<td>Financing for the poor pupils</td>
<td>1.112.500</td>
<td>-</td>
<td>-</td>
<td>2.014.500</td>
<td>3.127.000</td>
</tr>
<tr>
<td>11</td>
<td>Financing of Fund Program</td>
<td>8.000.000</td>
<td>1.287.000</td>
<td>6.515.500</td>
<td>-</td>
<td>15.802.500</td>
</tr>
<tr>
<td>12</td>
<td>Purchase of computers and printers for Pupils learning activities</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>13</td>
<td>Other spending According SOP</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount Per Quarterly and Total</th>
<th>Amount of funds that should be accounted</th>
<th>Funds that have not been accounted</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>44.370.000</td>
<td>44.370.000</td>
<td>44.370.000</td>
</tr>
<tr>
<td>2</td>
<td>33.757.250</td>
<td>44.288.500</td>
<td>24.188.350</td>
</tr>
<tr>
<td>3</td>
<td>44.288.500</td>
<td>24.188.350</td>
<td>146.604.100</td>
</tr>
<tr>
<td>4</td>
<td>1.112.500</td>
<td>2.014.500</td>
<td>180.235.000</td>
</tr>
<tr>
<td>5</td>
<td>3.946.250</td>
<td>1.048.750</td>
<td>8.050.500</td>
</tr>
<tr>
<td>6</td>
<td>1.035.000</td>
<td>2.719.000</td>
<td>5.894.000</td>
</tr>
<tr>
<td>7</td>
<td>7.350.000</td>
<td>7.350.000</td>
<td>29.400.000</td>
</tr>
<tr>
<td>8</td>
<td>8.000.000</td>
<td>6.515.500</td>
<td>15.802.500</td>
</tr>
<tr>
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<td>3.946.250</td>
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<td>8.050.500</td>
</tr>
<tr>
<td>10</td>
<td>1.112.500</td>
<td>-</td>
<td>3.127.000</td>
</tr>
<tr>
<td>11</td>
<td>8.000.000</td>
<td>6.515.500</td>
<td>15.802.500</td>
</tr>
<tr>
<td>12</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>13</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

**Source:** Department of Education Sumba Barat Daya District 2011

### 6.2. Discussion

**Dimensions of Efficiency**

The efficiency of the implementation of the views of whether the funds are available per quarter can be used appropriately according to the plan that has been set. Recognition of
school administrators that there are many activities that are not planned but financed and much work plan set out in the planning but it is not funded.

The budget planning should be understood as a series of activities to establish financing items prioritized in efforts to succeed the Funds Program of School Operational Assistance. Therefore, if there are other activities that are not stipulated in the planning but financed and ignore items that have been assigned activities in planned indicate that the use of the funds is still far from the principles of efficiency.

**Dimensions of Adequacy**

The adequacy of our views of the availability of funds can be used to solve problems facing the school. Use of the funds are considered sufficient if the principle of budgetary efficiency to be considered in planning and implementing their compliance to predetermined.

Conditions experienced by most schools are planning the budget made by the principal and the treasurer is unable to accommodate the needs of the learning process of any teacher or other needs that the board of teachers should receive priority in funding.

**Dimensions of Equity**

The dimensional of equity can be seen from whether the funds are available actually used by schools and has solved all of the problems encountered in proportion. Almost all schools use the highest funds for daily tests and general tests as well as the payment of honorarium while components other financing received a very low percentage of financing.

**Dimensions of Responsiveness**

The dimention of responsiveness dimensional seen of managers's responsiveness to the needs facing the school. Data shown previously showed that in every quarter of the schools always receive the funds and finance a number of activities on a regular basis, but in every quarter of the same there are a variety of teacher complaints over shortages of facilities and infrastructure support in the learning process is an indicator of the use of funds that are not responsive.

Responsiveness managers closely related to transparency in planning. Because only with transparency all needs can be identified and used as the basis for financing, indeed require the presence of a fairly high responsiveness to various needs of the school, but managed responsiveness as well. Responsiveness that is not managed can make funds available always considered insufficient.

**Dimensions of Appropriateness.**

The dimention of appropriateness seen of the funds used in schools really benefit the school community. Use of funds that do not pay attention to aspects of equity and efficiency as described previously made use of the funds are considered to be less precise. Various complaints put forward by the teacher relevant shortages experienced in the learning process is an indicator of the inappropriateness of use of the funds at the school.

7. **CONCLUSION**

The funds Program of School Operational Assistance at the elementary school in Sumba Barat Daya District of Nusa Tenggara Timur Province is not effective based on the criteria of efficiency, adequacy, equity, responsiveness. Implementation of a program organized by the school at the elementary school level has not run properly. The problems that arise in funds Program of School Operational Assistance include: the activities are designed to accommodate the needs of assistance programs have not been the learning process in schools, budget disbursement is not appropriate in terms of time and the amount of aid realization, the realization of the budget does not match the the number of pupils eligible for benefits, and its use is not in accordance with the financing items based planning program.
a. Implementation Assistance have not been able to solve the problem of funding needs required by the school. Still many minimum requirements of the school to fund the learning process can not be met from the operational assistance programs. Implementation Assistance have not been able to solve the problem of funding needs required by the school. Still many minimum requirements of the school to fund the learning process can not be met from the operational assistance programs.

b. The responsiveness program management has not been achieved since not been able to respond to various problems needs teaching and learning process. There are still many items financing needs of the learning process have not been accommodated in program planning activities that will get help financing.

Suggestion
To reorganize the management of school operational funds in order to meet the criteria of effectiveness, efficiency, adequacy, equity, and responsiveness it is necessary to note the following:

a. Strict and intensive Oversight by the relevant authorities such as management team of operational assistance fund, the Regional Inspectorate, and Representative Financial Control Agency and Development Nusa Tenggara Province.

b. The involvement of the school committee should also be done in order to be in cooperation and mutual balance in the planning and implementation of operational funds.

c. In addition to internal party it is necessary also for the involvement of external parties such as the Board of Teachers, parents, media, and education observer in the context of external oversight.

d. The need reexamination of standard operational procedures (SOP) that already exist, given that the SOP is now less supportive of flexibility realization operational funds to schools beneficiaries.

LITERATURE


CHALLENGES FOR A MODERN UNIVERSITY MANAGEMENT

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ABSTRACT
In the last decades, society has changed sustainably and universities have thus faced new requirements. As a result of competition and globalisation, education and knowledge management had to be adapted. Universities were forced to establish a modern management system primarily known from the private sector. In 2002, the Austrian government implemented a revised Universities Act to integrate these concepts. But changing has led to strong resistance, as the law seems to question the self-conception of the universities.

The objective of this study was twofold. Firstly, we analysed the challenges for a modern university management. Secondly, we investigated specific characteristics that may affect the attitude towards a modern university management. Referring to our first objective, literature review has revealed severe contradictions between modern university management and the traditional understanding of universities. While the traditional scheme has focused mainly on research, teaching is becoming more relevant in the new demand-driven university. Also, the freedom of science and teaching is limited by the strong orientation on goals that have been agreed upon with the government. Further contradictions can be identified in budgeting, leadership, hierarchy, and employee participation. To examine the second research aim, we sent a paper-and-pencil questionnaire to all members of the university under investigation. A total of 414 respondents (51% women; 58% academic members; 12.58% response rate) have submitted full data. Canonical correlations indicate that a higher engagement in research and leadership positions results in a higher acceptance of a modern university management. Interestingly, no significant differences were measured regarding the area of science.

Our findings identify the challenging factors for a modern knowledge and education management at universities and can certainly help to understand the ambivalent attitude towards modern university management.

Keywords: attitude, knowledge management, leadership, new public management, university

1. INTRODUCTION
In the last decades, Central European universities have changed radically. Economic parameters, prevalent organisation structures, and the expansion of universities require adoptions to ensure continuing performance (Titscher, 2000). Willingness to finance public services is decreasing continuously and citizens are becoming noticeably dissatisfied with the administration (Fellmann, 2000). Increasing expenses and scarce state resources necessitate reforms (Biedermann and Strehl, 2004).

According to Badelt (2004), universities have to expect increasing scarcity of public resources and are therefore increasingly exposed to business management-orientated mechanisms. They have to seek third-party funding and are in competition with colleges and private universities. All in all a commercialisation of the tertiary education sector is noticeable (Badelt, 2004). In addition to these economic changes, universities face requirements and duties that are also subject to change; e.g. today’s universities are increasingly taking on vocational training issues (Hödl, 2002). Globalisation also has effects on universities, causing a high level of competition as well as a steady increase in mobility and societal demands. The development of the European Higher Education Area can be seen as a reaction to the globalisation of
society (Pellert, 2006), as it aims to strengthen the competitiveness of the member states of the European Union in relation to North America and East Asia (Pechar, 2006).

To overcome these challenges, the new Universities Act was issued in Austria in 2002. In this act, a modern management and leadership system oriented towards methods and instruments of the private sector in many fields was implemented. The implementation of the Universities Act was accompanied by numerous protests, arguing that this act seemed to question the universities’ self-conception. Therefore, two questions are raised in this article:

1) What are the challenges of modern university management? Causes and problems are localised through a literature research.

2) What is the attitude of university members towards this modern university management? An empirical study examines which characteristics influence the attitude towards modern university management.

2. CHALLENGES FOR A MODERN UNIVERSITY MANAGEMENT

In the first part of this article, we will identify challenges and problems that may be responsible for missing acceptance among the university members.

When considering the history of Central European universities on the one hand, a traditional university model is prevalent that focuses on research, where students can participate in the cognitive process enhanced by research-oriented teaching, and researchers are able to conduct pure research in absolute freedom and solitude (Kopetz, 2002; Sieg, 2005). University members participate in numerous committees and are involved in all decision and discussion processes (Höllinger, 2004). In an institutional budgetary system with single-entry bookkeeping (“cameralistic accountancy”) and a bureaucratic administrative management more attention is paid to the norm-related use of state resources and the compliance with budgetary estimates than to real needs (Müller-Böling, 2000). The university is characterised by a barely existing institutional autonomy in which the state tries to control details (Raschauer, 2004) and a hierarchical curia system (professors, assistants, students, non-academic staff) in which members face each other in troublesome discussions (Nickel and Zechlin, 2000).

On the other hand, the ideal type of a “modern” university has evolved. This type of university should encourage research and teaching to respond to social and economic demands, and needs to act in a customer and demand-oriented way (cf. in general with regard to a modern administrative management, Schedler and Proeller, 2006). While both internal and external competition should increase quality (Dumont du Voitel, 1996), the establishment of management-orientated elements should also raise efficiency and effectiveness (Titscher, 2000). The agreed social and economic goals are realised more effectively through performance-oriented actions. Universities obtain greater institutional autonomy together with a distinct operative independence (Müller-Böling, 2000). The participative decision process is replaced by lean hierarchies as well as a strong management with concrete responsibilities and the task of balancing the demands of the university’s stakeholders (Daxner, 2000). But this type of university is also subject to certain criticism because of its restricted freedom of researching and teaching (Ridder, 2005). Standardised parameters are used to evaluate performance without considering specialised requirements.
Table 1: Comparison of traditional and modern university management
(Source: Author's illustration)

<table>
<thead>
<tr>
<th>Elements of a traditional university</th>
<th>Elements of a modern university</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emphasis on research (Humboldt: Research imperative)</td>
<td>Emphasis on teaching (customer, demand, and application orientation)</td>
</tr>
<tr>
<td>Absolute freedom of research and teaching</td>
<td>Performance orientation of research and teaching, management by objectives</td>
</tr>
<tr>
<td>Institutional budgetary system with single-entry bookkeeping (&quot;cameralistic accountancy&quot;, input orientation)</td>
<td>Global budget, output orientation</td>
</tr>
<tr>
<td>Bureaucratic administrative management</td>
<td>Management orientation and implementation of economic mechanisms</td>
</tr>
<tr>
<td>No institutional autonomy</td>
<td>Great institutional autonomy</td>
</tr>
<tr>
<td>Participation of university members</td>
<td>Strong management</td>
</tr>
<tr>
<td>Hierarchical curia system</td>
<td>Lean hierarchies</td>
</tr>
</tbody>
</table>

Table 1 gives a compact overview of the various elements of a traditional and a modern university management. When looking at the comparison, contradictions between the two leadership and management types can be identified (marked by a lightning symbol). Challenges that the modern university faces have to be pinpointed there, as missing acceptance can lead to problems in their implementation. The most important contradictions and challenges are depicted as follows:

- **Challenge I – demand and customer orientation**: Since the traditional university focused on research, teaching was only a “by-product”. However, modern university management has to react to the social, political, and economic demand which especially includes education and further training respectively of qualified employees. Therefore, universities have to focus more on teaching.

- **Challenge II – performance orientation and management by objectives**: Researchers working in absolute freedom independent of purpose and utility for society are not compatible with an orientation towards performance agreements with the Ministry. Those agreements may restrict the freedom of research.

- **Challenge III – budgeting**: Institutional budgeting where resources are distributed with detailed specifications for usage but without reference to performance (input orientation), is contradictory to a goal-oriented budgetary allocation through global budgets (output orientation). Universities are granted much freedom in the usage of resources, which represents quite a challenge for the university organisation, since distribution battles now have to be resolved internally.

- **Challenge IV – management orientation**: A system of bureaucratic structures with many rigid norms, officialdom, and a strict competence system is confronted with a modern public management system, in which the state is a service provider striving to increase efficiency, effectiveness, and flexibility through managerial control mechanisms.

- **Challenge V – autonomy**: High individual autonomy (“freedom of research”) is weakened in favour of higher institutional autonomy with operatively autonomous universities. Individual action can no longer be seen as being independent of group interests. The individual has to accept its subordinate role in favour of the group.

- **Challenge VI – participation**: Intense participation of university members in the discussion and decision process is replaced by strong management in many areas. This management takes over lots of competences from committees and is strengthened in its decision and leadership responsibility. University members can no longer participate in every decision process.

- **Challenge VII – hierarchies**: The hierarchical curia system, consisting of professors, assistants, students, and non-academic staff, no longer meets modern requirements. Modern university management needs to establish lean hierarchies, filling vacant management positions regardless of class and status, as well as a decentralised management with clear allocation of responsibilities.
3. ATTITUDE TOWARD A MODERN UNIVERSITY SYSTEM
Considering the above mentioned challenges, it is clear that the implementation of a modern university management, which was carried out in Austrian universities with the Universities Act 2002, is a profound paradigm shift. Severe protests accompanied the implementation of the act, and even today, discussions are controversial. In this part of the article, possible factors that influence the attitude of university members will be examined. Two characteristics seem to be of special interest. First, it can be assumed that the activity structure has effects on attitudes towards a modern university management. Freedom of research is restricted by objective agreements and the demand orientation of universities is responsible for the increasing importance of teaching. Thus, the following hypothesis is formulated:

**H1:** Persons predominantly involved in research are more critical of aspects of a modern university management than persons chiefly involved in teaching.

Second, the various scientific fields exhibit highly differentiated cultures whose members are socialised in a different way. This could also influence attitudes towards a modern university management. Therefore, the following hypothesis is formulated:

**H2:** Acceptance regarding aspects of a modern university management depends on the scientific field.

4. METHODS
A paper-and-pencil interview was conducted using a standardised questionnaire. The paper-and-pencil questionnaire was sent to all members of the University of Graz, i.e. 3,290 persons in total. We received 414 returns (50.7% women, 58.21% scientific staff) which is a response rate of 12.58%. SPSS was used for analysing the data. The questionnaire was based on interviews with experts of university development and organisation. Prior to the survey, a pre-test with 15 persons was conducted. The sample was divided into non-scientific and scientific university staff whereby the latter can be divided into further subgroups. In cases where a person could have been counted as belonging to either group \((n = 24)\), that person was added to a subgroup of the scientific staff. Questionnaires from 73 professors, 120 assistants, 48 lecturers and project staff, and 157 persons of the non-academic university staff were taken into account in the study. Prior to the analysis, variables were transcoded so that higher values depicted higher characteristic attributes. In the next step, the consolidation of data was carried out based on an explorative data analysis (factor analysis). Beforehand, the data was tested regarding its applicability. Prerequisites are fulfilled according to Bartlett’s test as well as to the KMO criterion. The amount of factors to be extracted primarily followed the Scree test. The rotation was orthogonal. In relation to the general attitude towards university, four factors were extracted with an explained variation of 42.8% in total. With regard to university development, three factors were extracted with an explained variation of 52.9% in total. Concerning the attitude towards research and teaching, three factors were extracted with an explained variation of 53.9% in total. With reference to the attitude towards administration, two factors were extracted with an explained variation of 56.7% in total. Results from the explorative data analysis were used during further analysis. Canonical correlation analyses and multivariate t-tests were applied for the confirmatory analysis of the hypotheses.

5. RESULTS
One question investigated how strong employees assess the extent of change. A total of 325 persons (78%) from the sample answered this question. These assessments vary empirically (Figure 1) with lecturers and project staff, in particular, perceiving strong change less
frequently. However, these differences are not significant. As regards the question as to how changes are evaluated (rather positive; partly, partly; rather negative), assessments vary per group affiliation ($\chi^2 = 24.85; df = 6; p < .01$). Non-academic university staff assess change more positively respectively less negatively than the other groups (Figure 2).

\[\text{Figure 1: Extent of changes (amount on particular subsample, N = 325)}\]
\[\text{(Source: Author’s illustration)}\]

\[\text{Figure 2: Tendency of changes (amount on particular subsample, N = 307)}\]
\[\text{(Source: Author’s illustration)}\]

6. ACTIVITY STRUCTURE
The first assumption questioned whether the type of university activity had an effect on the attitude towards a modern university management. In the paper-and-pencil interview, the working time structure (research, teaching, management, committees, administration, other) was surveyed. The analysis was conducted for the scientific staff. The relation to the attitudes towards a modern university management was examined using canonical correlation analyses.

General attitudes and attitudes towards research and teaching. General attitudes and attitudes towards research and teaching are related to the reported working time structure (Table 2). The higher the reported amount of research and the amount of leadership roles per working time, the lower is the rejection of a strong management and pessimism related to controlling instruments (e.g. performance records), in particular. Aspects of institutional autonomy and performance as well as competition orientation tend to turn out stronger. The same applies to the opposite: the higher the reported amount of teaching per working time, the higher the rejection of a strong management and pessimism related to controlling instruments. Performance and competition orientation and the striving for institutional autonomy tend to turn out lower.

80
Table 2: Canonical correlation analysis: Correlation between general attitudes as well as attitudes towards research and teaching and the working time structure of scientific staff
(Source: Author’s illustration)

<table>
<thead>
<tr>
<th>Loadings</th>
<th>Can. corr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canonical correlation coefficient</td>
<td>$R = .45$</td>
</tr>
<tr>
<td>Significance</td>
<td>**</td>
</tr>
<tr>
<td>Degree of freedom</td>
<td>$df = 35/667$</td>
</tr>
</tbody>
</table>

**Loadings**

**Working time structure – items**

- Amount research
- Amount leadership roles
- Amount teaching

**General attitudes – factors**

- Rejection strong management
- Competition orientation
- Performance orientation
- Institutional autonomy

**Research and teaching – factors**

- Pessimism related to controlling instruments

Selected aspects of university development. Additionally, the assessment of aspects of university development is related to the reported working time structure. The rare case of all canonical correlation coefficients being significant occurs – here we have three. The first canonical correlation (Table 3) shows the relation between working time structure and striving for more autonomy. The higher the reported amount of administration per working time, the less meaningful aspects of autonomy are rated. The higher the other amounts of working time, the more useful those aspects are evaluated. The second canonical correlation (Table 4) especially shows the relation between the amounts of working time and the enterprising university. The higher the reported amount of leadership roles per working time, the more meaningful aspects of the enterprising university as well as aspects of autonomy are rated. The third canonical correlation (Table 5) shows the relation between the working time structure and the assessment of aspects regarding the performance orientation. The higher the reported amount of research, the more useful aspects concerning performance orientation are rated.

Table 3: Canonical correlation analysis: Correlation between aspects of the university development and the working time structure of scientific staff I (Source: Author’s illustration)

<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Canonical correlation coefficient</td>
<td>$R = .49$</td>
</tr>
<tr>
<td>Significance</td>
<td>**</td>
</tr>
<tr>
<td>Degree of freedom</td>
<td>$df = 15/455$</td>
</tr>
</tbody>
</table>

**Loadings**

**Working time structure – items**

- Amount research
- Amount leadership roles
- Amount teaching
- Amount committees
- Amount administration

**Aspects university development – factors**

- Autonomy striving
- Enterprising university

+++/- -- structure coefficient with absolute over .70; +/- -- structure coefficient with absolute over .50; +/- -- structure coefficient with absolute over .30; ** ‘highly significant’ outcome, assertion applies with 99% certainty; * ‘significant’ outcome, assertion applies with 95% certainty
+++/-—structure coefficient with absolute over .70; +/-—structure coefficient with absolute over .50; +/-—structure coefficient with absolute over .30; **‘highly significant’ outcome, assertion applies with 99% certainty; *‘significant’ outcome, assertion applies with 95% certainty

**Table 4: Canonical correlation analysis: Correlation between aspects of university development and the working time structure of scientific staff II**
(Source: Author’s illustration)

<table>
<thead>
<tr>
<th>2. Can. corr.</th>
<th></th>
</tr>
</thead>
</table>
| Canonical correlation coefficient | $R = .30$
| Significance | **
| Degree of freedom | $df = 8/322$

**Loadings**

<table>
<thead>
<tr>
<th>Working time structure – items</th>
<th></th>
</tr>
</thead>
</table>
| Amount leadership roles | ---
| Amount committees | +

<table>
<thead>
<tr>
<th>Aspects university development – factors</th>
<th></th>
</tr>
</thead>
</table>
| Autonomy striving | --
| Enterprising university | ---

+++/-—structure coefficient with absolute over .70; +/-—structure coefficient with absolute over .50; +/-—structure coefficient with absolute over .30; **‘highly significant’ outcome, assertion applies with 99% certainty; *‘significant’ outcome, assertion applies with 95% certainty

**Table 5: Canonical correlation analysis: Correlation between aspects of university development and the working time structure of scientific staff III** (Source: Author’s illustration)

|----------------|---|
| Canonical correlation coefficient | $R = .25$
| Significance | **
| Degree of freedom | $df = 3/167$

**Loadings**

<table>
<thead>
<tr>
<th>Working time structure – items</th>
<th></th>
</tr>
</thead>
</table>
| Amount research | +++
| Amount committees | -
| Amount administration | -

<table>
<thead>
<tr>
<th>Aspects university development – factors</th>
<th></th>
</tr>
</thead>
</table>
| Performance orientation | +++

+++/-—structure coefficient with absolute over .70; +/-—structure coefficient with absolute over .50; +/-—structure coefficient with absolute over .30; **‘highly significant’ outcome, assertion applies with 99% certainty; *‘significant’ outcome, assertion applies with 95% certainty

7. SCIENTIFIC FIELDS

The second hypothesis addressed the question as to whether the attitude towards a modern university management depended on the scientific field.

**Single disciplines.** First, the evaluation of single disciplines was conducted by multivariate t-tests. The only significant difference appeared in Theology ($T_{7,157} = .121; p < .05$). Theologians rated aspects of performance orientation less positively ($F_{1,163} = 7.21; p < .01; M = -.55/.20$) and showed higher values on the scale “institutional autonomy” ($F_{1,163} = 6.74; p < .01; M = .81/.17$) than persons from other scientific fields.

**Pooled disciplines.** Further analysis was conducted in relation to pooled disciplines. At first, the fields were separated into six groups (Table 6). Since the subsamples were too small for analysis with simultaneous consideration of the group affiliation, the groups were joined to form two respectively three groups. Still, no significant results emerged.
Table 6: Scientific fields (Source: Author’s illustration)

<table>
<thead>
<tr>
<th>Scientific field</th>
<th>N</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Economic sciences</td>
<td>20</td>
<td>8.3%</td>
</tr>
<tr>
<td>Natural sciences</td>
<td>64</td>
<td>26.6%</td>
</tr>
<tr>
<td>Social sciences</td>
<td>21</td>
<td>8.7%</td>
</tr>
<tr>
<td>The humanities</td>
<td>46</td>
<td>19.1%</td>
</tr>
<tr>
<td>Jurisprudence</td>
<td>25</td>
<td>10.4%</td>
</tr>
<tr>
<td>Linguistics</td>
<td>40</td>
<td>16.6%</td>
</tr>
<tr>
<td>No declaration</td>
<td>25</td>
<td>10.4%</td>
</tr>
<tr>
<td><strong>Sum</strong></td>
<td>241</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

8. CONCLUSION

Modern university management breaks with university traditions in many ways. Results show clearly that challenges occur especially where modern and traditional university management are inconsistent. Lack of acceptance of aspects like demand or customer orientation, management by objectives and performance orientation, budgeting, business-management orientation, autonomy, and participation can lead to problems in implementation. The investigated members of staff had observed great changes at universities over the last few years. External lecturers and project staff had the weakest perception. Due to their lower commitment to the university, they are probably less affected by changes. Non-academic university staff evaluated changes as less negative than all other groups. One possible explanation is that processes in university administration are consistently similar to those in the private sector. The use of managerial methods and instruments may therefore be less challenging than in research and teaching.

The initially postulated hypotheses regarding characteristics that may influence the attitude towards a modern university management were not confirmed. However, it was shown that the activity structure of researchers is an important factor for attitudes towards a modern university. The higher the reported amount of teaching per working time, the more negative is the attitude towards instruments of modern university management. Initially a reverse relation had been assumed. Two explanations can be mentioned here. On the one hand, the result could indicate that the teaching load has become too high in a modern demand-oriented university. Subsequently, the scientific staff would appreciate having more time for researching, but are not able to do so because they need to meet the demands in teaching. In this case, results would indicate that employees with a higher reported amount of teaching load already observe negative effects on their work and relate those directly to the modern university. Another possible explanation is that modern management methods not only entail risks for research but offer opportunities as well. Competition and performance orientation yields higher rewards (e.g. through more resources) for scientific performances. Hence, quality research can benefit much more from a modern university than from traditional management instruments.

Regarding the second hypothesis, it was assessed that there were no significant differences in the attitude to a modern university management concerning varying scientific fields or their groupings. Thus, this hypothesis has to be rejected. One reason for this may be that a harmonisation of demands on scientific staff has been observed in the last few years, independent of the differentiated socialization of single disciplines. Today, structured career paths, continuous evaluation of research and teaching, unified quality standards, and key
performance indicators only differ partly between single disciplines. The members and their attitudes are becoming similar in those aspects.

Although this study refers to Austrian universities, its results could also be applied to developments in other, especially Central European countries, due to similar tendencies in university management. To conclude, the feared downfall of universities did not occur and the predominant majority of university staff faces those changes neutrally. Every reform has its winners and losers and not always are they found where anticipated.

Results also indicate a development from the wide base to the top. The majority of scientists will have to expect a high load of teaching, low participation in decision-making and also probably low acknowledgement. However, the top segment will discover completely new opportunities, chances, and resources in a modern university management. Moreover, another trend can be detected which has to be followed with great care: While, on the one hand, sciences and their disciplines are increasingly specialising, scientists and their values and cultures are gradually growing together on the other. In the long run, this could also affect the diversity of opinions and ideas.

LITERATURE


ANALYZING THE RELATIONSHIP BETWEEN BOOK TO MARKET (B/M) VALUE AND PROFITABILITY RATIOS OF TEHRAN STOCK EXCHANGE COMPANIES

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ABSTRACT
The objective of the current research is to analyze the relationship between book-to-market (B/M) value ratio and profitability ratios in Tehran Stock Exchange companies during the recent years. If the research hypotheses are approved and the model proposed in the present research is confirmed, the investors and analysts of capital market in Tehran Stock Exchange will be able to benefit from the crucial and applicable B/M ratio. Through testing the hypotheses, it was found that there exists a significant and inverse relationship between B/M ratio and Return on Equity (ROE) ratio of stockholders and EPS value; this finding is in agreement with the results of research works formerly conducted in this scope. Also, no significant correlation was observed between B/M ratio and profit margin.

Key Words: Book-to-Market (B/M) Value Ratio, Profitability Ratios, Tehran Stock Exchange

1. INTRODUCTION
Individuals must invest their revenue surpluses for economic growth of any country. Therefore, any investor requires information about stocks to gain a stock with higher return and lower risk. Information concerning the stock of a company is based on either internal or external information of the respective company. Internal information of a company is reflected in financial statements such as loss and gain statements as well as balance sheets. External information of a company is also available in the Stock Exchange market; these internal and external factors affect the stock’s return and determine the stock’s price in the market. The respective information remarkably impacts the investors’ decisions. The stock return occasionally might not be a reliable criterion for stockholders to makes decisions. In such cases, the value created by stockholders can serve as the best index for assessing the stock’s status. Book-to-market value ratio under these circumstances might be reflective of the aforementioned value. This ratio can also act as a criterion for evaluation of risk and profitability.

2. LITERATURE REVIEW
In 1993, Fama & French pointed out that size of a company and its B/M ratio play crucial roles in explaining differences between companies’ returns. As extension of their researches, they reached to the conclusion that stocks with small size and large BV/MV ratio tend to gain larger returns compared to the growth stocks. In 1995, Fama & French inferred that the return of portfolios, which were only measureable based on market factor (beta) differ from those in which size of company and B/M ratio had been considered in addition to the market factor.
In a research on predictability of future stock return, Lewelen (2000) investigated whether the empirical models match the assumptions of efficient capital market regarding future returns of
stock or not. In the respective research, the focus was on the industry portfolios. These portfolios represent sectional variations in the return and risk. Also in the same research, portfolios were categorized based on size of company and B/M ratio. It was nonetheless realized that the regressions based on time series might be sensitive to the method by which the portfolios were formed. Company size portfolios are useful for controlling changes in market value which are linked to future risk and return. Also, the portfolios which are based on book-to-market value ratio were used to check the trend of the expected return variations and risk of bad financial state and/or high B/M ratio along the test duration. Results of the study indicated that book-to-market value ratio is able to explain the future return only together with other variables.

Penman et al. (2007) studied effect of book value ratio analysis. In this research, book-to-market value ratio was divided into two elements. The element related to the business unit operation was designated as “operational part” and the element pertaining to company’s finance mechanism was proposed as the “financial part”. The objective was to analyze the interaction of operational and financial parts with the stock’s return. Research results demonstrated that the operational part is positive with respect to the stock’s return whereas the financial part has a negative relationship with the stock’s return.

Clifford (1994) analyzed explanatory capability of beta variables, company’s size, book-to-market value ratio, stockholders’ debt-to-equity ratio, profit-to-market values ratio, and past to future returns ratio. Previously, Fama & French had figured out that company’s size and book-to-market value ratio are more capable of explaining future stock’s return in comparison with other variables. Results of Clifford’s study showed that “book-to-market value ratio” and “size of company” can explain the future return but these two variables are not sufficient to explain the expected returns.

Chui et al. (1998) investigated the relationship between the expected stock returns and beta variables, book-to-market value ratio of normal stock, and company’s size in five emerging markets of Atlantic Ocean Basin. Their findings revealed that book-to-market value ratio of normal stock can explain the temporary diversity of the expected return in Hong Kong, South Korea, and Malaysia.

Barry et al. (1999) studied effect of company’s size and book-to-market value ratio in emergent capital markets. Their results demonstrated that the effect of size is remarkable in certain months of a year whereas effect of B/M is significant and pervasive in the entire duration.

Namazi & Derakhshandeh (2003) conducted a research in 2003 entitled “Application of Sectional Analysis Method concerning Investigation of Effect of Company’s Size and B/M Ratio on Company’s Stock Return and Profitability”. Taking into account the analogous foreign researches, the authors in the respective study attempted to propose the relationship between company’s size and B/M ratio and their effect on stock return as a criteria, which must be utilized in investing decisions in the companies’ stocks. Results of the research for years 1997-2001 were suggestive of a significant and direct correlation among company’s size, return and profitability as well as a significant and inverse correlation among book-to-market value ratio, return and profitability after 1998.

ARAB MĀZĀRYAZDI & ARAB AHMADI (2011) studied the relationships between elements of B/M ratio and future stock’s return in Tehran Stock Exchange. In their study, the relationships between the elements were analyzed after dividing the book value into operational and financial elements and via formation of stock portfolios based on elements of this ratio using regression equations. Their results indicated that when all data are applied in the analyses, the financial element is significantly correlated to the future stock return of the companies. Yet, when the bankruptcy risk factor is involved in the calculations, a converse
result is obtained, and this time, the operational element of book-to-market value ratio exhibits a significant relationship with the future stock return. When research data are classified based on net B/M ratio of operational assets, the results manifest that the operational element is still significantly related to the future stock return for the data in which the respective ratio is smaller than one.

AHMADI & RAHMANI FIROUZJĀIE (2007) analyzed impact of company’s size and book-to-market value ratio on stock return in Tehran Stock Exchange. Their results suggest that market factors, company’s size, and B/M ratio are three factors affecting the stock return in Tehran Stock Exchange. Therefore, use of a multi-variable model could better explain discrepancy of stock return compared to a single-variable model.

Through a study, MOUSAVI & GHĀEDI (2005) investigated the relationship and effects of multiple accounting variables on stock return and profitability of automobile and auto-part manufacturing companies in Tehran Stock Exchange during 1999-2001. The research was conducted on four main subjects: company’s size, book-to-market value ratio, company’s return, and profitability. The research was carried out using a post-event method and was based on previous information taking benefit of Fama & French’s model. Furthermore, Pearson correlation technique was used for analysis of the statistical data. Their results indicated that there is always a positive correlation between company’s size as independent variable, and also return and profitability as dependent variables. The relationship between B/M ratio as independent variable and return and profitability as independent variables is always inverse, which is in accordance with the results acquired by Fama & French (1995), Barber (1997), GATCHEV (1999), PURAS (1998), Barry (1999), and other researchers.

RAHMĀNI & TAJVIDI (2004) studied the relationship between accounting variables and stock return. Some of these variables include price-to-equity ratio (P/E), company’s size, stockholders’ debt-to-equity ratio, stock’s book-to-market value ratio, and sales-to-price ratio per share. The intent of the respective research was also identification and analysis of roles of the aforementioned variables in explaining the stock’s return in Tehran Stock Exchange. In this research, the variables were tested within single-variable models with return as the dependent variable for each year during the “1997-2003” interval. The test results demonstrated that there is a significant relationship between sales-to-price ratio per share and price-to-equity ratio and the stock’s return. In addition, the results of book-to-market value ratio of stock were not consistent during the respective years. No relationship was observed between stockholders’ debt-to-equity ratio and stock’s return. REZAIE BIYUKĀBĀDI (2000) investigated effect of B/M factors and size on profitability of companies adopted in Tehran Stock Exchange. The research results indicated that whether high and low B/M ratio of stock and also small and/or large size of a portfolio can be representative of its high or low profit in the year of portfolio formation based on size and B/M ratio of the stock.

3. RESEARCH HYPOTHESES

Three hypotheses are proposed in the present research in order to examine the relationships between the variables under study. The historical records of the companies and statistical methods will be used to confirm or reject these hypotheses. The research hypotheses are:

1- There is a positive and significant relationship between book-to-market value ratio (B/M) and equity per share (EPS).

2- There is a positive and significant relationship between book-to-market value ratio (B/M) and net profit margin.

3- There is a positive and significant relationship between book-to-market value ratio (B/M) and return on equity (ROE).
The required reports of companies were gathered from “www.codal.ir” website belonging to Tehran Stock Exchange Organization. Analysis methods and correlation coefficient were used for statistical analysis and testing the hypotheses. SPSS software was used for data processing. This research is regarded as a descriptive study. The spatial domain of the research encompasses 15 companies with large B/M ratio and 15 companies with small B/M ratio operating in Tehran Stock Exchange. To collect the needed data for testing the hypotheses, the available information of year 2011 belonging to some Stock Exchange companies transacted in 2012 were selected. As a result, the time duration of the present research is the interval 2011-2012. The statistical population of the research comprises all companies accepted in Tehran Stock Exchange within the aforementioned time interval. The statistical sample of the research consists of two groups: 15 large companies and 15 small companies. The companies were selected based on mentioned method. The 15 large Stock Exchange companies include; Communications, National Copper, MOBĀRAKEH Steel, PĀSĀRGĀD Bank, GHADIR Investments, OMID Investments, GOLGOHAR, CHADORMELO, GOSTARESH, PARSIĀN Oil and Gas, MELLAT Bank, PARSIĀN Bank, SAIPA, MAPNA, SĀDERAT Bank, and BAHMAN Holding. The 15 selected small Tehran Stock Exchange companies were: ITĀLRĀN, GORJĪ Biscuit, MARVDASHT Sugar, LA’ĀBIRAN, ALUMORĀD, INDĀMIN Shock Absorber, PARS PĀMCHĀL, Iran AMLĀH, Iran Carburetor, IRAN YASA Tire & Rubber, MAHĀM Production, TAKIN Corrosion Inspection & Control, NIRU MOHARREKEH Automobile-Manufacturing, BĀFGH Mines, and OFFSET. The objective of the present research is to analyze the relationship between book-to-market values ratio of company’s stock and three instances of profitability ratios in Tehran Stock Exchange.

**Testing the First Hypothesis:**

H₀: There is no significant relationship between B/M ratio and EPS value.

H₁: There is a significant relationship between B/M ratio and EPS value.

According to the results of the following table, if significance level is greater than the error value, the null hypothesis will be deduced; otherwise, hypothesis 1 will hold.

<table>
<thead>
<tr>
<th>B/M ratio</th>
<th>Pearson correlation</th>
<th>EPS value</th>
</tr>
</thead>
<tbody>
<tr>
<td>-.473</td>
<td>Sig</td>
<td>N</td>
</tr>
<tr>
<td>0</td>
<td>Sig</td>
<td>N</td>
</tr>
<tr>
<td>30</td>
<td>Sig</td>
<td>N</td>
</tr>
</tbody>
</table>

According to the results of the table above, H₀ hypothesis is rejected and H₁ (research hypothesis) is confirmed. Significance level is below 0.05. Therefore, a relationship is proved to exist between B/M ratio and EPS value. There is also a significant relationship between B/M ratio and EPS value at confidence level of 99% and the correlation coefficient equals -0.473 and the relationship between B/M ratio and EPS value is negative and inverse. To assess the relationship, the impact level was analyzed as regression model fitting, which will be discussed in the following. Accordingly, in order to analyze and propose a model between B/M ratio (Y) and the EPS (X) value, the processed model is presented after analyzing model fitting indices.
The correlation between independent variables and dependent variable equals 0.473. Determination coefficient was acquired to be 0.224, which value indicates that 22% of EPS value variations are associated with B/M ratio. Since this value does not take into account the degree of freedom, which is equal to 20% in this test, adjusted determination coefficient was accordingly used for this purpose. As value of Durbin-Watson’s statistics lies in the standard interval of 1.5 to 2.5, therefore independence of residuals is inferred. According to the aforementioned indices, the model enjoys the needed fitness. In the table below, significance of regression is tested by F test.

### Table 2: Correlation between variables (regression fitting indices)

<table>
<thead>
<tr>
<th>Correlation coefficient</th>
<th>Determination coefficient</th>
<th>Adjusted determination coefficient</th>
<th>Standard deviation of error</th>
<th>Durbin Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>.473</td>
<td>.224</td>
<td>.196</td>
<td>.33304</td>
<td>1.796</td>
</tr>
</tbody>
</table>

According to the table above, the significance level calculated for this statistic equals 0.008 and indicates significance of the regression at 0.99% p-value. The plotted histogram confirms normality assumption of data for regression model. Thus, the estimated linear regression model is acceptable.

### Diagram: Normality of residuals

![Diagram: Normality of residuals](Image)
Table 4: significance of regression coefficients of B/M ratio value and EPS value

<table>
<thead>
<tr>
<th>Model</th>
<th>Non-Standard coefficient</th>
<th>Standardized coefficient</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>Constant value</td>
<td>.809</td>
<td>.122</td>
<td></td>
<td>6.630</td>
</tr>
<tr>
<td>EPS value</td>
<td>-.481</td>
<td>.000</td>
<td>-.473</td>
<td>-2.842</td>
</tr>
</tbody>
</table>

Dependent variable: B/M ratio

The variable inputted in the regression equation is the main core of regression analysis as shown in table above. Regression equation can be calculated using non-standardized coefficients:

\[
\frac{BV}{MV} = 0.809 - 0.481(EPS)
\]

It can be stated that: with one unit of increment in the independent variable, the dependent variable will increase as much as the above-written multiplier. Or in other words, with one unit of increment in EPS ratio value, B/M ratio will increase -0.481 times the standard deviation; therefore, the correlation is negative.

The t-test for regression coefficients are also represented in this table. The value equals 0.008 for this variable. Consequently, it affected the B/M value.

**Testing the Second Hypothesis:**

H0: There is a significant correlation between B/M ratio and net profit margin.

H1: There is no significant correlation between B/M ratio and net profit margin.

In this hypothesis, B/M ratio and net profit margin are respectively considered as the dependent and independent variables. The test results are as follows

<table>
<thead>
<tr>
<th>B/M ratio value</th>
<th>Pearson Correlation</th>
<th>Net profit margin</th>
</tr>
</thead>
<tbody>
<tr>
<td>-.261</td>
<td>Sig</td>
<td>N</td>
</tr>
<tr>
<td>.163</td>
<td></td>
<td></td>
</tr>
<tr>
<td>30</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

According to the results of the table above, H0 hypothesis is confirmed and H1 (research hypothesis) asserting existence of a relationship between B/M ratio and net profit margin is rejected because the observed significance level equals 0.163 and is larger than the acceptable p-value (0.05). Also, due to poor correlation between B/M ratio and profit margin, it can be
stated that the profit margin had no effect on B/M, and as a result, there was no need to perform regression analysis. Based on the abovementioned correlation coefficient and probability value = 0.261, no strong linear correlation holds between the two variables. However, H₀ hypothesis is not disproved due to probability value=0.163 in Analysis of Variance, which is larger than significance level p-value= 0.05. It means that there exists a significant relationship between B/M ratio and net profit margin.

**Testing the third hypothesis:**

H₀: There is no significant relationship between BV/MV ratio and ROE.

H₁: There is a significant relationship between BV/MV ratio and ROE.

In this hypothesis, the dependent and independent variables respectively are B/M ratio and ROE. The test results are shown below.

<table>
<thead>
<tr>
<th>B/M ratio</th>
<th>Pearson’s correlation</th>
<th>ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>-6</td>
<td>Sig</td>
<td>N</td>
</tr>
<tr>
<td>0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>30</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

According to the results of the table above, H₀ hypothesis is rejected and H₁ hypothesis asserting existence of relationship between BV/MV ratio and ROE is confirmed because significance level is smaller than 0.05.

As observed, there is a significant relationship between BV/MV ratio and ROE and the correlation coefficient equals -0.600; the relationship between BV/MV ratio and ROE is negative and inverse and roughly strong.

The regression model was analyzed to investigate the level of impact based on fitness, which will be discussed in the subsequent parts.

**Regression Model Fitting:**

In order to analyze and propose a model between B/M ratio (Y) and stockholders’ debt-to-equity ratio (X), the processed model is offered after analyzing the model fitness indices as mentioned in the following table.

<table>
<thead>
<tr>
<th>Correlation coefficient</th>
<th>Determination coefficient</th>
<th>Adjusted determination coefficient</th>
<th>Standard deviation of error</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>.600</td>
<td>.361</td>
<td>.338</td>
<td>.30232</td>
<td>1.759</td>
</tr>
</tbody>
</table>

The correlation coefficient between the dependent and independent variables is 0.473. Determination coefficient was obtained 0.361, which indicates 36% of B/M ratio variations are correlated to the ROE. Since this value does not take into account the degree of freedom,
the adjusted determination coefficient is therefore applied for this purpose, which equals 34% in this test. As Durbin-Watson’s statistic lies within the standard interval 1.5 to 2.5, the independence of residuals is inferred. Based on the aforementioned indices, the model has the needed fitness. In the table below, regression is computed using F-test.

Table 8: F-test (Analysis of Variance) for significance of regression

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of squares</th>
<th>Degrees of freedom</th>
<th>Mean sum of squares</th>
<th>F-statistic</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>1.443</td>
<td>1</td>
<td>1.443</td>
<td>15.786</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>2.559</td>
<td>28</td>
<td>.091</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total sum</td>
<td>4.002</td>
<td>29</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

According to the table above, the calculated significance level for this statistic is equal to 0.000 and implies significance of regression at 0.99% p-value. The plotted histogram for the regression model approves the normality of data. Thereby, the estimated linear regression model is acceptable.

Diagram: Normality of residuals

Table 9: significance of regression coefficients of B/M ratio and ROE

<table>
<thead>
<tr>
<th>Model</th>
<th>Non-standardized coefficient</th>
<th>Standardized coefficient</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>Constant value</td>
<td>.864</td>
<td>.105</td>
<td></td>
</tr>
<tr>
<td></td>
<td>ROE</td>
<td>-.813</td>
<td>.205</td>
<td></td>
</tr>
</tbody>
</table>

Dependent variable: B/M ratio
The variable incorporated in the regression equation is the main core of regression model as included in the table above. The regression equation can be calculated using non-standardized coefficients column as below:

\[
\frac{BV}{MV} = 0.864 - 0.813(\text{ROE})
\]

It can be stated that the dependent variable will increase as much as the above-written multiplier if the independent variable undergoes one unit of increment. Consequently, the relationship is negative. T-test of regression coefficients is also included in the same table; this value equals 0.000 for the respective variable indicating its effect on B/M ratio.

4. CONCLUSION

The present research examined existence of a significant relationship between book-to-market value ratio and profitability ratios. The former research works which investigated the inverse relationship of this ratio with other financial variables such as stock return and capital structure of the company suggest that there exists a significant relationship between the respective ratio and some of fundamental financial concepts. It was realized in the current research through testing the hypotheses that there is a significant and inverse relationship between this ratio and ROE ratio as well as EPS value; this finding is in agreement with other studies conducted in this scope, corroborating the associated hypotheses. Nevertheless, no significant relationship was observed between B/M ratio and profit margin; hence, the third hypothesis is disproved. The results of the present study can help the investors in their investments and decision-making. Based on the current research results, the investors are recommended to incorporate the book-to-market value ratio of the respective stock in their analyses.

LITERATURE

5. Clifford.s.a.(1994)"variables that explain stock returns:simulated and empirical evidence “
MEXICO: TAX SYSTEM FOR GROWTH AND ECONOMIC DEVELOPMENT

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inzunzap@uas.edu.mx

ABSTRACT
In this research, we start from the idea that the tax system of a country is closely related to the degree of state intervention and economic policy that applies. In this article, it is recognized that from little more than thirty years, Mexico's tax system has been characterized by low tax burden, high evasion and tax inefficiency, and very high tax inequity. These features are related to the neoliberal economic policy that has prevailed since the beginning of the eighties: a weak and permissive, flexible and deregulated state, and highly disciplined. Now, in the same way that Mexico retained throughout his life traces of an adverse economic policy, also suffers the fate and future of their economic development. In the descriptive research method with mixed approach, under which exposes and analyzes statistical data applies. Reveals the situation that has prevailed upon fulfillment of the policies derived from the Washington Consensus and through consultation occurs documentary shows that Mexico requires reducing economic and social inequality; therefore, it is considered necessary to apply a progressive tax system, either from the perspective of spending and tax revenues. Hence, from the analysis of the Mexican tax system, the nature and composition of its structure, as well as tax changes observed for economic growth over the last three decades is explained. The main theories of taxation are revealed and analysis of statistical data is exposed for design fiscal policy strategies that foster economic development. The study focuses on the possibility of specific tax reforms. The choice of the period 1990-2014 to obtain average data that enable the tax system of the country, according to the level of the tax burden to estimate the possibility of mitigating the high economic and the low volatility of GDP, considering an idea more accurately the strengths and weaknesses of the Mexican real tax system.

Keywords: Taxation, Economic Growth, Tax Policy, Tax Systems.
JEL Classification: E62, H23, H21, F43.

1. INTRODUCTION
In Mexico, from just over 30 years ago, the tax system is characterized by low taxation, high evasion and inefficiency, and high inequality. Relate These features the State Neoliberal model, has prevailed since the beginning of the eighties: a state highly disciplined and permissive, weak, flexible and deregulated, with a high rate of corruption, which is functional to trade liberalization and financial, generating adverse outcomes for the country. Importantly to study the Mexican tax system, will identify its advances and retreats; which, help you think about fiscal conditions and tax that the Mexican government has determined to achieve sustained growth in all sectors of the economy, which, should affect a better income distribution and economic and social development. It is considered a landmark study for the Government and Public Sector Economics, given that, given the high levels of economic inequality, a window of discussion about tax progressivity of the tax system opens. It starts from the idea that a tax system should
guarantee fund economic and productive activities of State for sustained growth and improve income distribution to mitigate the high rates of inequality. However, it also recognizes that three decades of operating a loaded fiscal policy of fiscal discipline, there has been a high containment of productive public spending and an increase in consumption taxes.

2. THE TAX SYSTEM
The importance of the tax system in fiscal policy is based on three thematic areas: 1. The tax system as a source of financing of public spending, 2) Problems of tax technical and legal application, and 3) The tax system and its impact on the economy.

a) The tax system and public finances: Studies examining the role of the tax system as a source of financing public spending.

b) The tax system and tax laws: Analysis of specific problems about mechanics and tax technique, based on this, the calculation and determination of taxes arising from tax regime of taxation to which they relate.

c) The tax system and economy oriented to describe and quantify the effects of taxes on the economy and development research: the gap between potential collection and effective (evasion), its causes, the analysis of so-called tax expenditures, the distribution of the tax burden, among other economic aspects.

Given these themes, Martner, et. al. (2013), consider the case of countries like Mexico, the challenge is to enhance the catalytic role of the public sector with high social returns policies, avoiding displacement effects associated with inadequate financial management, a inadequate fiscal pact that distortion you the tax system.

2.1. Taxes and fiscal pact
Globally, there is a general condition that justifies the emergence of taxes. These arise from the need to activate the economic and financial life of the state and formalized under a social and fiscal pact.

Based on this principle of analysis, it is understood that the tax system is a fundamental socio-political agreement that legitimizes the role of the State and the scope of responsibilities of the federal government in economic circle from a social pact that is linked to the strict economic, financial and taxation, providing a strong fiscal component that commits it to mean a fiscal pact.

However, from a political and social vision, this fiscal pact is based on the relationship between the state and citizens, expressed in the will of the majority of people, companies and households to pay more taxes to the extent that optimize the quality of public health services, education and security, and have less corruption and tax evasion control (ECLAC, 2013). In this regard, Martinez, et al (2013) tell us that spending on education, health, social exclusion, housing, family and children, pensions and unemployment, increase macroeconomic efficiency; to the extent that favor formality, quality employment, participation rates of women and youth in the labor market and employment of persons excluded.

Many types of social transfers, in addition to direct spending on education and health, have the characteristic of being potentially progressive and pro-growth: food and nutrition security, social protection and the environment, housing, culture and recreation (see Table No. 1).
TABLE No. 1

ECONOMIC IMPACTS OF SOCIAL FUNCTIONS

<table>
<thead>
<tr>
<th>Social function</th>
<th>Examples of economic impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>The theory of human capital is the main theoretical framework under which you can see that education has economic impact. Education fosters productivity of workers, making them more capable and qualified for the labor market, therefore has an impact on economic growth.</td>
</tr>
<tr>
<td>Health</td>
<td>Investing in health results in increased production capacity, with benefits for people and for the production units.</td>
</tr>
<tr>
<td>Food security and nutrition</td>
<td>Both undernutrition and overweight and obesity generate personal and social costs, but its decline means direct savings to the economy of the countries in health, education and particularly in productivity. In turn implies incentives in key sectors of the economy, such as production and distribution of food.</td>
</tr>
<tr>
<td>Social protection</td>
<td>By ensuring a level of resources to people and mitigate the effects of the economic crisis and unemployment, facilitates the existence of a minimum level of consumption in the population, injecting resources directly to the market by way of demand. It also has a direct effect on employment, to the extent that its functions is the regulation of the labor market and thereby promote decent employment.</td>
</tr>
<tr>
<td>Protection environment</td>
<td>Through methods for reducing pollution, environmental protection can have an economic impact. There is an impact in the construction sector with the “greening” of homes and buildings.</td>
</tr>
<tr>
<td>Housing and community amenities related</td>
<td>Indirect impact through spending on housing affects the construction sector, which has a significant share of GDP in the region. The public sector creates partnerships with the private sector for the implementation of infrastructure projects which include housing.</td>
</tr>
<tr>
<td>Culture and recreation</td>
<td>The production of cultural goods and services usually leads to activation of private economic activities. For example through the remuneration paid in private employment.</td>
</tr>
</tbody>
</table>


It is under this scheme, we find that the quality of public spending has a strong link with taxes, and therefore with tax systems. In addition, the tax system has to observe with greater weight ratio of public social and productive spending with taxes in order to achieve sustainable development.

3. THE MEXICAN TAX SYSTEM

The Mexican tax system is set in a fiscal policy that favors indirect taxation and consumption, rather than the imposition to the utility and capital. In the last thirty years, there has been more emphasis on the collection of Value Added Tax (VAT) and the Special Tax on Goods and Services (IEPS) and other indirect taxes, and the granting of schemes clientelistic that privilege waivers, exemptions and special regimes that prevent big companies pay their taxes with equity and fiscal responsibility. It is recognized, then it gains made by the Mexican tax system have been poor relative to the distribution of income and economic growth. We understand that it was not significant in levels of economic growth (average 2% annually), and therefore it has been inefficient and unfair. Hence, the poor distributional effects of taxes, decreased tax base, tax regressive, tax inequity and weak income tax and capital are the main issues to resolve.

3.1. Who promotes the Mexican tax system?

Recurrently in Mexico, professionals, workers, employers and the general public are overwhelmed by the constant tax changes imposed by the tax reform every year. In this, the overwhelming changes are felt, after passing through the inertial uncertainty involved pending
tax rigidity and tax severity. However, in this scenario, also reach us the following questions: What essential objectives lead the tax system?, Why is designed tax system?, Who benefits? We know that the tax system is not a work done at random but a thoughtful and scientifically designed to promote the growth and development of a country, and especially to benefit the majority of citizens. While tax reforms are an ongoing process that has been analyzed and observed for over five decades, this time is taken up and pursue objectives with emphasis on distributional issues relating to taxation, in close and constant relationship with the spirit of tax reforms implemented in Mexico since the early 80's. During the last thirty years are observed in Mexico major changes in taxation and fiscal matters, most of which correspond to a "first generation of tax reforms" initiated in the heyday of the Washington Consensus. However, many of the main problems or weaknesses of the Mexican tax system persist and worsen, reflecting a slow and complicated solution. The macroeconomic context of Mexico, led by the principles of "consensus", have guided the government to adopt the changes or reforms; hence, arises the possibility of each year, a new agenda for reforms to tax, on the one hand, secure the achievements; and, on the other, make the necessary changes in the country, not only to improve the quality of tax policy, but the tax structure to adapt to new national and international economic conditions. In that sense, the work of Fnochietto and Pessino (2010: 69) have noticed that in most Latin American countries a level of tax revenue that is below the potential level would correspond according to the degree of is collected economic development of the same, ie exhibiting low levels of tax effort. In the case of Mexico, it appears that the current tax structure, presents a typical strong bias towards indirect taxation and consumption, which determines, in many cases, the regressivity of the tax system as a whole. The tax structure in Mexico, asymmetric disparity reflects direct and indirect taxes and other contributions that exposes the regressive effect on income distribution (Goñi; et al; 2008). In Mexico, the tax system is not only guides the collection of indirect taxes, but also is represented by different rates, preferential regimes, high waivers and exemptions, special treatments and subsidies, which explains the low levels of revenue and tax downtime. The existence of a large number of differential tax treatments involving the tax waiver from the State and distortion to the basic principles of equity among taxpayers, represent a significant amount of potential tax revenues whose resignation and resignation by the State generally not is sufficient justification. Another experience that exists in Mexico is the lowest relative participation of individuals with regard to the legal entities (companies) in total tax collection. Hence, the low weight of the tax on personal income is taxed in Mexico, unlike the income tax to be taxed in the OECD countries. The justification of the tax system is the progressivity which lies in the collection of income taxes or utilities of individuals and corporations, but especially in the redistributive effect of taxes on capital and utilities. To this must be added that the Mexican tax system has been transformed dramatically over thirty years. As the tax system has diversified into Mexico, the tax structure has evolved significantly between 1980 and 2014. Consequently, Gómez Sabaini and Moran (2013: 10) suggest that "could be better conditions and more space to boost tax changes leading to tax reforms framed on social cohesion and fiscal sustainability" designed to ensure obtaining more resources to finance productive and social costs, to consolidate macroeconomic stability, and improve their impact on income distribution. It is observed that in Mexico, heterogeneity of public policies that make life in the public sector, have experienced significant changes regarding the level and structure of tax revenue collected. The sustained increase in the average tax burden shows some regularity; and at the same time, overwhelming hidden dynamics and divergent deserve to be studied. We must remember the tax gap between our country and the countries of the OECD. Notably, this gap is characterized inter alia by prosecutors and tax revenues that make up the respective tax systems, but reflect major differences due to the comparatively higher
values. For Gomez Sabaini and Moran (2013), tax structures in Latin America exhibit several common characteristics that contrast sharply with those observed in most developed countries. Consider the size and characteristics of these differences, it is crucial to identify areas of opportunity that require greater needs and demands of new tax reforms outweigh the hitherto existing. In Mexico, since the early 80's the "neoliberal revolution of fiscal policy" (Jenkins, 1995), implying that in the years following a change was given in the main objectives that guided its tax policy. Thereafter, tax policy focused diversification of tax instruments, and the design was placed on tax efficiency, horizontal equity and adequacy of tax revenue, minus courage and strength to the objective of redistribution income. From there, fiscal policy has faithfully followed the recommendations of international organizations like the World Bank and the International Monetary Fund, the makers of fiscal and tax policy in Latin America. The orientations of these institutions, gave strength to the neoliberal model by proposing an aggressive reduction and extinction rates or tax rates to international trade, considered as an inefficient source of tax revenue that caused the limitations on the export of local production and international resource allocation.

3.1.1. Changes in the Mexican tax system
Changing economic and social circumstances facing the country in the last three decades, abandoning the entrepreneurial role of the state, increased informality of labor markets, rising unemployment and poverty; coupled with the increasing concentration of income in a few people have left their stamp on the tax system in Mexico, has undergone profound structural changes during the period of application of the model IOE. These changes were not harmonic, but rather, shown which have been unbalanced and permanent. Unbalanced, because they have failed the balance provided distribution of income between socioeconomic strata to acquire a degree of social consensus, nor have been established patterns decisive participation of the different levels of government in shaping the tax burden. Continuous, because the process in the fiscal reform, in the tax structure and administration did not achieve the basic goal of raising enough to meet the demand for public expenditure and achieve fiscal sustainability. Even when in the last thirty years, there have been changes to the Mexican tax system, These changes have been based more efficient collection of taxes. These changes have been made to achieve simplification and ease of paying taxes. Another major change in the tax system has been the creation of the Tax Administration Service. It was also necessary to create the first reform mechanisms to achieve certain objectives such as greater neutrality and horizontal equity, and the harmonization of the tax system with major trading partners; strengthening tax revenues through broadening the tax base; and control of evasion and tax avoidance. However the constant changes, there have been few results, highlighting the complex issue of simplification, administrative modernization and fiscal harmonization with municipal, state and federal structures.

4. LOADING AND TAX BURDEN
Of the factors affecting the tax system, both the tax burden as its structure, are becoming increasingly important; however, we found that two variables are crucial to strengthen or to thin. On the one hand the fiscal capacity and secondly, how the collection of these resources are distributed. Regarding the tax burden, we understand that one way to assess whether the level of tax collection and structure are "adequate" is to compare the relationship between taxes and GDP to demonstrate the financial situation of the country. In different studies on the financial situation of Latin American countries shows that the potential level of tax collection of countries is significantly higher than cash. According to recent studies Sabaini Gomez Jimenez and Podesta (2010), only Argentina, Brazil, the Plurinational State of Bolivia and
Nicaragua, there is a high tax burden in relation to per capita GDP, while in other countries Latin America, register the tax pressure clearly lower than they should have, according to their levels of development. This means that there is scope to increase government revenue and thus, the redistributive capacity of the State, through the provision of more resources and funding. The funding provides some fiscal space to introduce countercyclical measures in economic and social policies in a context of declining tax revenues and a demanding service of public debt (ECLAC, 2010: 25). Providing resources could be done through tax revenues to foreign transactions, from commercial and financial, but we believe that there is clear evidence that not apply, let's see what offers the reality. According to Jimenez and Gomez Sabaini (2009: 27), "the level of tax burden is a key indicator of the possible effects of the crisis on tax collection, and places the countries with the lowest tax burden in the group the most exposed to it". In this sense, Mexico, is considered a country with low tax and tax burden that barely meets just over 10% of GDP, while for example Brazil is a country with a tax burden of 36.2%, the main difference is the size public sector, Brazil in its fiscal policy guidelines are implemented to preserve their public companies, and their exploitation not only allows you greater revenue, but also higher tax revenues.

### Table No. 2

**LATIN AMERICA AND THE CARIBBEAN (17 COUNTRIES): TAX BURDEN, 2007**

<table>
<thead>
<tr>
<th></th>
<th>Less than 15%</th>
<th>Between 15% and 23%</th>
<th>Over 23%</th>
</tr>
</thead>
<tbody>
<tr>
<td>MEX</td>
<td>11.7</td>
<td>12.5</td>
<td>12.9</td>
</tr>
<tr>
<td>GTM</td>
<td>14.4</td>
<td>15.0</td>
<td>15.8</td>
</tr>
<tr>
<td>PRY</td>
<td>16.6</td>
<td>16.0</td>
<td>16.6</td>
</tr>
<tr>
<td>ECU</td>
<td>17.0</td>
<td>17.2</td>
<td>17.2</td>
</tr>
<tr>
<td>SLV</td>
<td>20.1</td>
<td>21.3</td>
<td>21.9</td>
</tr>
<tr>
<td>COL</td>
<td>24.1</td>
<td>22.5</td>
<td>24.1</td>
</tr>
<tr>
<td>DOM</td>
<td>29.1</td>
<td>36.2</td>
<td></td>
</tr>
<tr>
<td>PAN</td>
<td>17.0</td>
<td>20.1</td>
<td>21.3</td>
</tr>
<tr>
<td>VEN</td>
<td>21.3</td>
<td>21.3</td>
<td></td>
</tr>
<tr>
<td>PER</td>
<td>21.9</td>
<td>22.5</td>
<td></td>
</tr>
<tr>
<td>BOL</td>
<td>24.1</td>
<td>24.1</td>
<td></td>
</tr>
<tr>
<td>CHL</td>
<td>36.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NIC</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CRI</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>URY</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ARG</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>BRA</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


This low tax burden is the lowest in three decades. It is attributable to tax collection deficiencies of structural character that are enhanced in times of crisis, coupled with the debt payment obligations that prevent spending is expansive. Note that at a low tax burden and its tax case, means less spending allocations; whereas higher taxation (involving more public resources) and greater tax burden (which implies a higher tax burden), mean more revenue capacity and thus greater reallocation of resources In Latin America and the Caribbean not only collects tax little, but it also raises bad, says a study by ECLAC (2010). In the case of Mexico, occurs equal, we see that less than a third of the collection consisted of direct taxes (income tax, flat tax, etc.), while the bulk of the burden falls on consumption taxes (VAT, IEPS, ICExt., IDE among others) and other indirect taxes, affecting the poor people. Thus, the difference in the levels of tax burden among OECD countries and Latin America can be explained mainly by the low tax burden on income and wealth in the region, since the level of taxes consumption is quite similar. While the collection of corporation tax is similar (slightly more than three points of GDP in the OECD), there are significant disparities in income tax (0.9 percent of GDP in Latin America compared to almost nine points of GDP in the OECD).

### 4.1. TAX SYSTEM AND THEORY OF TAXATION

Derivative of public finances, we need the tax system is formed by the set of taxes in force in each country, at a certain time and dynamically. According to Queralt et al (2001: 280), "a tax system is a systematic and coherent set of taxes that cater to the tenets of constitutional principles, help to achieve a sufficient level of income with which to meet public needs serving as an essential instrument of economic policy". In the opinion Serra (2006: 190) "The
effects of taxation on the economy depends on how it is collected, how taxes are collected and how the taxes collected are used", but these three are closely related, because their complexity, are usually studied independently. This section summarizes both the theoretical and empirical literature on these topics.

Meanwhile, Feniochietto (2006 and 2010), notes that a tax system is all taxes that apply in a country in a given time, and configuration due to many political, economic, historical, cultural and other reasons in each country. According Dario Gonzalez (2009: 9), "Latin America, although they have tried to apply an orthodox tax policy, numerous reasons have prevented their implementation effectively and efficiently". These reasons are considered by the limited capacity of control by the tax administration, coupled with high government spending and high levels of evasion caused by the size of the informal economy; reflecting a low level of tax awareness and a high level of fraudulent maneuvers, creating inefficiencies in the application of orthodox fiscal policy.

These events encourage that much of the income, wealth or consumption, have no effective taxability, motivating formulators of fiscal policy to adopt orthodox measures for a share of the escapees income, ie increasing consumption taxes, or simply increasing tax rates or designing new income taxes.

A study of Martner et al (2013) reveals that in Latin America and the Caribbean, over 60% of tax revenues (excluding social security) comes from indirect taxes (excise taxes), while about 37% of the tax burden levied on income or property. In this sense, in the case of Mexico, 65% of the total earnings of the federal government are tax revenues (see figure no. 1), while the total revenue of the federal government, 48% are income levied on the capital and earnings, and 52% gravel consumption (see figure no. 2).

![Chart No. 1](source: Based on data from the Ministry of Finance and Public Credit)

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In this graph it can be seen that of the total earnings of the federal government of Mexico, 30% are recorded to capital income and profits, while 33% recorded consumption and 37% corresponds to contributions by services to the public finances. Hence, it can be inferred that 70% are contributions that affect consumption taxpayers. The structure of the Mexican tax system is heavily loaded to consumption taxes. This indicates that in Mexico is complicated encourage savings and investment of citizens.

Based on these data, we understand that the Mexican tax system lacks neutrality and lacks the principle of revenue capacity. The level of the charge to capital and profit is insufficient to promote progressive conditions in the tax system.

This is reinforced by Considering That tax systems aim to boost savings, investment and economic growth. Hence in Mexico is necessary to design taxes to observe the principle of neutrality; However, according Sanz-Sanz y Sanz (2013), the absolute tax neutrality is impossible and even undesirable.

To that taxes are designed to meet the principle of neutrality, must balance the income via levies on capital and earnings they are the product of the economic productivity of operators and not of the Needs of consuming of subsistence or service of survival.

4. CONCLUSION

due to the undesired effects and highly adverse of the model "of development" which was driven to the late twentieth century, are have revalued significantly by the scientific
community and international organizations, the objective treatment of the distributional problems, calls for the "equitable distribution" and "social inclusion" so, for routing the State to the estabilidad macroeconomic, and to the redistribution of income, involves studying the taxation sistem and the resource mobilization.

With this research, we infer that the tax system should be implemented to improve saving economy and investment in economic agents, and hence economic growth, however, this does not happen in Mexico; since most of the taxes and fees, make the tax system is to tax consumption. We note that Mexico has a tax system that does not keep the principle of neutrality by taxing consumption mostly to the capital.

Nationally, tax revenues fell, but not the tax burden for most individuals, also increased foreign borrowing and was decreased the productive public spending (aspects further limited growth), thus increasing the inequality and fiscal volatility, which prevents fiscal cohesion and tax certainty of the economic agents.

The results analyzed, report that even when the difference between taxes on capital (48%) and consumption taxes (52%) is conservative, that 4% still represents an important part of the income of the federal government. Moreover, if we consider the nontax revenue, represented by 35% of the total income of the federal government, as part of the indirect contributions, we must 39% of federal government revenue comes from taxing consumption; therefore, we have that 74% of federal revenues directly affect the consumption of families, professionals, workers and employers.

These results show us the incompetence or unwillingness of the Mexican government to increase public revenues via direct taxes levied on the capital and profits; what has contributed to the realization of tax changes by implementing new taxes or new methods of taxation and exemption from taxation. In the tax system, we can find tax regimes facilities and innovative tax instruments, as is the corporate tax rate only, extinct last year 2010, as well as the tax on cash deposits.

The reaudatoria state capacity, may be verified by "the ability of the tax system to correct the unequal distribution of income, depending on the volume of collected resources and the fee structure by income level, but also evasion tax income and the number of exemptions "CEPAL (2014: 282).

However, demonstrating the reaudatoria ability the Mexican State, which means display the fiscal pressure increases also identify the causal relationship between fiscal and economic policies. This involves establishing relations of the actions of the state in the economy ranging from income generation, application of spending and hiring public debt to grow; therefore, it is unavoidable, study the influence of the level and composition of public expenditure and revenue in the macroeconomic cycle and the trend of medium and long-term GDP.

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2. ECLAC (2014), Time for equality for closing gaps, opening trails, United Nations Economic Commission for Latin America and the Caribbean Santiago de Chile.
FISCAL DECENTRALIZATION AND THE ROLE OF LOCAL GOVERNMENT IN LOCAL ECONOMIC DEVELOPMENT IN THE REPUBLIC OF MACEDONIA

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ABSTRACT
The process of decentralization in Macedonia brought many responsibilities for local governments. With the Law on Local Self-Government were established and transferred responsibilities of local importance, which were placed under the jurisdiction of state institutions and which local authorities should perform independently.

In this paper the Local Economic Development (LED) is analyzed as one of the first obligations transferred to the local level. The focus is placed on local authorities as a significant role in LED and their impact regarding on their natural resources, municipal infrastructure, their fiscal autonomy, financial capacity, administrative capacity, educational structure of people, etc. We analyzed some aspects of LED such as the level of fiscal decentralization, the legal and institutional framework, the support of the central government, capital investments, etc. to conclude that the major units of the local government in Macedonia implement the responsibility for local economic development at a low rate compared to the other responsibilities that are delegated to the municipalities and that the municipalities are still dependent on central governments activities.

In order to analyze the impact of local government, in this paper we included a study for the municipality of Ohrid as a main tourist center in the Republic of Macedonia. In the study, there are presented the effects from the budget policy on the tourism as a main potential of local economic development.

Finally, taking into consideration the results of the survey, in the paper there are presented recommendations that can serve as a basis for policymaking aimed to stimulate and support local and regional economic development in the Republic of Macedonia.

Keywords: decentralization, local economic development, local government, budget policy

1. INTRODUCTION
Fiscal decentralization and local government development are among of the priorities stemming from the Accession Partnership of the Republic of Macedonia with the EU, the realization of which opts for careful and phased approach, which is successfully implemented by the Government.

Since the beginning of decentralization, municipalities recognized local economic development as a competence that can largely affect the overall development of the municipalities, but also as a measure that will improve the weak economic situation of the population through the implementation of local projects.

Local economic development (LED) is seen as one of the most significant ways of decreasing poverty and unemployment as well as providing economic and social welfare, improving living conditions.
Macedonia for several years successfully is implementing the decentralization process. Due to the low quality of life, mainly caused by the 1990s economic crisis, the country was urged to take some steps towards establishing a functioning market economy and improving the living standards of its citizens. This led to the understanding of the local government that the creation of policies for economic development and growth is not only a duty of the central government but also a responsibility of the units of the local government through their influence and performance. With the process of decentralization of the local government, implemented in June 2005, with the Local Government Law within transferred responsibilities, the local economic development is central on the list of transferred responsibilities. However, even after seven years since the implementation of the second phase of the fiscal decentralization, a small number of municipalities are capable of realizing this important responsibility. The reasons for the lack of implementation of the responsibility that we identified through survey in the larger municipalities, are various, such as: the low level of fiscal decentralization, the lack of financial means, responsibilities not clearly defined between the central and the local government, the municipalities do not own construction ground, unqualified local administration workers, etc.

In this paper, it is analyzed the implementation of the new decentralized concept of local self-government and how municipalities fulfill this responsibility. Besides introduction and conclusion, the paper also contains three more parts.

The first part of the paper presents a brief overview on the implementation of the decentralization in the Republic of Macedonia, the level of its implementation and the local economic development as one of the transferred responsibilities. In the second part the focus is placed on the legal and institutional framework as a theoretical base for successful implementation of local economic development where goals and regulations are clearly defined.

It is the third part that elaborates in details the role of the local government, its activities and responsibilities and whether local governments are autonomous and capable of implementing local economic development as their responsibility. In this part it is presented the case of the Municipality of Ohrid, as a unit of the local government, its budget before and after decentralization and its contribution for the local economic development through the capital investments.

At the end, recommendations and measures for further stimulation of the local economic development are pointed out.

2. LOCAL GOVERNANCE AND DECENTRALIZATION IN THE REPUBLIC OF MACEDONIA

The policy framework for the local government decentralization was established with the adoption of the Strategy for the Reform of the Local Self-Government System in May 1999. The Strategy was aimed at building local governance based on principles of democracy and decentralization. This Strategy was further supported by the adoption of the Ohrid Framework Agreement in 2001 as well as the development and adoption of a set of constitutional amendments and laws on decentralization by the Macedonian Parliament, which transferred a wide range of competences to the local government such as the management of primary and secondary education, increased responsibilities in urban planning, local economic development, social services and cultural institutions and activities (Novovic, 2011). The implementation of the decentralization process, however, was initiated in June 2005 following the adoption of the Law on Local Self-Government, which stipulated the transfer of responsibilities from the central to the local government. Consequently, according to the Law,
the local economic development was one of the responsibilities being transferred to the local level based on which the local government has become responsible for:

“The Local Economic Development – planning of the local economic development; establishment of the development and structural priorities; implementing a local economic policy; support to the development of small and medium-sized enterprises and entrepreneurship at the local level and, within that context, participation in the establishment and development of the local network of institutions and agencies for promoting partnership;” (Official Gazette, no. 5/2002).

Based on the Report on the Implementation of the Programme for the Implementation of the Decentralization Process and Local Self-Government Development in the Republic of Macedonia 2011-2014 and the analysis of all data used in its preparation, the progress achieved and the challenges for further action are divided into five groups according to the Programme chapters as follows:


<table>
<thead>
<tr>
<th>Programme Chapter</th>
<th>Progress Achieved and Major Challenges</th>
</tr>
</thead>
<tbody>
<tr>
<td>The legal and institutional framework for the devolution of powers and resources</td>
<td>Within the framework of the current Programme Chapter, 54% of the anticipated activities have either been completed or their implementation has commenced. The inception of 33.3% of the activities has been postponed, while 14% of the activities have been removed from the Action Plan due to the matter being covered by another law.</td>
</tr>
<tr>
<td>Fiscal decentralization</td>
<td>Within the framework of the current Programme Chapter, all anticipated activities have either been completed or their implementation has started.</td>
</tr>
<tr>
<td>Improved delivery of local services</td>
<td>Within the framework of the current Programme Chapter, 56% of the anticipated activities have either been completed or their implementation has commenced. The launch of 26.0% of the activities has been postponed. 9% of the activities have been removed from the Action Plan due to activity overlapping with another project, while for 9% of the activities the authorised institution is still to be identified.</td>
</tr>
<tr>
<td>Development of the administrative capacities of LSGUs</td>
<td>Within the framework of the current Programme Chapter, 86% of the foreseen activities have either been completed or their implementation has commenced, while the inception of 14.0% of the activities has been adjourned.</td>
</tr>
<tr>
<td>Local democratic practice and citizens’ participation in local decision-making</td>
<td>Within the framework of the current Programme Chapter, 67% of the envisaged activities have either been completed or their implementation has begun, while the inception of 33.0% of the activities has been adjourned.</td>
</tr>
</tbody>
</table>

However, there is still a lack of implementation of the transferred responsibilities by the local government due to the following reasons: there are lots of challenges to be met in relation to the fiscal decentralization, the insufficient local economic development due to the lack of financial means, a lack of marketing strategies for concluding public-private partnerships for public service delivery at local level, a lack of marketing strategies in the promotion of the advantages and the conditions for the investment in the local community etc.
3. LEGAL AND INSTITUTIONAL FRAMEWORK FOR THE SUPPORT OF THE LOCAL ECONOMIC DEVELOPMENT

To understand the role and the responsibilities of the local government it is necessary to briefly review the Law on Local Government introduced into Macedonia’s local governmental system. The responsibilities of the local government have been increased with the adoption of the Law on Local Self-Government in 2002. To be more precise, article 22 of the Law stipulates the responsibilities being transferred to the local government, whereby among the first obligations transferred to the local level is the local economic development. According to this Law, the municipalities are given the opportunity to create and implement policy strategies concerning LED. It also enables the cooperation between the municipalities, the private sector, NGOs for the purpose of stimulating the local economic growth.

Additionally, the Law on Equal Regional Development from 2007 (Official Gazette, no. 63/2007) is also an integral part of the legal framework regulating this issue. This Law defines the goals, regulations and holders of the policy on planning the economic development, the financing and allocation of funds for evaluation of the equal regional development and monitoring of the development plans and project implementation etc.

Furthermore, the Law on Financing the Units of the Local Self-Government (Official Gazette, no. 61/2004) plays a significant role in the local economic development. According to this Law, “The sources of financing of the municipality are: its own sources of income, grants of funds from the Budget of the Republic of Macedonia and the budgets of the funds and loans.” (The Law on Financing the Units of the Local Self-Government, art.3). This Law also stipulates that the implementation of the fiscal decentralization as “…a mechanism for financing the municipalities which is transparent and based on objective criteria and measures.” (The Law on Financing the Units of the Local Self-Government, art.44).

The Law on local government significantly increases the responsibilities of the local units and LED is one of the first obligations transferred to the local level. The responsibilities of the local economic development is the same in all municipalities in the urban as well as the rural municipalities and the city of Skopje as a separate unit of local government, regardless of the large development regional and municipal disparities in the domain of the economic development. As regards the institutional framework, after the implementation of the decentralization, the transfer of the responsibility for local economic development to the local government has led to the formation of special sectors for local economic development within the urban municipalities with greater financial and staff capacities for the purpose of implementing activities related to the local economic development. In the rural municipalities, however, no special units for LED have been formed, but only officials for LED have been appointed.

4. THE ROLE OF LOCAL GOVERNMENT IN THE LOCAL ECONOMIC DEVELOPMENT

The successful local economic development is the result of wise planning and evaluation and successful application of the development instruments and techniques. To implement the competences in the area of the local economic development, as stipulated by Article 22, the Law on Local Self-Government prescribes several measures and activities that should be undertaken by the municipalities, such as: planning of the local economic development, establishment of the development and structural priorities, implementation and execution of local-economic activities, support to the development of small and medium-sized enterprises and entrepreneurship and participation in the establishment and development of the local network of institutions and agencies for promoting partnerships. As elaborated above, these
activities are being implemented at a very low level, which means that the units of the local
government in Macedonia implement the responsibility for local economic development at a
low rate. This is due to various reasons among which: the partial fiscal decentralization (many
of the responsibilities of the local government units are not fully covered by financial means),
the marginal utilization of the IPA funds, especially the component on regional and rural
development, the lack of instruments for attracting new investments, the lack of fiscal
economy for the tax exemptions and relief as an instrument for stimulating new investments
and businesses etc. The responsibility of the local economic development is de facto mutual
for both the local and the central government, and in such circumstances there is no specific
address for the responsibilities and the obligations.

In regard to implementing LED-related competences municipalities are still heavily
dependent on the central government. With the process of fiscal decentralization,
municipalities are given responsibilities and they are granted sources of funding, but there is
still a high level of centralization in the local government’s financing.

Nevertheless, the latest observations related to the development of the process of fiscal
decentralization show that the process is successfully accomplishing which can be seen by the
fact that local revenues are increased.

Today, compared to 2005, when the fiscal decentralization process commenced, municipal
revenues have increased by five times (Denar 5.9 billion in 2005, Denar 28.2 billion in 2013).

Share of local taxes of 1% of GDP in 2006 increased to more than 1.5% in 2013.

Although local governments have not increased funds for realization of capital projects, the
municipalities demonstrated better preparedness to allocate funds from own revenue sources
and take loans in order to support LED. Municipalities still do not pay great attention to
multiannual planning of capital investments. Notably, the share of realized capital
investments planned under the municipality’s 2011 budget accounted for 65.65%, which
shows improved performance compared to 2010 and 2009 shares, i.e., 63% and 45%,
respectively.

Most municipalities are aware of the need to prepare comprehensive developmental strategies
which – in addition to local economic development – would address other developmental
needs (small and medium-sized enterprises, environmental protection, education, social policy,
etc.). The main problem faced by the municipalities is their inability to fully implement
activities and projects defined in relevant strategic documents, notably because most strategic
documents are not based on municipality’s actual possibilities and the manner of priority-
setting from the array of measures and activities is not appropriate.

Municipalities face the challenge of weak institutional capacity to manage their investment
responsibilities and communal enterprises, many of which lack market-based strategies and
are not financially sustainable. However, major challenges remain with regard to insufficient funds for education in block grants for heating and student transportation costs, the lack of a fully functional system of fiscal equalization, and the growing number of municipalities with blocked accounts.

On one hand, municipalities are still heavily dependent on central government’s funding for implementation of LED policies, whereas, on the other hand, increasing is the number of municipalities which believe that successful implementation of LED policies can be achieved by means of loan-taking (borrowing), i.e., if they enjoy greater autonomy.

The local government plays an important role in the creation of a positive environment for the business development. Each unit of local government has its specific local conditions which will increase or decrease the potential for local economic growth.

4.1. Fiscal decentralization and the local economic development in the Municipality of Ohrid

The Municipality of Ohrid is a good example for the approach and the role of the local government in the local economic development. The town of Ohrid is a tourist, cultural and spiritual center of the country. Tourism is a major economic and dominant branch in Ohrid. Besides tourism, industrial facilities and diverse economy make Ohrid, attractive for business. Therefore, a good strategy for improving the tourism should be created for promoting local development in Ohrid. Local government should encourage tourism in order to achieve sustainable tourism development with sustainable economic growth, bringing economic benefits and improve the quality of tourism and also life for all in the community. For this purpose it is necessary budgetary planning of the funds. In recent years, the Municipality of Ohrid, has faced with serious problems in its financing.

Before decentralization, Ohrid’s budget was conducted in accordance with existing regulations, and as budget revenues were used: sales tax on real estate and rights, communal fee for using street lighting, fees for communal activities, other local taxes, grants and VAT, transfers from other levels of government and transfers from the budget of funds. There was no interest in municipal administration, because revenues were subjected to restriction. Financing of Ohrid in the period from 2005 to 2014 is realized according to the laws and legal regulations which regulate the issues of financing of the municipalities.

In its financing, Municipality of Ohrid in the period from 2006 to 2014 has seen a steady increase in budget revenues, which in 2014 increased by 137.4% compared to those in 2006.

![Figure 2: Budget revenues and budget expenditures in the Municipality of Ohrid in the period 2006–2014 (Municipality of Ohrid, 2014)](image_url)

Characteristic for the growth of budget revenues in the Municipality of Ohrid is the fact that from 2006 to 2010 there was a steady growth, which for the entire period is 70%, or an annual
average of 14%. In 2011, there was a greater increase in the budget, and this is due to revenues from domestic borrowing, which in the previous period the Municipality of Ohrid vanished. In the period from 2011 to 2014 there is a decline in budget revenues by 11.5% for the entire period. This period the fee for arranging the land does not produce expected and projected results, and the other greatest reduction is quite technical.

Total expenditures in the Municipality of Ohrid follow the dynamics of total revenues. In the period from 2006 to 2012, capital expenditures, expenditures for goods and wages have the largest share. Since 2012, with the passage of Ohrid in the second phase of the decentralization process these expenditures still remain as the largest expenditures, but now the largest participation have the wages.

Capital spending plays an important role in a quality of life for local residence and it enhances a municipality’s capacity for creating a more competitive business environment and for increasing the employment. Capital investment is a critical component of a sustainable tourism sector. Greater investment will drive long-term profitability, innovation and growth in the sector, more tourists and more nights spent.

We made a comparison of the total budget and capital expenditures in the Municipality of Ohrid in order to see how much of the total revenue of the municipality is allocated for capital investment. Below is the data:


<table>
<thead>
<tr>
<th>Year</th>
<th>Total Budget</th>
<th>Capital Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>498,539,567.00</td>
<td>203,015,402.00</td>
</tr>
<tr>
<td>2009</td>
<td>476,677,919.00</td>
<td>172,919,367.00</td>
</tr>
<tr>
<td>2010</td>
<td>605,670,609.00</td>
<td>300,063,022.00</td>
</tr>
<tr>
<td>2011</td>
<td>574,498,756.00</td>
<td>277,221,251.00</td>
</tr>
<tr>
<td>2012</td>
<td>840,532,215.00</td>
<td>216,411,346.00</td>
</tr>
<tr>
<td>2013</td>
<td>760,724,369.00</td>
<td>106,166,118.00</td>
</tr>
</tbody>
</table>

%  

<table>
<thead>
<tr>
<th>Year</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>%</td>
<td>40.72</td>
<td>36.28</td>
<td>49.54</td>
<td>48.25</td>
<td>25.75</td>
<td>13.96</td>
</tr>
</tbody>
</table>

For the analyzed period, it is notable that capital expenditures follow the dynamics of total revenues, except in 2012 when increasing in total budget is not followed by increasing in capital expenditures. But, it is surprising the fact that in 2012 only 25.75% of the budget is allocated for capital expenditure and in 2013 only 13.96% which is almost twice less then in 2012.

In this period most of the capital projects are not implemented and most of the revenues are allocated for the new employments in administration departments in the Municipality of Ohrid.

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3 Denar is the official currency of the Republic of Macedonia
Ohrid. That is the main reason for reducing the capital expenditures in the period of second phase of the decentralization.

The direct economic impacts of tourism development are primarily measured in terms of visitor spending on accommodations, entertainment, attractions, food and beverage, and transportation, for both domestic and international travel. Below is the data from the Municipality of Ohrid sector for Local economic development regarding tourism indicators (night spent, domestic and foreign tourists), from 2008 to 2013:


<table>
<thead>
<tr>
<th>Year</th>
<th>Number of tourists</th>
<th>Number od nights spent</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>Domestic</td>
</tr>
<tr>
<td>2008</td>
<td>202,104.00</td>
<td>139,643.00</td>
</tr>
<tr>
<td>2009</td>
<td>189,699.00</td>
<td>122,258.00</td>
</tr>
<tr>
<td>2010</td>
<td>165,109.00</td>
<td>105,213.00</td>
</tr>
<tr>
<td>2011</td>
<td>178,277.00</td>
<td>102,730.00</td>
</tr>
<tr>
<td>2012</td>
<td>183,335.00</td>
<td>99,850.00</td>
</tr>
<tr>
<td>2013</td>
<td>191,504.00</td>
<td>92,637.00</td>
</tr>
</tbody>
</table>

It can be seen from the table above that in 2013 for the first time the number of foreign tourists was greater than the number of domestic tourists, while the number of domestic visitors fell by over 139 thousand tourists in 2008 to over 92 thousand tourists in 2013 year, at the expense of increasing the number of foreign tourists of nearly 63 thousand in 2008 to almost 99 thousand tourists in 2013. It is the same situation in nights spent because larger percentage belongs to domestic tourists. But it is worth mentioning the fact that the nights spent by domestic guests fell by over 874 thousand nights in 2008 to 522 thousand nights in 2013 while foreign visitors have increased the number of overnight stays, or about 172 thousand nights in 2008 to 271 thousand nights in 2013. Because we were limited in terms of the available data for the Municipality of Ohrid because of its entry into the second phase of decentralization and hence the data is limited to make a statistical analysis, we made a comparison and analysis based on the chain index. The next chart shows the corresponding index:

Figure 5: Annual change in total number of tourist related to capital expenditures

Capital expenditures are significant tool for attracting new visitors and they affect the increase in the number of tourists. As the figure 5 shows, after 2010 when capital expenditures are the largest, they have continuously downward trend. In the same period the number of domestic tourists is decreasing and this trend is present today. In contrast, the number of foreign tourists in the period after 2010 increases. In this period the increase in the
number of foreign tourists refers to the work realized from 2010 onwards, with the strategy for attracting tourists through subsidizing the tour operators and subsidizing air flights low budgetary companies that will bring foreign guests of the European and worldwide destinations. These subsidies are the major factor for increasing in the number of foreign tourists, especially they are important in 2013 when Ohrid have a right to use subsidies for stimulating private accommodation, too.

Ohrid must become more accessible for domestic tourists and tourists that do not come with a charter aircraft, and this must be met by certain infrastructure preconditions, improving the overall tourism offer, attracting new investment, and it means that a greater share of the budget has to be allocated for capital expenditures or investments. In order to remain competitive, increase market, employment and continue to attract visitors from overseas, the Government should continue to support capital investments.

Based on data from the Employment Agency of the Republic of Macedonia\(^4\), in the Municipality of Ohrid in the last few years there is not a significant increase in the number of employees. Even after entering the second phase of fiscal decentralization it is noted reduction of established labor relations in this municipality. Therefore, there is still space for improving the local economic development in the Municipality of Ohrid. Today this responsibility is implemented on a solid level and for further local development and for maintaining good economic condition new capital investments are primarily needed: the realization of large infrastructure projects in road infrastructure, education, energy, mineral resources, so that every aspect of citizens' lives can be improved.

5. CONCLUSION

Based on the above elaboration, it is a fact that the responsibility for achieving local economic development is new for the local government and the municipalities are still dependent on the measures and activities undertaken by the central government of the Republic of Macedonia. Therefore, it can be generally concluded that the units of the local government show the weakest performance in the LED compared to the other responsibilities being delegated to the municipalities with the decentralization process. What can be evidenced for sure is that the major part of the municipalities in the Republic of Macedonia has only developed strategies, plans and programs for local economic development but they remain only on paper without being implemented either due to the lack of funds or due to the fiscal dependency from the central government. Instead of implementing activities for creating public-private partnerships and regional economic networks, the municipalities focus on the improvement of the local infrastructure, promotion-related activities and standardization of the administrative procedures.

Generally, to have success in LED, every local government has to have practical understanding of what the local area does well and what it has to offer, be aware of its strengths and weaknesses, the external threats and opportunities, but most importantly what the local area needs and wants. Additionally, the local government has to improve the business environment attractive for investments and companies that can operate successful and efficiently on the local market. To stimulate the local economic development in the Republic of Macedonia, the key priority is to strengthen the financial aspect of the municipalities and the regions as this is directly related to the promotion of the local and regional economic and overall development. In that direction, certain measures could be recommended that would have an impact on the financial aspects of the municipalities as

\(^4\) Employment Agency of the Republic of Macedonia

follows: implementation of full fiscal decentralization in accordance with the transferred responsibilities, development of a methodology for making the municipalities’ financial capacities equal, transparent allocation of funds from the budget intended for financing the equal regional development and allowing the regions and municipalities to submit project proposals within the total amount of funds allocated to the regions and municipalities based on the Law (minimum 1% of GDP), facilitation and simplification of the conditions for crediting the municipalities as a possibility for stimulating the local economic development, maximal utilization of the IPA funds etc.

Other recommendations and measures, which are not directly linked to the financial aspect of the local and regional development, include the following: development of a separate and adequate organizational structure (a sector or a unit) in all municipalities, both urban and rural, that would be exclusively engaged in and committed to the development needs of the municipality, with adequate job positions filled in by quality personnel, development of better marketing strategy for attracting new investments, practical and transparent implementation of the developed strategies, plans and programs for local economic development through the development of public-private partnerships where the private capital would provide the financial support to the realization of these documents, establishment of a system for monitoring and evaluation of the realization of the developed strategies, plans and programs for local economic development.

In order to strengthen the local economic development, municipalities should have the support of the central government, but still it is very important for municipalities to be independent in making their decisions relating to the responsibilities that are assigned to them. Without provision of funds, property, expertise, and full right to operate efficiently, municipalities may feel that problems and challenges have been decentralized without the tools to solve them.

In the case of the Municipality of Ohrid, the quantitative analyses that we made has shown that the local economic development is not at a satisfactory level. In recent years the municipality of Ohrid is facing with problems in its funding. The municipality is in bad financial and material condition. The new local government has inherited outstanding debts where there problems with normal servicing of that liability. Therefore, in the period after the second phase of the decentralization, the local economic development in the Municipality of Ohrid measured by employment, has not been improved. The funds allocated for capital investment as a driver of local economic development and the tourism as a main economic branch are not enough. Even after investments made by various donors, institutions and the municipality itself, the need for investments in this field are still great.

6. LITERATURE

1. EC Progress Report, (2013), Republic of Macedonia
RISK MANAGEMENT IN THE BANKING SECTOR – OBSERVATIONS ON BASEL II IMPLEMENTATION IN CROATIA

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ABSTRACT
The approach to risk management in organizations consists of the following stages: risk identification, measurement and treatment. When credit institutions are concerned, risk management entails the implementation of particular procedures and methods for all stages of management, including the reporting obligation. Efficient risk management enables crisis prevention, enhanced performance, reputation protection and increased stock value. The Credit Institutions Act, which largely relies on Basel II regulations, was introduced in Croatia in 2009. The pillars of Basel II recommendations are minimal capital requirements, supervisory reviews and market discipline. In this paper we focus on the IRB framework for regulating bank capital and consider some scenarios of capital reservations practice in the changing economic conditions, prevailing in Croatia for last several years. Indications that risk management practice in the Croatian banking sector was not fully satisfactory in recession period, are revealed here. Nowadays, considering the availability of credits as perhaps the most important function provided by the banks, effects of the crisis are still very evident. Banks have developed an aversion to taking risks and consequently now in Croatia is lower financial offer and the availability of credits.

Keywords: banking sector, Basel II, credit risk, LGD, PD, risk management

1. INTRODUCTION
Each new activity or event occurring in an organization should involve the uncertainty and unpredictability hypotheses. Risks are not merely accidental phenomena. Instead, they arise, to a considerable extent, from insufficient organization, negligence, failure to monitor processes and flaws in project execution. Applying risk management procedures allows for the discovery and identification of risks that arise in an organization's business activity so that they can be minimized, supervised and maintained at a low level. According to (Culp, 2001), risk management as a business process can be divided into several key activities: identifying risks and determining tolerances; risk measurement; risk monitoring and reporting; risk controlling; supervision, review and a new risk adjustment. In terms of risks, the banking sector is quite specific. Therefore, in addition to military organizations, the vast majority of
theoretical and practical references in the domain of systematic risk management concern financial sector organizations. There are at least three risk categories that shareholders and bank managers have to face: market risk (interest rate risk), default risk and inflation risk (Hadjimichalakis and Hadjimichalakis, 1995, pp. 55-57). Efficient risk management can yield benefits in terms of prevention (crisis avoidance etc.), performance (risk management strategies and key business processes), protection of reputation and increased stock value.

The well-known Basel regulations issued by the Basel Committee on Banking Supervision are – as reflected in their name – aimed at regulating the coverage of risk to which financial institutions are exposed. The Committee was established in late 1974 by central bank governors of 10 countries after serious monetary disorder in international currencies. Their first meeting was held in 1975, and the Committee has been convening three to four times a year ever since (Basel Committee on Banking Supervision, 2014). The Committee's principal goal is to harmonize financial institutions supervision at the international level, thus creating preconditions for intensification of competition in international banking. The Credit Institutions Act (Credit Institutions Act, 2013), which succeeded the Banking Act, was introduced in Croatia in January 2009. The new act largely relies on Basel II regulations as a highest supervision standard. Strict deadlines within which banking (credit) institutions need to apply the guidelines of the Basel II Accord are defined by the legislation of EU member states. Considering Croatia's recent accession to the European Union, the Croatian National Bank has initiated a new Credit Institutions Act to facilitate the adoption of Basel II recommendations. Part of the Act which implements Basel II and related by-laws came into force on 31 March 2010 when credit institutions started with quarterly reporting on capital adequacy ratio based on the methodology of Basel II, the so-called- first tier. (Croatian National Bank, 2011).

The Basel II Accord is the successor to regulations on capital adequacy known as the Decision on Capital Adequacy (Basel I) adopted in 1988. The key feature of Basel I framework is liable capital and the requirement that it should cover 8% of banking risks (Basel Committee on Banking Supervision, 2014). Owing to insufficiently radical regulation, first modifications were implemented in 1996, while the entire process of developing Basel II was initiated in 1999, when the Basel Committee officially announced their first proposal of the new capital adequacy framework. The final text of the Revised Capital Framework, generally known as a Basel II Accord was published in 2004, while the official implementation of the framework in developed countries was initiated in 2006 (Basel Committee on Banking Supervision, 2014). According to the Credit Institutions Act (2013), the term risk management refers to a set of procedures and methods to identify, measure, evaluate, contain and monitor risks, including reporting on the risks to which a credit institution is or may be exposed in its operation. According to the decision of the Croatian National Bank, credit institution is required to (Decision on risk management, OG 1/2009, 41/2009, 75/2009, 2/2010 and 160/2013): (1) adopt a risk management strategy, (2) clearly define and document its preference regarding risk taking, (3) regularly align risk management strategy with business strategy.

As stated in Sverko (2002), financial institutions face a vast number of risks, most important of which are: credit risk, operational risk, market risk, interest rate risk, currency risk/foreign exchange risk, country risk, liquidity risk and solvency risk.

2. CREDIT RISK
Among those, for banks that do not invest into securities it is credit risk that is of greatest importance. It is the most common, most relevant in material terms and, arguably, most complex risk that financial and non-financial subjects need to address so it will be the focus of
our analysis in the following sections of this paper. Credit risk is the risk of loss due to the debtor's failure to repay a loan. Rules for managing credit risks have been defined for all banks. Minimum requirements for credit risk management comprise (CNB, Decision on risk management, OG 1/2009, 41/2009, 75/2009, 2/2010 and 160/2013): organizational requirements, credit process, credit risk control, testing stress resistance and management of connected risks.

2.1 The credit process
A bank needs to have a clear and consistent organizational structure, clear organizational setup with precise, transparent and consistent chains of command and responsibility, effective management of all risks and adequate internal control systems. Criteria for credit approval, policies and procedures also need to be well-defined, along with powers and responsibilities. The credit process also presupposes a requirement for successful credit risk management that consists of the following steps (CNB, Decision on risk management, OG 1/2009, 41/2009, 75/2009, 2/2010 and 160/2013.): (1) placement granting process, (2) placement monitoring process, (3) credit portfolio analysis, (4) treatment of non-performing placements; (5) credit risk early warning system, and (6) a placement classification process according to the degrees of risk. The placement granting process includes an assessment of the creditworthiness of the debtor and the very decision on credit approval. That process is executed by means of evaluating credit rating. In other words, banks employ forms that are required for assessing a client's creditworthiness. The criteria of traditional assessment of creditworthiness are quantitative and qualitative, with distinct criteria for personal loans and firms, uperior, including among others, the amount of income and liquidity status (Presber and Stengert, 2002, p. 46). The term rating is interpreted as relative evaluation or estimate. In economic terms, it refers to evaluation of creditworthiness by means of established rating symbols (Osmanagić Bedenik, 2003a, p. 99). Scoring reflects the evaluation of creditworthiness of a physical person. When used for examining creditworthiness rating, future-oriented technical and economic criteria account for approximately 80% of the rating, while only 20% of it is based on recorded credit history. Expressed by means of letter designations (such as AAA), a rating indicates a company's future prospects (Osmanagić Bedenik, 2003b, p. 75). After all the criteria for the evaluation of creditworthiness have been assessed, the examined borrower is assigned a particular tier. A particular tier denoting the rating grade is determined according to the evaluation of creditworthiness, gridlock risk and non-payment risk. The evaluation of creditworthiness is very important as it is used to prevent a business crisis from occurring in advance. According to the data available from the (Croatian National Bank, online, December 2014), long-term credit rating of the Republic of Croatia assigned by Standard & Poor's, Moody's and Fitch is BB, Ba1, and BB for foreign currency and for domestic currency is BB, Ba1, and BB+, which is worse than the year earlier period. For example, Fitch Ratings downgrades the rating from BBB- to BB +, to give a mark of the country in which it is not advisable to invest.

2.2 Risk drivers
According to Gopi (2008), risk contains the following three components: the event that could occur – the risk; the probability that the event will occur – the likelihood; and the impact or consequence of the event if it occurs – the penalty (the price you pay). Risk drivers and risk events that occur with regard to credit risk lend themselves to classification. Bank can exert its influence on risk exposure. The bank decide whether it will approve a certain loan and thus assume the consequent risk. Having assumed the risk, the bank can easily assess the size of risk events. However, other risk drivers are beyond the scope of bank influence (Bessis, 2002): creditworthiness migration, probability of non-payment and collateral compensation.
Regardless of the rating, the probability of non-payment increases with time. Client that was assigned a BBB (e.g., i.e. adequate, or medium creditworthiness) rating will accrue an approximately identical probability of non-payment in the tenth year as a client that was assigned a BB (i.e. questionable) rating in the first year (1.12%). The creditworthiness migration risk is the probability of a client's financial status being changed (Jakovcevic, 2006a, p. 144). This risk is assessed on the basis of recorded credit history. In case that the client's creditworthiness is diminishing, new protection measures are activated, such as a higher interest rate. With regards to migration, a particular client that has a BBB rating is most likely to maintain its rating in the following year as well (approx. 88-89%). The total probability that a client's rating will improve in the following year by being upgraded to A, AA or AAA tiers is approx. 6-7%. On the other hand, the probability that a client will be assigned a lower rating (BB) in the following year is about 5.3% (Standard & Poor's CreditWeek, 1997; referenced by Djiambou, 2009). When risk drivers and risk events are concerned, a collateral plays an important role as a contractual instrument aimed at ensuring payment or settling liabilities that the crediting bank uses to rationally reduce its exposure to the debtor. It comprises a set of financial instruments, ownership rights and legal norms aimed to protect the creditor's claims (Jakovcevic, 2006b, p. 139). Credit risk is a central issue in risk management in banking. Crediting essentially rests on conscious adoption of controlled risk that can lead to profit.

3. OPERATIONAL RISK IN THE FRAMEWORK OF BASEL II RECOMMENDATIONS

Basel II offers rules for risk measurement and management and, among others, provides the guidelines for the management of key factors related to credit, operational and market risk. Prior to the introduction of Basel II recommendations, operational risk had not been differentiated from other risk categories, which made its measurement, control and management difficult. This type of risk has been brought to closer attention owing to certain features of contemporary business, such as internet banking, increasingly more sophisticated banking products and banking system globalization. The obligation of calculating the capital requirements for operational risk was the key novelty afforded by Basel II, when introduced. Operational risk is ‘the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events’, including legal risk (Basel Committee on Banking Supervision, 2003). The three concepts of operational risk measurement recommended by the Basel Committee are: Basic Indicator Approach, Standardised Approach and Internal Measurement Approach (Basel Committee on Banking Supervision, 2001). The Basic Indicator Approach relates the required level of a credit institution's capital for operational risk with a total exposure indicator for the whole institution. Banks using this approach need to hold capital for operational risk equal to their three-year average relative to the percentage of their positive annual gross income. The Standardised Approach (Basel Committee on Banking Supervision, 2001, p. 7) presupposes the division of a financial institution's activities into several business lines, such as population (personal loans), corporate finance, banks, service agencies and countries, among others (Akkizidis and Bouchereau, 2005, pp. 105-107). For each business line a fixed percentage (the beta factor) is calculated that is used to determine the capital requirements for operational risk coverage. This procedure is recommended for medium-sized banks. The third (and most complex) indicator is the Internal Measurement Approach (Basel Committee on Banking Supervision, 2001, pp. 5-6). Using that approach it is possible to calculate the probability of a loss occurring in particular segments of business based on internal models and
to determine risk values for each segment of business to which a fixed percentage (the gamma factor) is consequently applied.

Banking institutions in Croatia are obligated to use one of the three aforementioned approaches for the calculation of capital requirements for operational risk. In doing so, all banks are encouraged to move to a more advanced approach, so once a bank has opted for a more advanced method it is supposed to proceed with its implementation. Should it revert to a less advanced method it can do so only on justifiable grounds and subject to the prior permission of the Croatian National Bank (Credit Institutions Act, OG 117/2008, 74/2009, 153/2009, 108/2012 and 54/2013).

The development of a new standard – Basel III – was primarily driven by the consequences of the unexpected global financial crisis that began in 2007 as well as by the perceived shortcomings of Basel II, especially concerning crisis events. After several years, the financial crisis led to a lack of confidence in financial markets, which in turn jeopardized the liquidity of financial institutions that tried to salvage themselves turning to state capital injections. The most outstanding advantages of Basel III concern the improvement in the quantity and quality of levels of capital, regulation of the financial leverage degree and expansion of the risk group for which risk coverage capital is required as well as better-defined risk management standards. Implementation of Basel III standard should be done in the period from 2011 to 2013.

4. BANK LOANS AND REGULATORY CAPITAL REQUIREMENTS-
QUANTITATIVE ILLUSTRATION

Basel II allows banks to calculate capital reservations by employing the Standardized Approach that is based on agency ratings as well as the Internal Ratings Based (IRB) Approach (Benzin et al, 2004). Institutions using the IRB Approach also need to develop their own methods of assessing credit risk components. According to the IRB Approach, the risk parameters to be assessed for calculating capital requirements are (Flores et al, 2010): probability of default (PD) – degree of likelihood that the borrower of a loan will not be able to repay the loan within a year; loss given default (LGD) – loss incurred when a borrower defaults on a loan, wherein a collateral is included; exposure at default (EAD) – degree of exposure; maturity (M) – effective date of payment expressed in years.

4.1. The Internal Ratings-Based Approach (IRB) of Basel II- one illustrative simulation

Institutions using the IRB approach, are allowed to determine the borrowers’ probabilities of default, while with advanced IRB approach are also permitted to rely on own estimates of LGD and EAD parameters. These indicators are understood as risk measures and can be used for determination of regulatory capital requirements by means of risk weight formulas specified by the Basel Committee (Bank for International Settlements, 2005). Expected loss (EL) can be calculated according to the formula (1), as in (Huckestein, 2010), which in the case of collateral takes the form (2):

\[ EL = EAD \times PD \times LGD \]  
\[ EL = (EAD - COLL) \times PD \times LGD \]

EAD denotes exposure at default and COLL refers to the value of the collateral insuring the loan agreement against risks. Exposure at default indicates the potential credit exposure in case of the debtor's failure to repay a loan. In doing so, determines the collateralized transaction as a transaction where the credit exposure of the credit institution is hedged, in
whole or in part, by collateral (Dohnal, 2008). A collateral is the asset offered by a debtor to a financial institution to secure a loan in the event of default.

4.2. Model parameters and assumptions
We consider a hypothetical set of contracted loans, according to the rules of the Basel regulation, under the IRB approach. Such a scenario could be realized in Croatia in the period 2007-2009, in business practices of some banks, when it actually started severe economic crisis. According to the assumption of our model, the probability of the occurrence of a default event is determined by client category and delay time. Let us assume that Table 1 is relevant for PD and LGD for given client segmentation. To obtain more precise calculations, the examined delay time is broken down into several time segments. Justification of assumption for application of the PD estimation model in a manner as presented in Table 1, can be found in (Flores et al, 2010, pp. 16-17).

Table 1. PD and LGD client segmentation by category and delay time

<table>
<thead>
<tr>
<th>Client category</th>
<th>Delay time (in days)</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Up to 30</td>
<td>31 to 60</td>
<td>61 to 90</td>
<td>91 to 120</td>
<td>121 to 150</td>
<td>151 to 180</td>
</tr>
<tr>
<td>PD, LGD %</td>
<td>PD, LGD %</td>
<td>PD, LGD %</td>
<td>PD, LGD %</td>
<td>PD, LGD %</td>
<td>PD, LGD %</td>
<td>PD, LGD %</td>
</tr>
<tr>
<td>Personal loans</td>
<td>1, 1</td>
<td>10, 2</td>
<td>30, 10</td>
<td>100,20</td>
<td>100, 55</td>
<td>100, 100</td>
</tr>
<tr>
<td>State institutions</td>
<td>1, 1</td>
<td>3, 10</td>
<td>10, 15</td>
<td>100, 25</td>
<td>100, 45</td>
<td>100, 60</td>
</tr>
<tr>
<td>Entrepreneurial sector</td>
<td>3, 3</td>
<td>20, 15</td>
<td>50, 35</td>
<td>100, 75</td>
<td>100, 90</td>
<td>100, 100</td>
</tr>
<tr>
<td>Corporate sector</td>
<td>2, 2</td>
<td>15, 7</td>
<td>40, 20</td>
<td>100, 40</td>
<td>100, 65</td>
<td>100, 100</td>
</tr>
</tbody>
</table>

In our model, with considerable freedom in the quantitative determination, PD and LGD factors have highest values in the case of the entrepreneurial sector, which also entails highest reservations for that client segment. This understanding was significantly represented in the actual practice of lending in Croatia. Considering that in the aforementioned example the entrepreneurial sector refers to craftsmen, most of whom are affected by instability of business operations in Croatia, it is to be expected that this group of clients would represent the highest-risk borrowers. The lowest factor values and amounts of reservation were obtained for state institutions. Owing to the functioning of the rule of law, as well as considerable state budget funds they can dispose of in accordance with applicable laws, state institutions are viewed as having the lowest risk in terms of financing. According to the obtained values, reservations for contracts with persons and somewhat higher reservations for the corporate sector are placed between the two aforementioned categories.

In the following simulation we administer the formula (2) on a fictional portfolio of 30 agreements, for the calculation of capital requirements.

4.3. Illustrative simulation - comparison of exposures and capital requirements by client category
The exposure values and the amount of collateral were randomly selected in the range of 5,000-30,000 for exposure and 1,000-7,000 for the amount of collateral. The number of days
expressing the time delay was also determined randomly in the range of 0-120 days. The values of PD and LGD factors were taken from Table 1 for each client segment. For each amount of exposure less the amount of collateral the factors of each client segment were administered so as to indicate the differences in the amount of capital under identical financing terms.

In case of delay that is longer than 90 days, the amount of capital requirement grows significantly since the probability of the occurrence of a default event as well as the loss in the occurrence of a default event are also increased. Should the delay in case of a particular client exceed 90 days, provided they have substantial funding at their disposal (defined by the risk management policies of a particular financial institution), the custom approach is applied. In our example, identical input values (Table 2), at the average exposure amounting to 12,840,54 and delay in days amounting to 61.27, will yield the average amounts of reservation equal to 865,11 (Personal loans), 1,006,86 (State institutions), 3,536,74 (Entrepreneurial sector) and 1,821,43 (Corporate sector). It is evident that using this perspective for determining parameters does not stimulate the crediting of the entrepreneurial sector. Achievement of high credit placement in the segment of population, with low PD and LGD values, results in the saturation of this segment and its financial paralysis with regards to closing new deals with banks, in the next period of time. The potential sectorial orientation in lending we may analyze focusing on the Italian Banking Association's (ABI) model of bank regulation classification. This model is based on the strategic goal formulation within two dimensions: internal efficiency and market positioning (Arhivanalitika, 2005). For both of these components of the strategic objective, the strategic areas can be defined and triggers of the creation of new values can be link with this areas, such as e.g. regulatory areas in which the new value is created by improving of regulation.

Furthermore, while Table 1 contains the aspect of dynamic adjustment in the evaluation of risk parameters, although very regular periodic controls regarding PD, LGD is not sufficient here for successful risk management, especially if we know that Croatia in 2008 entered into a severe recession period. For banks which applied RBI at that time, incremental periodic changes in the risk assessment or correction in reservations by simple procedure with using amounts (PD ± ΔPD) and (LGD ± ΔLGD), could not reduce the gap in referring to the main downward process of recession.

The suggestion of (Deloitte, 2011) is that in the circumstances of mild or severe recession, must be taken into account the changed value of parameter PD- so called Stressed PD. Such modified parameter, in simple approximation, should be defined as the function of stressed macroeconomic variables, such as change in GDP, unemployment rate, industrial production, etc., as e.g. in formula (3):

\[ \text{Stressed PD} = \beta_1 \times \text{GDP} + \beta_2 \times \text{unemployment rate} + e \]  


(3)

Sensitivity of risk parameters and capital requirements to changing economic conditions are considered in many papers, such as (Dohnal, 2008), (Zsámboki, 2007). With regard to the recording of a relatively significant number of "bad loans" for banks in Croatia, it is hard to believe that the good practice of the successful application of risk management is widely applied in a period of a recession so far.
<table>
<thead>
<tr>
<th>Exposure</th>
<th>Amount of collateral</th>
<th>Exposure less amount of collateral</th>
<th>Delay time (in days)</th>
<th>Personal loans</th>
<th>State institutions</th>
<th>Entrepreneurial sector</th>
<th>Corporate sector</th>
</tr>
</thead>
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<td>28,795.00</td>
<td>6,054.00</td>
<td>22,741.00</td>
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<td>0.01</td>
<td>2.27</td>
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<td>6,456.00</td>
<td>20,514.00</td>
<td>7</td>
<td>0.01</td>
<td>0.01</td>
<td>2.05</td>
<td>0.03</td>
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<td>6,327.00</td>
<td>6,327.00</td>
<td>0.00</td>
<td>7</td>
<td>0.01</td>
<td>0.01</td>
<td>0.00</td>
<td>0.03</td>
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<tr>
<td>25,318.00</td>
<td>4,854.00</td>
<td>18,464.00</td>
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<td>13,620.00</td>
<td>13,434.00</td>
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5. CONCLUSION
It is in the financial sector that risk management makes business processes considerably more efficient. When credit institutions are concerned, risk management refers to implementing appropriate procedures and methods to identify, measure, monitor and control risks. The recommendations concerning credit risks in banking provide banks with safer business operations, less bad placement of funds and greater stability. The international Basel II Accord brought in a standardized framework for the operational risk segment, which previously was not subject to external regulations. For several years financial markets have been continuously tormented by the financial crisis which is considered to be the greatest challenge of our time, leaving an impact on the banking sector as well. Although the banking sector in Croatia is treated as one of relatively more stable sectors owing to a strict legislative framework, the consequences of the crisis are overtly evident indeed. They can be seen in the domain of liquidity, increase in the financing costs and the very quality of credit placements. Nevertheless, analysts maintain that the influence of recession on the Croatian banking sector will not significantly undermine the quality of the banking sector assets and claim that it will remain at a satisfactory level of stability. Macroeconomic models show that smaller banking groups in Croatia that are primarily oriented toward enterprises, that is, more risky credit placements and the economy are the most exposed ones in terms or risk. On the other hand, large banking corporations have the lowest openness to risk and potential losses. Upon the introduction of the new Credit Institutions Act in Croatia, which is largely based on the recommendations from the Basel II Accord, questions were raised of the readiness of Croatian banks for adopting and implementing those recommendations as well as of the impact that the law would have on the disposable capital of banks in the conditions of financial crisis. Although the availability of credits is perhaps the most important function provided by the banks, effects of the crisis are still very evident, primarily in lending loans. Banks have developed an aversion to taking risks and consequently in Croatia is lower financial offer and the availability of credits.

BIBLIOGRAPHY
THE LISBON STRATEGY LESSONS: PERSPECTIVES OF THE EUROPE 2020 IMPLEMENTATION

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ABSTRACT
The Europe 2020 strategy was launched in 2010 as a successor of the Lisbon strategy with the main aim to generate smart, sustainable and inclusive growth in the European Union. Concretely, the Europe 2020 strategy has set five ambitious objectives on employment, innovation, education, social inclusion and climate/energy to be reached by 2020. Each Member State has adopted its own national targets in each of these areas. Almost half way from the start of the implementation, is a good time to assess accomplishments of the Europe 2020. Very similar to idea of the Lisbon strategy which did not meet expectations, the Europe 2020 strategy was launched with great optimism trying to retrieve all the things that did not function with the Lisbon strategy; from the aims via measures to the way of implementation. One of the problems of the implementation of the mutual strategy of the European Union member states is their heterogeneity. Furthermore, economic and financial crisis that occurred does not contribute to the achievement of the Europe 2020 goals. This paper analyses the perspectives of the fulfillment of the Europe 2020 goals assessing the so far results, but also comparing its contents and implementation to the Lisbon strategy to determine whether the past mistakes are corrected. In order to do that paper analyses and determines the deficiencies of the Lisbon strategy. Also macroeconomic conditions and characteristics of member countries are taken into consideration to answer to the question whether we can hope the Europe 2020 strategy to be achieved in 2020 or not. Finally, paper identifies weaknesses of the Europe 2020 implementation and points out possible measures to strengthen the Europe 2020 implementation.

Keywords: Europe 2020, European Union, Lisbon strategy

1. INTRODUCTION
The European Union (EU) is heterogenous integration with economic and social differences among member countries and its regions. These differences are mostly caused by unequal spatial distribution of economic activities which reflects of variations on the level of the quality of life (Tvrdon, 2012). The basis for bringing any European strategy, as well as the Lisbon and the Europe 2020 strategies is interdependence. Interdependence makes the main reason why is coordinated implementation of strategies more beneficial than its individual implementation (Höpker, 2013). Also, the coordination of reforms conducted among Member States can bring to positive spillovers effects. The Europe 2020 strategy was launched in 2010 as a successor of the Lisbon strategy to generate smart, sustainable and inclusive growth in the European Union. Concretely, the Europe 2020 strategy has set five ambitious objectives on employment, innovation, education, social inclusion and climate/energy to be reached by 2020. Each Member State has adopted its own national targets in each of these areas. Almost half way from the start of the implementation, is a good time to assess accomplishments of the Europe 2020. Very similar to idea of the Lisbon strategy which did not meet expectations, the Europe 2020 strategy was launched with great optimism trying to retrieve all the things that did not function with the Lisbon strategy; from the aims via measures to the way of implementation. One of the problems of the implementation of the
mutual strategy of the European Union member states is their heterogeneity. Furthermore, economic and financial crisis that occurred does not contribute to the achievement of the Europe 2020 goals. The main aim of the paper is to analyze and determine the perspectives of the fulfillment of the Europe 2020 goals assessing the so far results, but also comparing its contents and implementation to the Lisbon strategy to determine whether the past mistakes are corrected. The paper is divided into four parts. The first part represents the introductory part. The second part of the paper is devoted to the analysis of the background and accomplishments of the Lisbon strategy and the background as well as so far accomplishments of the Europe 2020 strategy so far. It analyses and determines the deficiencies of the Lisbon strategy and identifies weaknesses of the Europe 2020 implementation and points out possible measures to strengthen the Europe 2020 implementation. The third part of the paper analyses similarities and differences between the Lisbon and the Europe 2020 strategies as well as factors of the influence on the implementation of the Europe 2020 strategy. Fourth part of the paper represents the conclusion in which appropriate lessons from the Lisbon strategy for the Europe 2020 strategy are given as well as the prospects of the full implementation of the Europe 2020 strategy.

2. THE LISBON AND THE EUROPE 2020 STRATEGIES: BACKGROUND AND ACCOMPLISHMENT

2.1. The Lisbon strategy
The Lisbon strategy was a first serious attempt to coordinate reforms which are needed to conduct in Member States. It provided necessary frame and guideline. At the beginning, it is important to highlight conditions under which this strategy was launched. The Lisbon strategy was launched due to the need for economic and social reforms in Europe in order to achieve sustainable success in terms of globalization. Competitiveness towards the USA and emerging economics like Brazil, India, China, etc., were one of the main wanted accomplishments of its implementation. The employment rates were lower and unemployment rates higher than in the USA, for instance; structural long term unemployment was considered to be major problem. Also, due to high unemployment and aging population, European pension systems were not sustainable any more (Höpker, 2013).

In 2010, when the Lisbon strategy was launched the European Commission stated that too many markets in the EU are still fragmented. The special attention was given to decreasing obstacles on the European capital markets and low investments in to research and development (R&D). For instance, in 1999, all the EU15 countries, except Sweden and Finland had lower investments in R&D than Japan and the USA. Considering all the above mentioned, on 23rd and 24th of March 2000, Member States agreed on the mutual goals and instruments named the Lisbon strategy. Namely, this strategy has three pillars. First pillar prepared transition into economies and societies based on knowledge, which should be accomplished through improvement of policies for the establishment of the information society, increase of R&D, speeding up processes of structural reforms for achieving competitiveness and innovation, and through full establishment of the internal market. The main goal of the second pillar was modernization of the European social model, as well as investing in people and lowering social exclusion. Third pillar considered the protection of the environment and it was added to the Lisbon strategy on the meeting of the European Council in Göteborg on 15th and 16th June 2001. This pillar was added in order to ensure that economic and social goals of the Lisbon strategy would be conducted on a sustainable way.
Because of different areas it covers, the Lisbon strategy was planned to be implemented via combination of existing processes and instruments, like regulative and directives which Member States are legally obliged to commit to and via newly introduces the Open Method of Coordination (OMC) (Höpker, 2013). The OMC depends upon political will and Member States are not legally obliged to commit to it. Existing processes in that time, Broad Economic Policy Guidelines (BEPGs), processes form Luxembourg, Cardiff and Cologna were considered to be suitable instruments for the implementation of the Lisbon strategy. BEPGs were introduced in 1996 in order to ensure economic convergence among countries which decided to introduce Euro (Heuse and Zimmer, 2011). BEPGs represent general yearly directions of the European Council to Member States of the EU and for the EU itself. The Luxembourg process introduced in 1997 and it is also known as the European Employment Strategy was focused on employment. It refers to yearly drafting of directions for employment, national action plans of implementation and common report on employment. Together with BEPGs make the central instrument of the EU agreement for coordination considering economic and employment questions. The Cardiff process, introduced in 1998, points out the need for coordination of structural reforms for fostering economic growth and employment. Through the Cologna process, introduced in 1999, macroeconomic dialog was established among the representatives of the European Commission, the European Council, social partners, the European Central Bank in order to support each other and increase of employment and economic growth with keeping the stability of prices.

The OMC has its roots in 1997. It was introduced with the aim of fostering implementation of the strategic goals of the Lisbon strategy and help Member States in the progressive development of their own policies. Although, many authors consider that the main reason for establishment of this instrument was non-existing of the EU authority in more important policy areas like labor market, tax systems and social security (Höpker, 2013). Through the OMC directions and plans with deadlines and goals of implementation were made, as well as qualitative and quantitative indicators and benchmark which made possible to compare practices among Member States. These directions were translated into national and regional policies and the accomplishment of the goals was analyzed and evaluated periodically through common process of learning. It is important to point out that the OMC was considered to be a new way of governance, since it represented decentralized approach according to the principle of subsidiarity (top-down approach).

For the evaluation of the main areas of the Lisbon strategy (economic results; employment; research, innovation and education; economic reforms; social cohesion; environment protection) 79 structural indicators were developed.

Five years after launching the Lisbon strategy, the European Council analyzed its results and concluded for results to be weak. This middle term report about the Lisbon strategy was also called Kok's report in the name of Wim Kok, former prime minister of the Netherlands who was on the head of the group of 13 experts “High Level Group”. This group had a task to objectively evaluate the implementation and accomplishments of the Lisbon strategy. They warned that the accomplishments of all goals in 2010 will not be possible. The main reasons were: lack of political activities of the European institutions and Member States, weak coordination, and disparity between certain priorities. This report suggested redirection of goals towards economic growth and employment, not in a way to abandon the goals of social cohesion and the environment protection, but in a way to support them too (Höpker, 2013). Besides above mentioned, the report suggested also more active role of the European institutions and all stakeholders in the implementation of strategy, introduction of two-years national action plans of the implementation, BEPGs and directions about employment revision because they did not seem to be mutually coherent, better planning of the EU budget
according to the strategy goals, lower number of goals and indicators, etc. Not less important, they stated that the OMC needs improvements since it does not give wanted results. Besides this cited report, many experts evaluated in this period the results of the Lisbon strategy and although their explanations and methods vary, common critics can be recognized and it refers to governance.

As a consequence, the European Council redirected goals of the Lisbon strategy in the document “Working together for growth and jobs” in 2005 on the areas: (1) knowledge and innovation, (2) making Europe a better place for investment and business and (3) economic growth and employment for greater social cohesion.

Comparing defined goals and accomplished results in 2010, one can argue that the Lisbon strategy did not gave results since quantitative goals in connection with economic results, employment, research and innovation, social cohesion and sustainable development are not achieved (Höpker, 2013). Although, it cannot be argued that the Lisbon strategy did not fulfill any of its tasks, but the main goal of establishing “the most competitive and dynamic economy based on knowledge in the world capable for sustainable economic growth with more and better jobs and greater social cohesion” is not achieved.

Besides governance issues, which we can refer to as internal factors, there are some external factors which lead to these poor results. First, during the implementation of the Lisbon strategy, it was many economic disturbances and the Lisbon strategy was launched in the period before. Second, the expansion of the EU in 2004 and 2007 lead to decreasing relevant indicators. However, governance failure is considered to be major obstacle in accomplishing goals of the Lisbon strategy.

Cantillon (2011) explores the effects of the Lisbon strategy on economic growth, employment and social inclusion. Results show that the implementation of the Lisbon strategy did not bring to decreasing poverty rates, but, on the contrary, these rates stagnated or even increased. It is because the increase of employment brought little benefits to households were nobody works, so the number of households in which more members works increased, but the ones in which nobody works remained unchanged. It is the fact for almost all Member States.

2.2. The Europe 2020 strategy

In the further text, only the most important information about the Europe 2020 strategy are discussed, which are necessary for the further analysis in part 3 of the paper.

The European Council adopted formally the Europe 2020 strategy on the summit in Brussels on the 17th June 2000. New strategy is generally more oriented macro economically than the Lisbon strategy. The reasons for launching this strategy are very similar to the ones of launching the Lisbon strategy. Consequently, their goals are very similar. Main goals of the Europe 2020 strategy, shown in Table 1, reflect three priorities of this strategy: (1) smart, (2) sustainable and (3) inclusive growth. Smart growth assumes development based on knowledge and innovation, sustainable growth promotion of more resource efficient, greener and more competitive economy, and inclusive growth represents fostering employment, social and territorial cohesion (European Commission, 2010a).
### Table 1 Five headline targets of the Europe 2020 strategy (European Union Committee of Regions, 2012, p. 10)

<table>
<thead>
<tr>
<th></th>
<th>Employment</th>
<th>R&amp;D / innovation</th>
<th>Climate change / energy</th>
<th>Education</th>
<th>Reducing poverty and social exclusion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>75% of 20-64 year-olds to be employed</td>
<td>3% of the EU’s GDP (public and private combined) to be invested in R&amp;D/innovation</td>
<td>greenhouse gas emissions 20% lower than 1990 (or even 30%, if the conditions are right)</td>
<td>reducing school drop-out rates below 10%</td>
<td>lifting at least 20 million people out of the risk of poverty and social exclusion</td>
</tr>
<tr>
<td>2.</td>
<td></td>
<td></td>
<td>20% of energy from renewables</td>
<td>at least 40% of 30-34-year-olds completing tertiary education</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td></td>
<td></td>
<td>20% increase in energy efficiency</td>
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</table>

National reform programmes which are launched yearly through the European semester reflect transmission five goals of the Europe 2020 into national goals and define measures of the implementation. Setting their own national goals, Member States take into consideration their starting positions and each Member State contributes to the full implementation of the strategy.

The analysis of national reform programmes in 2011 showed that goals set by Member States will not be sufficient to achieve the Europe 2020 targets (Heuse and Zimmer, 2011). The Europe 2020 strategy involves stronger economic governance and thematic approach. Also, it involves reporting of Member States together with fiscal surveillance through stabilization and convergence programmes.

BEPGs and Employment Guidelines (EGL) represent main tool for coordination of economic and social policies in the EU. Also, EGL has to be compatible with BEPGs and together make integrated directions. In 2010 were adopted 6 BEPGs directions instead of previous 16 and 4 EGL directions, instead of previous 8 (Heuse and Zimmer, 2011).

The European semester represents new instrument which is used for organization and coordination of yearly political cycle of the EU. It starts with the European Commission's Annual Growth Survey, adopted usually at the end of the year and setting priorities for the EU for the next year. On the basis of this survey, the European Council during the spring summits gives directions for national policies. In April Member States deliver their National Reform Programmes and Stability and Growth Pacts and on the basis of the evaluation of the European Commission, the European Council formally adopts specific political directions at the end of June or beginning of July, and Member States are obliged to implement them in the second part of the year.

## 3. PROSPECTS OF THE EUROPE 2020 STRATEGY FULL IMPLEMENTATION

Learning from the experiences of other Member States and best practices fostered through evaluations and comparisons conducted by the European Commission was key part of the Lisbon strategy and the OMC (Vilpišauskas, 2011). Vilpišauskas (2011) states that although the Europe 2020 strategy represents some elements of learning from experience, one cannot argue on solid arguments that this strategy takes into consideration all experiences from the implementation of the Lisbon strategy. However, the OMC is not mentioned in the Europe 2020 strategy.

The main difference between these two strategies is in the governance system and the number of indicators. The Lisbon strategy used 127 indicators and the Europe 2020 five sets of basic indicators, i.e. goals. Also thematic approach, reporting countries in parallel with national
reform programmes and stabilization and convergence programmes ensures better connection between macroeconomic goals and the Europe 2020 goals. One cannot forget to mention the role of the European semester.

However, the Europe 2020 strategy was launched in the period of the greatest financial crisis which occurred in the world after the Great Depression and started in 2007. Pereira (2011) states that all improvements accomplished by the implementation of the Lisbon strategy were wiped out and that crisis had great influence on shaping the Europe 2020 strategy. Also, non-defining the goal of GDP growth rate within the Europe 2020 strategy can be considered as a consequence of a failure of the Lisbon strategy.

Quality and quantity of education will play the key role in sustaining the EU competitiveness according to Roth and Thum (2010), but they point out that goal of tertiary graduation rate of 40% many Member States, including Germany, which is considered to be one of the more advanced Member State, will not be able to achieve by 2020. Their crucial critique on the Europe 2020 strategy is that the issue of the quality of education is not even tackled in the strategy although it is clear that this issue is very important. For instance, in time when the Europe 2020 strategy was launched, China had the same number of citizens with tertiary education as the EU15 countries, and by 2020 China wants to triple this number. But the quality of education system can represent an obstacle to China for removing gap with the USA and the EU concerning innovation potential (Roth and Thum, 2010). Increasing number of high educated citizens is crucial for increasing innovations. Theodoropoulou (2010) also warns on the importance of quality of education. Increasing number of better educated citizens does not guarantee that students will acquire skills which certain country needs. These skills are important for all three goals of the Europe 2020 strategy, but by themselves will not foster and/or ensure smart, sustainable and inclusive growth if they are not followed by adequate policies which will ensure opening of workplaces. Also, Theodoropoulou (2010) states that there is not enough knowledge about the skills which will be needed for achieving the Europe 2020 strategy goals by 2020. Gros and Roth (2012) also conclude that the Europe 2020 strategy deals only with quantitative, but not and qualitative education goals.

Albu (2011) warns on big differences among Member States concerning the share of expenditure for R&D in GDP at the moment of launching the Europe 2020 strategy and the probability of achieving common goal of 3% of these expenditures in GDP.

Some authors analyzed weaknesses and strengths of the Europe 2020 strategy from the point of view of their countries. For instance, from the point of view of BRIC countries, the main strength of the Europe 2020 strategy is in the fact that it represents unique and common strategy of all Member States for which implementation they have legal obligation. Some international experts argue that the Europe 2020 strategy lacks of ambition and clear strategic vision and that this strategy did not go any deeper or further than already existing agreements (Pereira, 2011). For instance, the Europe 2020 with the goal of decreasing greenhouse gas emission for 20% just adopted existing obligations which are even lower than in other countries. In Brazil, this goal is 50% by 2022, in China 40-45% for the GDP unit and in Russia 40% of decreasing energy consumption by 2020 (Pereira, 2011). Concerning this goal, Gros and Roth (2012) suggest to increase it in the Europe 2020 strategy to 30%, with amendment of internal pricing through European Emissions Trading System, with external dimension; carbon tariff, carbon border tax. Otherwise, according to them, major improvements on the protection of environment cannot be expected.

The Europe 2020 strategy gives little attention to the global economic and political context, it is more inward oriented. Deregulation of international markets and financial sectors is blamed for the world economic and financial crisis. The Europe 2020 does not pay attention to these markets and sectors at all (Pereira, 2011). This issue was also recognized by Gros and Roth...
According to them, although the Europe 2020 strategy was launched after the crisis, it doesn’t content any respond to the crisis. Annicchiarico, Dio and Felici (2011) researched potential quantitative effects of reform measures from the Europe 2020 strategy on the Italian economy and developed four scenarios. Main conclusions of their research is that labor market reforms will potentially bring benefits for output and employment and that real wages for better educated workers will increase. Some interventions will cause transitional costs because of temporary decrease of consumption and/or employment, but simultaneously performing all reforms could alleviate these costs in the middle term. Also, as results of higher economic growth, in the scenario in which reforms will not generate costs, the ratio of public debt and GDP decreases. However, their results showed that some structural reforms which are neutral for stated budget can have impact on external imbalances.

Hyman (2011) analyzed the participation of trade unions in the public discussion on the Europe 2020 strategy. It was 1200 comments in total, of which 16 from national trade unions and 10 of supranational trade unions. In fact, it means that trade unions were not interested in the Europe 2020 strategy. Hyman (2011) explains it as the results of the disappointment of the trade unions with the Lisbon strategy.

European Union Committee of the Regions (2012) suggests local and regional government to define their own vision of 2020 in order for them to be more successful in the implementation of the Europe 2020 strategy. This vision should be based on SWOT analysis, the way of transmitting national reforms into local and regional specific, connecting their budgets to the determined goals, maximum use of structural and cohesion funds, etc.

Gros and Roth (2012) analyzed whether the accomplishment of five main the Europe 2020 strategy goals will foster the global competitiveness of the Member States economies. Their results show that some of the goals cannot be evaluated because of differences in national definitions, and for the most of it, it is questionable whether will be achieved. For instance, about the goal concerning innovations, the rate of the investment in R&D in the EU was slowed down more than ten years and the fulfillment of the goal in 2020 will require great detachment from the long term trend (Gros and Roth, 2012). Also, the goal of 3% of GDP investments into R&D was determined by the Lisbon strategy and the Europe 2020 strategy left the same benchmark although new sets of indicators were developed. Namely, abovementioned indicator is criticized a lot for concentrating more on the production sector, and less on the service sector (Gros and Roth, 2012). From the analysis of the goal of employment, Gros and Roth (2012) conclude that improvement of workers skills in the EU will be crucial to fostering higher employment rates. Concerning the subject of education, European research area should enable Member States universities to achieve synergy effect, like it was the case in the USA. European universities have to become excellent. In the first 20 universities in the world, 15 of them are from the USA. It reflects a danger from ignoring necessary reforms in high education. Also, Gros and Roth warn about social cohesion which had very important place within the Lisbon strategy till its revised version in 2005. In the Europe 2020 strategy, social cohesion is reduced on three indicators. Trivialization of social cohesion can put in danger long term sustainable economic prosperity of the EU.

Theodoropoulou and Watt (2011) claim that it is questionable whether Member State can and want to adjust policies of fiscal savings introduced due to crisis with the measures needed for achieving smart, sustainable and inclusive growth. Especially, concerning planned savings in public investments and education expenditures. Authors express their doubts about accomplishing the goal concerning poverty, and others goals proposed by the Europe 2020 strategy in these conditions.
Zuleeg (2010) argues that the basic question is whether the Europe 2020 strategy is sufficient for achieving higher economic growth rates in the EU. Without economic growth it is going to be impossible to fight with crisis on labor markets and with public finance or ensure the sustainability of economic and social model.

Stahl and Spinaci (2010) point out that the Lisbon strategy did not succeed in involving all factors into its implementation, especially local and regional government and that the Europe 2020 offers them and other actors completely into process. Furthermore, authors believe that subsidiarity still needs to stay leading principle. Flexibility and different forms of strategic planning on decentralized level will contribute to achieving the Europe 2020 priorities.

ESPON Atlas (2013) research shows that achieving smart, sustainable and inclusive growth through the Europe 2020 strategy has clear territorial dimension. The contribution of European regions and cities demands territorial different implementation strategies. Differences among European region represent a challenge to the implementation of the Europe 2020 strategy. For the full accomplishments of goals it is necessary to take into consideration specifics of certain areas in the implementation of policies which will contribute to achieving goals of the Europe 2020 strategy.

4. CONCLUSION
One can claim that the spirit from the 1950s when the EU was established is not present in such manner today although that political initiative and engagement serve as examples for the politicians all over the world.

It is questionable whether the Europe 2020 strategy will bring back the EU its position as a leading global economic and political actor. The Europe 2020 strategy lacks of global approach and certain dimensions which would be necessary for achieving above mentioned goal.

Based on the so far analysis, one can say that are still remaining challenges of the implementation of the Europe 2020 strategy. For successful implementation, the Europe 2020 needs, besides stronger governance, stronger political commitment. The challenge remains how to achieve or increase ownership of the Europe 2020 strategy by the EU citizens and institutions. Stronger governance than of the Lisbon strategy offers optimism. However, taking into consideration occurred financial and economic crisis, and its influence on the implementation of the Europe 2020 strategy, as well as differences in many areas among Member States, one can start doubting in the full accomplishment of the Europe 2020 strategy. Detailed quantitative assessment should be conducted in order to determine the perspectives of the full implementation of the Europe 2020 strategy precisely.

LITERATURE


WHEN ABDUL MEETS DAVID – DEVELOPING A RESPONSIVE REGULATORY SYSTEM FOR ISLAMIC FINANCIAL INSTITUTIONS: A CASE STUDY OF AUSTRALIA

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ABSTRACT
Islamic Financial Institutions serve as a substantial potential opportunity for the Australian economy given the steady growth of the Islamic banking, its closeness to the 60% of the Muslim who reside in the Asian countries and Australian Federal Government’s ‘Asian Century Strategy’. Though Islamic financial institutions have expanded significantly over the recent two decades in Australia, they face a laissez faire market, which failed to address their particular regulatory needs. Operating in a conventional banking favoured environment without special regulatory treatment, the Islamic financial institutions may give in to competition at the risk of jeopardising Shari‘ah compliance in Australia. Taking a risk-based perspective, a responsive regulatory system is developed, incorporating self-regulation such as the IFSB Standards, a black-letter laws and the hybrid, responsive to the business characteristics and corporate governance. A Seven-stage model was also developed to operationalise the responsive regulatory framework. This study may shed light on the development of Islamic Financial Institutions to be introduced into a new market in the advanced economies similar to Australia.

Keywords: Responsive regulation, Islamic financial institutions, case study

1. EXECUTIVE SUMMARY
The purpose of this paper was to identify the unmet regulatory needs of Islamic financial institutions in Australia and to develop policy options to cater to such unmet needs on the condition that no negative externalities were to incur to the existing financial service providers. Given the uniqueness of the Islamic financial institutions, this report challenged the extant ‘one size fits all’ regulatory model in the Australian financial service sector by proposing a new responsive regulatory framework which has a strong focus on the interests of stakeholders rather than shareholders. Furthermore, the paper argues that the responsive regulatory model yields more efficient outcomes in regulatory enforcement comparing to the other alternatives. The paper analysed the demand and supply of Islamic finance in the global context and identified the potential opportunities for Australia. Then the paper went on to review the current financial regulatory and governance system in Australia (Figure 1) and identified the regulatory gap for Islamic financial institutions. After taking both the distinct features of the Islamic financial institutions and their unmet financing needs into consideration, it is recommended that the proposed responsive regulatory framework would be the most suitable option due to its economic efficiency, suitability, accountability and sustainability features. A seven-stage model (Figure 4) is developed accordingly to operationalise the responsive regulatory model (Figure 3). The establishment of the Shariah Supervisory Board has been used as an example to illustrate how the proposed models may be applied to the improvement of governance and regulation of Islamic financial institutions in Australia.
2. INTRODUCTION

Abdul who come from an Islamic background in Australia is keen with establishing an Islamic financial service company to serve people with similar religious belief like him. He did not realise how few Islamic finance service providers are in Australia. He approached an Australian commercial banker David who comes from a Western background. David intends to introduce Islamic finance into his company. But both David and Abdul are not clear about the regulations that they may face and how they can lobby for a more pleasant regulatory environment. This paper intends to help David and Abdul to understand the regulation and propose a better regulatory framework to cater to the fast-growing Islamic financial service sector in Australia. Hence our research questions for this paper are:

i. How is the Islamic service sector regulated in Australia?; and,

ii. Given that the Islamic finance market is still premature in Australia, how should it be better regulated?

This paper aims to understand and develop a regulatory reform framework for Islamic finance sector in Australia. Acknowledging the heterogeneity of Islamic finance under different jurisdictions, this study is only scoped down to the analysis of development of Islamic finance in Australia. The case study adopts a problem-oriented method, with a particular interest in identifying the major regulatory challenges facing Islamic finance in Australia and in developing solutions to these problems. The paper proceeds as follows, the rest of the section summarised the global development of the Islamic finance, identified opportunities for Islamic finance in Australia, reviewed Australian governments’ supportive policies toward the Islamic finance and evaluates the regulation of the financial service providers in Australia. Section 2 reported the findings from the case study, including the shifting of the governance paradigm from the shareholder hegemony to a stakeholder interest, as well as that of the regulation from the ‘one size fits all’ model to a responsive regulation framework. Section 3 discussed the application of the proposed policy option based on two examples, corporate governance and stamp duty. Section 4 concluded with acknowledgement of the limitation of this study, recommendations and proposition of future research direction.
2.1. Global development of Islamic finance

Islamic finance is one of the fastest growing segments of the global financial services industry. Shariah-compliant financial assets have been growing at over 10 per cent per annum over the past 10 years. Measured by Shariah-compliant assets of financial institutions, the global Islamic finance industry is estimated at US$822 billion in 2009 (Austrade 2010). Austrade (2010) identifying the following factors pertinent to the growth mentioned thereof:

- petrodollar liquidity: Foreign investment plays an important role for petrodollar investors, whose domestic economies and financial systems are too small to absorb all capital from oil export revenues. This presents significant opportunities for the Islamic banking and finance industry. Petrodollar liquidity is expected to remain high over the long term due to the finite supply of oil reserves;
- Muslim population: Relatively rapid Muslim population growth worldwide and rising living standards will see increased demand for Islamic finance;
- low penetration levels: In spite of growth in the Islamic banking and finance industry, there remains a lack of depth across asset classes and products, signifying untapped potential. There is considerable scope for further development of Islamic banking and finance in countries such as Indonesia, India and Pakistan, which have the largest Muslim populations in the world; and
- ethical character and financial stability of Islamic financial products: Islamic financial products have an ethical focus (notably excluding investment in alcohol and gambling) and a risk profile that will also appeal to a wider ethical investor pool.

Currently, the Middle East and South East Asia are the primary locations for Islamic capital. In particular, the United Arab Emirates, Bahrain and Malaysia are seen as the main centres of Islamic finance, with significant activity also taking place in the United Kingdom and more recently in Europe, Africa and Indonesia. The demand for Islamic finance has not been matched by supply despite the rapid growth in the sector in recent years. An increase in supply is necessary to meet current and expected demand.

2.2. Opportunities of Islamic finance in Australia

Islamic finance has considerable potential to become an important element in Australia’s aspirations to be a global financial services centre in the region. It has the potential to facilitate further innovation and competition in the wholesale and retail banking sectors and to support the Australian Government’s commitment towards credit market diversification. Australia’s growing trade linkages with Asia reflect the demand for Australian commodities from developing countries such as China and India. Of the top 10 trading partners, eight are in the Asia Pacific Region with China and Japan being the country’s top two-way trading partners. Continued growth in major Asian economies will result in a need to develop resources-related services and infrastructure, which are ideal assets for some forms of Islamic financing, such as Sukuk, Mudaraba, Murabaha and Ijarah. Australia is well positioned to structure and offer such instruments as part of financing packages for resources-related development. Australia’s Muslim population of 365,000 (1.7 per cent of the total population), exceeds the combined Muslim population of Hong Kong and Japan and is more than half of that of Singapore. Australia’s political stability and geographic position, especially its proximity to the large Muslim populations of the Asia Pacific where 62 per cent or 972.5 million of the world total Muslim population resides, present an important base to service this fast growing sector in the global financial services market (ABS 2010). Australia’s attractiveness as a financial centre is supported by a sizeable domestic economy and financial
market. The nation has the fourth largest economy in the Asia Pacific (after Japan, China and India). Australia’s finance and insurance industries generate around 8.1 per cent or A$82 billion of real gross value added (Austrade 2010). Australia is well placed to take advantage of the Islamic finance opportunity, with widely recognised strengths in retail and commercial banking and experience in infrastructure, property, resources and agricultural financing. Specific opportunities for Australia include:

- attracting foreign full-fledged Islamic banks and conventional bank Islamic windows to establish operations in Australia;
- attracting investment in Australian assets and businesses from overseas Shariah investors and tapping into new funding sources through Sukuk and other securitised issues;
- Australian-based banks providing from Australia a range of Shariah-compliant investment and financing products and services to Islamic banks, corporations, institutions and high net worth individuals in the Asia Pacific and the Gulf regions;
- fund managers establishing Shariah-compliant funds for Asian and Gulf institutional and high net worth individual investors;
- local exchanges providing an Islamic listings platform for domestic and international issuers of Shariah-compliant instruments;
- provision by Australian-based financial institutions of Shariah-compliant/ethical financial services and products to Muslim and non-Muslim customers in Australia;
- Australian-headquartered banks and insurance companies exporting Islamic financial services through windows as they grow their operations into Asia; and
- Australian-based financial firms, professional services providers and educational institutions exporting their services into Asia and the Gulf.

2.3. Australian governments’ supportive policies toward Islamic finance
Australian Federal and state governments recognise that growth of Islamic finance in Australia requires supportive government policies. It is important that there is (NSW Government 2009):

- a level taxation, legal and regulatory playing field for Islamic and non-Islamic finance. Taxation must be responsive and enabling but non-preferential;
- strong promotion and facilitation through government investment attraction and export promotion agencies;
- government engagement with the private sector in achieving Islamic finance objectives, identifying impediments to, and opportunities for growth;
- a focus on deepening Islamic finance skills – education, training, attainment of relevant qualifications – and on access to appropriate Shariah scholars; and
- growth in Islamic finance professional services providers.

2.4. Regulatory and governance framework of the financial service sector in Australia
The government regulation and corporate governance of the financial service providers are intertwined in the Australian context. Government regulation can be defined as (1) a principle, rule or law designed to control or govern conduct of people and business; (2) the way a particular regulation is implemented in practice. This definition incorporates not only legislation and formal regulation, but also quasi-regulation, for example, a code of conduct or advisory instruments (Banks 2006).
Corporate governance can be defined as:

The system of regulating and overseeing corporate conduct and of balancing the interests of all internal stakeholders and other parties (external stakeholders, governments and local communities ...) who can be affected by the corporation’s conduct, in order to ensure responsible behaviour by corporations and to achieve the maximum level of efficiency and profitability for a corporation (Du Plessis, Bagaric et al. 2010, p. 10).

Thus corporate governance is not simply a product of government regulation. Companies have inherent incentives to establish governance procedures to demonstrate their bona fides to investors, in order to attract capital. Executives also have incentives to deliver good performance to maintain their professional reputations. But rules can reinforce such incentives and diminish the risk of a loss of confidence in a market resulting from poor behaviour of a few. However, as it is evident in Figure 1, the religious component of the governance of the Islamic financial service companies has been largely ignored. The identified gap signals two questions: 1. Does the ‘one size fits all’ model work? And, 2. If not, what are the alternatives? Answers to these two questions will be provided in the following sections.

Figure 1   The regulatory and governance framework of the financial service sector in Australia

Note: Acronyms are as follows — a. ACSI: Australian Council of Super Investors; AICD: Australian Institute of Company Directors; APRA: Australian Prudential Regulation Authority; ASA: Australian Shareholders’ Association; ASIC: Australian Securities and Investments Commission; ASX: Australian Securities Exchange; IFSA: Investment and Financial Services Association. b. Listed public companies will predominantly be ASX-listed entities. Exceptions are companies listed on other Australian stock exchanges, such as the National Stock Exchange of Australia and the Bendigo Stock Exchange. c. Most ASX listed entities would be listed public companies in the context of the Corporations Act. Exceptions include some listed trusts and companies incorporated outside Australia. d. Some APRA-regulated banks and insurance companies would be ASX-listed entities. However many, including credit unions, building and friendly societies, and superannuation funds are not ASX listed.
3. FINDINGS AND DISCUSSION

Legislation for the regulation of financial services is developed by the Commonwealth. The Australian Securities and Investments Commission (ASIC) implements and administers the law. Many financial services are also regulated by the Australian Prudential Regulation Authority (APRA).

ASIC administers the Corporations Act 2001, which requires people who carry on a business of providing financial services to hold an Australian Financial Services (AFS) licence (unless they are covered by an exemption or are authorised as a representative of an AFS licence holder).

Islamic financial products are regulated in the same way as any other financial product in Australia. Regulation is generally in terms of product approvals, disclosure and accounting standards, standards for intermediaries (i.e. stockbrokers), as well as regulation of non-banking entities such as collective investment schemes. Regulation of the finance sector is designed to maximise market efficiency, with minimal regulatory intervention to protect investors.

In Australia, the regulators treat Islamic financial services providers as a normal financial company; hence there are no shariah law-binding requirements (Figure 1). The complexity of the regulatory compliance requirements is only contingent on whether the company is listed on the stock exchange. Obviously, the regulators have yet to be educated about the fundamentals of Shariah law and Islamic finance.

Regulation to protect investors is limited to conduct and disclosure requirements imposed on AFS licence holders. Licensees authorised to provide advice about financial products are required to meet certain minimum legislative standards when advising clients. The National Consumer Credit Protection Act 2009 (Cth) is designed to provide additional safeguards and protections for consumers to the process of obtaining credit in Australia. This covers all types of consumer credit from credit cards to mortgages.

APRA is the prudential regulator of the Australian financial services industry. It oversees banks, credit unions, building societies, general insurance and reinsurance companies, life insurance, friendly societies, and most members of the superannuation industry. In essence, APRA ensures that regulated entities honour the financial promises made to beneficiaries. It creates and administers an extensive set of prudential standards to give regulated entities extensive guidance in matters such as risk management and minimum capital levels. Recent decades in Australia has witnessed the shift of the regulatory reform from ‘one-size fits all’ model to a responsive regulatory paradigm. At the same time, the governance reform extended the shareholder hegemony model to the stakeholder model, which takes into account not only the shareholders, but also other stakeholders such as employees, customers, investors, community, suppliers and industry associations.

There is no single or enduring best-practice model for corporate governance: different approaches and combinations of approaches can promote alignment and trust, while company structures and market expectations change over time. Indeed, the diversity of companies makes flexible governance arrangements highly desirable — one size is unlikely to fit all. In addition, regulations designed to promote alignment and accountability, if they are excessively prescriptive, have the potential to impede the ability of managers to manage. To accommodate diversity and to balance objectives, Australia’s corporate governance framework has accordingly evolved over time, combining ‘black letter’ law with ‘soft’ law requirements, as well as other industry-based guidance.

Moreover, a properly designed regulatory regime catering to the needs of the Islamic financial service providers must imbed the Shariah principles in the regulation design and implementation, while taking into account the distinct features of the Islamic institutions.
Hence, governance mechanisms related to the Islamic financial service companies should incorporate the internal governance and external governance (Gillan 2006). Internal governance may include the Shariah board, board of directors, sub-committees and internal control mechanisms such as internal audits; while external governance may include market control and regulation.

Of relevance to the internal governance of Islamic financial institutions are two prominent theories, one is the dominant Agency Theory and the other the Stakeholder Theory. While the regulatory options, with a particular interest in design and enforcement here, may include coercion via ‘black letter’ law (also known as the public ordering), self-regulation via ‘soft’ law (also known as private ordering) and internal governance, as well as the hybrid of the two options. These two paradigm shifts are discussed as follows.

3.1. Corporate governance: shareholders or stakeholders?

The Agency Theory originated from Jensen and Mackling (1976) who contends that firms are the nexus of the contracts. The essence of the agency problem is the separation of management and finance. Due to the incompleteness of contracts, managers withhold control over the residual control rights, which are not foreseeable ex ante. Thus, corporate governance concerns with managers putting constraints on themselves, or investors putting constraints on managers, so that the misallocation problem can be reduced and investors will be induced to provide more funds.

Freeman’s Stakeholder Theory intends to address three problems: (1) the problem of value creation and trade; (2) the problem of the ethics of capitalism; and (3) the problem of a managerial mindset (Freeman et al. 2010, p. 29). Freeman et al. (2010) holds that: (1) the basic objective of a firm is to create value for stakeholders; (2) business is a set of relationships among groups which have a stake in the business activities; (3) business is about how customers, suppliers, employees, financiers (such as stockholders, bondholders, banks, or investors), communities, and managers interact and create value. To understand a business is to know how these relationships work. In this context, the executive’s or entrepreneur’s job is to manage and shape these relationships. Hence, stakeholders are defined as customers, suppliers, employees, investors, communities, and managers who interact and create value for firms.

Li et al. (2012) find that Profit-sharing Investment Accounts (PSIAs) holders may suffer from lack of protection due to information asymmetry. Consequently, PSIAs-holders may expect a high risk premium by increasing the cost of capital, or may withdraw their deposit. Hence, corporate governance in Islamic financial service institutions should aim at protecting investors’ rights as well, which warrants the appropriateness of the adoption of stakeholder theory.

3.2. Regulatory theories: public ordering vs. private ordering

Given that the Agency Theory’s omnipotent focus is on developing corporate governance mechanisms to solve the distributed shareholding problem in large corporations, it failed to consider the other stakeholders, particularly the Islamic beliefs. From a legal perspective, governance requirements deserve scrutiny on balancing the expectation of the Islamic financial service providers and that of the regulators.

McCahery and Vermeulen (2008) analysed corporate governance for non-listed companies and provides a detailed explanation of public ordering and private ordering. Public ordering is also called hard law, which cover the legal requirements, rules and regulations. Private Ordering is the process of setting up of social norms by parties involved in the regulated activity, and not by the State. Private Ordering aims to achieve public goals, such as
efficiency, enhancing the market, and protecting rights. Private Ordering may include customised contracts and private arrangements amongst different stakeholders. Incorporating self-regulation of the international regulatory requirements into the regulatory model (Figure 2), Islamic Financial Service providers who are members of the International Financial Service Board (IFSB) has to be abide by the IFSB guidelines and The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) guidelines, as well as other industry/product specific regulatory guidelines whenever applicable, which are either ‘rule-based’ or ‘principle-based’ and requires ‘comply or explain’ compliance requirements. If a member organisation fails to comply with the guidelines, it has to explain why the regulatory requirements had not been met (or ‘if not, why not’).

Figure 2 Regulations of Islamic Financial Institutions in Australia

3.3. Developing a responsive regulatory framework for Islamic finance sector in Australia
Given the complexity of the corporate governance issue in Islamic finance companies and the heterogeneity of Islamic companies at large, the hybrid approach which combines the public and private orderings, seems to be a better option. Specifically, regulators, Islamic finance companies, and the other stakeholders should make joint effects to solve governance problems in the operation of small corporations, detailed proposal will be presented as responsive regulation below.
Since the influential work of the Chicago school of economics in the 1960s and 70s, economists, lawyers and social scientists have been interested in government regulation and its efficacy (Stigler 1961, 1971). The international literature has been concerned with regulation that is both ‘effective’ and ‘responsive’ in order to ensure that government is attuned to differing motivations of regulated actors (Ayres and Braithwaite 1993). Much of
the literature has argued for less government intervention and for the need to formulate efficient legal rules to foster an optimum environment in which small corporations can flourish.

The best regulatory strategy depends on context, regulatory culture, and history (Ayres and Braithwaite 1993, p.5). Cultural, social, economic and political imperatives are vital. In Australia, for example, the Hawke federal government introduced the notion of regulatory impact statements, and such statements are now commonplace in other contexts, such as the environment: efficacious regulation should speak to the diverse objectives of regulated firms, industry associations, and individuals within them (Ayres and Braithwaite 1993).

The responsive regulatory system model builds on the McCathery and Vermeulen’s three pillars of regulation on governance of non-listed small businesses (2008 p. 12) and Ayres and Braithwaite’s responsive regulatory model (1993, p. 21). It advocates that the regulation of small corporations should not be ‘one size fits all’, but responsive to the contextual contingencies and responsive to the compliance responses from small corporations. Though the responsive regulatory pyramid was first developed to address the regulatory compliance issues by Ayres and Braithwaite, it offers an excellent opportunity to present the self-regulated corporate governance and coerced regulation in a continuum.

Proper corporate governance mechanisms may serve as a self-regulatory mechanism, which requires the least regulatory cost, sitting at the bottom of the ‘regulatory pyramid’ (Ayres and Braithwaite 1993). While government regulation serves as enforcement or coercion, and demands a significant amount of resource and efforts to comply with, sits at the top of the pyramid. The other private arrangements in the form of customised contracts, optional guidelines, good practices, and corporate governance system serve as self-regulatory mechanisms. The hybrid may involve interactions between the external environment and internal environment of the Islamic finance companies, including regulation of corporate governance, optional guidelines, CSR, social networks, public-private partnership. Such requirements are responsive to the size of the Islamic finance companies, the development stage on the business life cycle, the industry that Islamic finance company operate and business connections with the government and government agencies. Responsive regulatory system has a strong focus on generating incentives for regulatory compliance (Braithwaite 2006).

Given that the responsive regulatory framework has proven to be effective by a number of applications in regulatory design in Australia and overseas, for example, the Australian Taxation Office, it should replace the current ‘one size fits all’ model. It has to be implemented by joining the efforts of multiple parties, including the governments and their agencies, Islamic finance companies, industry associations and the community.
Different from the previous two models (as presented in Figure 1 and Figure 2), the proposed Responsive regulatory framework for Islamic finance companies incorporates the public ordering (through legislation and coercion), private ordering (through private arrangements) and the hybrid (through reactions to the regulation responsive of the contingencies such as firm size, development stage, and industry structure). One may see regulation as the external governance of corporate governance (Gillan 2006). Similarly, one can also view corporate governance as a special form of regulation - self-regulation. The proposed model has two ultimate objectives, one is to abide by the Shariah law, and the other is about optimising the stakeholders’ interests.

Comparing to the ‘coercion only’ regulatory model and the ‘self-regulation only’ model (or lass faire), the ‘responsive’ is able to engage the stakeholders at different stages hence may significantly reduce the monitoring and reporting costs. The responsive regulatory model suits the Islamic financial service providers’ need in both religious and financial terms and they
have the autonomy to select the optimal combinations of the SSB or market mechanisms for the certification of their products and transactions. The timely evidence-based evaluation system ensures the feedback to be incorporated in the planning and reforms, hence increasing the responsibility and sustainability of the Islamic financial institutions. Thus the responsive regulatory option outweighs the alternatives.

The responsive regulatory framework can be operationalised as a ‘seven-stage model’ (Figure 4). The seven stages include

Stage 1: Identifying the governance and regulation problem
Stage 2: Identify the objectives of governance and regulation
Stage 3: Establish the baseline of regulation as per the ‘public ordering’
Stage 4: Develop the self-regulatory mechanisms
Stage 5: Identifying the hybrid mechanisms
Stage 6: Establish a code of conduct & transfer the good practice into policies & procedures
Stage 7: Develop an evidence-based evaluation system to monitor the progress and provide feedback to Stage 1.

Figure 4 A Seven-Stage Responsive Regulatory Model for Islamic Financial Institutions in Australia

4. APPLICATION OF THE PROPOSED MODEL: CORPORATE GOVERNANCE OF THE SHARIAH SUPERVISORY BOARD (SSB)

This section applied the seven-stage model (Figure 4) on the corporate governance of the SSB.

Stage 1: Identifying the governance and regulation problem
The SSB is a binding requirement in the Shariah Law as the ‘public offering’ which has the coercion power. Hence, a SSB has to be presented in order to meet the religious requirements. However, the SSB becomes a corporate governance issue due to that set rules are yet to be establishment on the selection, composition, assessment and dismissal of the SSB members. While some international jurisdictions have established regulatory requirements for the appointment of Shariah advisory bodies, there is no standardised requirement across jurisdictions in respect of the eligibility and qualification of Shariah advisors (IOSC 2004). Should the SSB members be elected or appointed?
The stakeholders in this problem include the regulators from IFSB and AAOIFI, national and local level regulators, investors, directors of the SSB and the board of directors.

**Stage 2: Identify the objectives of governance and regulation**

The objectives of the introduction the SSB is to bind with the Shariah compliance as well as improving the Stakeholders’ interests.

The credibility of the Islamic finance sector is a paramount concern to the majority of stakeholders. The importance of trust in the Islamic capital market was repeatedly raised by stakeholders and reputation is seen to be an essential component of establishing Islamic businesses anywhere in the world.

Shariah is open to interpretation and scholars frequently hold varying views on key Shariah issues. Islamic jurisdiction is not bound by precedent, and opinions may deviate from previous decisions made by other Shariah scholars. This lack of standardisation may become a cause for concern. It may result in different transactions being interpreted differently, leading to consumer uncertainty regarding Islamic finance products.

National and state regulations often necessitate a compromise of Shariah compliance in Australia – for example, the requirement to declare the level of interest on a mortgage contract, which is not appropriate for Islamic mortgages. However, in instances like these where there is no legal alternative Shariah scholars allow a degree of flexibility in the application of Shariah law. This flexibility is also not uniformly applied.

The pool of Shariah scholars from whom to draw advice upon financial products is relatively small in Australia. Notably, many of the wholesale providers currently seek compliance endorsement overseas. Other jurisdictions that have a mature Islamic capital market, such as Malaysia and Dubai, regulate Shariah compliance.

The lack of industry standards or regulation of Shariah compliance gives rise to three possible problems:

- Allowing potential rogue operators to flourish and damage the reputation of the Islamic finance sector in Australia;
- The compromise of consumer confidence in cases where the interpretation of Shariah compliance does not meet with common interpretation, or where the Shariah ruling is not disclosed;
- The decline in international investment if Shariah compliance does not meet international standards.

**Stage 3: Establish the baseline of regulation as per the ‘public ordering’**

The establishment of the SSB requires that the directors to be elected have to possess sufficient Shariah knowledge and should exercise Shariah compliance checks as an internal auditing mechanism. Other requirements may be pertinent to the regulatory requirements for financial service companies in Australia.

**Stage 4: Develop the self-regulatory mechanisms**

Financial institutions have their own in-house independent Shariah advisory bodies that screen and endorse their Islamic products. The Shariah certification process is generally undertaken by private sector in-house Shariah advisory bodies, driven by private sector-led initiatives, and is not mandated by any specific regulatory or policy requirement. The SSB may have to work with the Shariah advisory bodies in order to exercise a final check.

An industry-led ‘Shariah compliance board’ was proposed as a means by which to regulate Shariah compliance and secure the market nationally. It may be the case that the current Islamic market in Australia is too small to warrant introducing additional regulation at this time. Alternatively, the industry could develop its own set of voluntary standards. There is benefit to developing an industry voluntary code of conduct for Shariah boards as an industry development exercise. A voluntary code would provide additional certainty for investors as to
the Shariah compliant nature of a product (i.e. brand integrity) and maintain industry standards at an international level. This approach would have the greatest benefits if adopted nationally.

Industry codes of practice have been developed by a number of industry associations in the financial services sector. They range in content from general statements of principle about how the financial services industry operates, to listing specific industry practices which are guaranteed by the code.

**Stage 5: Identifying the hybrid mechanisms**

Appropriate Shariah certification is issued for all Islamic capital market products and services e.g. in Malaysia, Indonesia, Sudan and Pakistan. The Shariah certification process is undertaken at the regulator’s level, under the guidance of their own Shariah advisory bodies to formally advise on issues of Islamic capital market products and services. Shariah compliance issues are taken into consideration in the regulator’s functions such as product approval, eligibility criteria for intermediaries, reporting requirements of regulated entities, and enforcement of regulatory requirements.

**Stage 6: Establish a code of conduct and transfer the good practice into policies and procedures**

Existing codes either contain minimum standards or standards which are aimed at best practice, some examples include the Finance Brokers Association of Australia’s Code of Practice & Disputes Resolution; and Financial Services Council’s Code of Conduct and Code of Ethics.

In recognition of the strong stakeholder support the national and local level regulators should facilitate stakeholder development of a voluntary code of conduct for Shariah boards in order to promote industry development.

The code of conduct, as well as the procedure of SSB director selection, evaluation, compensation and removal and other good practices as well as lessons learned can be codified into policies and procedures to govern the operation of the Islamic financial institutions.

**Stage 7: Develop an evidence-based evaluation system to monitor the progress and provide feedback**

Evidence-based system can be introduced to evaluate the performance of the proposed responsive regulatory system. Any feedbacks can be incorporated into Stage 1 for another round of reform.

As mentioned at the beginning of the case, Abdul and David had been challenged by the perplex but yet to be developed regulatory framework for Islamic finance companies in Australia. The abovementioned seven-stage model offers a guidebook for them to analyse any governance and/or regulation problems at any stage of the development of their Islamic financing businesses.

5. **CONCLUSION, LIMITATIONS AND FUTURE WORK**

After investigating the potential development opportunities of Islamic finance in Australia, it was found that their regulatory requirements have been largely ignored. As such, the shadow existence of Islamic finance has been further impeded by the unintended consequences of ‘one size fits all’ regulatory model. A responsive regulatory model was developed (Figure 3), followed by its seven-stage operational model (Figure 4) to guide application of the proposed responsive regulatory model. Furthermore, the responsive regulatory model has been applied to the corporate governance of the Shariah Supervisory board. The model, comparing to the extant ‘one size fits all’ model, it has shown advancement in efficiency, suitability, accountability and sustainability.
Admittedly, this study is subjected to the limitation that it only focused on the Islamic finance in Australia from the macro-level. Hence, future endeavours may be devoted to micro-level analysis, which analyses the regulatory compliance behaviour of each individual Islamic financial service provider in Australia.

**LITERATURE**

THE ROLE AND FUNCTION OF SMALL TOWN IN REGIONAL DEVELOPMENT - CASE STUDY: SORAK TOWN

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ABSTRACT
The purpose of this paper is to study the role and function of Sorak town as a small civic center in the regional development. The current town of Sorak in Miyandorood city, Mazandaran province, is one of the towns which have been changed into a town in 1995. The present study has been descriptive-analytic and the process was library and survey. In this direction by choosing 6 functions (1. Clinical/Medical, 2. Educational/Cultural, 3. Telecommunicational/Communications, 4. Agricultural, 5. Commercial/Services, 6. Political/Administrative) in the form of 35 variables and using network analysis method we have studied and compared the current affairs and relations in the understudied village in two intervals before and after Sorak becomes a town. The results of studies indicate that Sorak town as a central place, have played an important role in giving services to the regions in its surrounding which has consequently caused to reduce the dependence of rural regions to city center of Sari.

Keywords: Network Analysis, Regional Development, Small Town.

1. INTRODUCTION
The less-developed countries have raised this issue that the development of the small and medium towns cannot be regarded as a gradual and automatic process. On the contrary, they get rapid spatial distribution through well-thought and purposeful policies with a well-accepted and appropriate prospective outlook. Nowadays, the relations of the cities and villages have expanded diversely due to all the vast technological, commercial and social revolutions, especially the ones in transportation and road links. These relations manifest themselves in terms of population, goods, doctrines, capital, information and creativity. In the past few decades, there have been many strategies proposed for rural development one of which that has a spatial approach, is establishing and strengthening the small towns and town-villages (Satterthwaite and Tacoli, 2003, 56). Within our developing world, urban concentration has caused so many problems in large cities of which dense population (crowdedness), immigration, lack of accommodation, unemployment and environmental destruction could be brought up as examples (Lynch, 2004, 27). Consequently, the urban and regional analysts have devoted their attention to the development of small and medium towns as a necessary strategy to overcome the imbalance caused by the development of large cities. As long as the growth is limited to some certain cities, these cities are more inclined to more development and as a result, the smaller urban zones will be subject to less gradual transformation and growth (Silberfein and Kessler, 1988, 87).

Generally, the rural and urban development will be fulfilled through bilateral links and interactions. On this basis, in development planning processes, the strengthening and growth of the large villages (small towns) could not be ignored. In fact, these centers provide facilities and services to their surrounding areas and therefore, could play an integral role in developing rural regions (Trager, 1988, 31). In an overall outlook, the small towns could be regarded as centers, which play an important role in reinforcing the incentives for rural growth and development of their region of interest (Dalal-Clayton et al, 2003, 124). There is
no hierarchical function for the urban network in Iran and the residential centers, spatial
distribution, and population volume do not follow a hierarchical functional system, therefore,
the urban network keeps evolving in centricity (Hashemzahi et al., 2014, 1071). On the other
hand, if the goal of development in a country is the development of all non-urban regions in
order not to only have cities developed but also rural areas, then one major effort would be
taking the small towns into consideration and to assess and appoint them for regional
development (Fanni, 2008, 117).

Based on this policy, setting up new towns, reinforcing planetary towns, and transforming
large villages into small towns have been implemented by urban and regional planners in
order to decentralize and depolarize large cities and to revive the urban hierarchy. In the past
few decades, many rural zones have been transformed into urban zones through the policy of
turning large villages into towns, and that is why the number of urban zones has increased to
more than 1000 in Iran (Mahdibeigi et al., 2010, 159).

In 2015, the number of urban zones has reached to 58 in Mazandaran province and most of
these zones had been originally formed from rural regions. The town of Sorak (the centre of
Koohdasht rural district) is one of these rural centers which has been changed to city in 1995.
Koohdasht is one of the rural districts of Central district located in Miyandorood city; the
center of which is Sorak town (Iran Statistics Centre, 2015).

Concerning the goals of changing large villages to towns, the present paper has been brought
forth for discussion to study the function of Sorak city in the development of surrounding
villages and also to give an answer to this question: could Sorak city, as a small town, play a
key role in providing services for the rural regions in its surrounding and consequently reduce
the dependency of these regions to the center of township?

In this direction, the function of Sorak city in providing services for villages of rural
district has been analyzed by using network analysis method and comparing the results before and
after that.

2. MATERIAL AND METHODS

The research method is based on the application objective and descriptive data (non-
experimental) collected via survey. The method for collecting information and data is the
library and field method. In the field method the means for collecting information are
questionnaires.

Through using network analysis methodology in this research, the most efficient functions
within this rural district as well as the interactions and links between the town of Sorak and its
surrounding villages were studied before and after the transforming of this village into a town.
In network methodology, the binary pair of 0 & 1 is used to refer to the existence or non-
existence of relations between two factors or two residencies within one complex.

These functions are:
1-Clinical/Medical, 2-Educational/Cultural, 3- telecommunicational/communications, 4-
Agricultural 5- Commercial / Services, 6- Political/Administrative.

Each of these functions was evaluated based on the most functional parameters (35
parameters). Of the region which are as follow: Clinical/Medical function including: Clinical
Medical Centre, Clinical House, Physician, Medical Assistant or Midwife, Clinical
Assistance, Clinical Trainee, Dentistry, Pharmacy. Educational/Cultural function including:
Primary School, boy elementary School, girl elementary School, Males’ High School,
Females’ High School, Males’ gymnasium, Females’ gymnasium, Public Library.
Telecommunication/communications functions including: Post Box, Post Office,
Telecommunication Office, Access to Public Transportation, Access to Newspapers and
Magazines. Agricultural functions including: Farming Machines Repair Center, Shopping Center of Surplus Harvest, Agricultural Implements Stores.
Commercial and civil including: Cooperative Stores, Home Appliance Stores, Building Materials Stores, Stationary Stores, Food Stores, Gas Station, Post Bank.
Political and Administrative function including: Islamic Council of Village, Basij Centre, Police Office and Corporation Company of Village.

2.1. Network analysis method
In regional science different methods have been used and suggested for analyzing patterns relations and hierarchies of human residential places. One of these methods is the method of social network analysis. Researchers use statistical models based on network analysis for about 60 years. The purpose of these models is a quantitative testing of the specifications of social relations among factors and components of a specific network. The range of these applications is from the studies on action and reaction between personality’s internal relations friendship and leadership studying the relations among groups and the studies of society’s political behavior and power sector. This method is used to determine the key residential place among different kinds of residential places by considering the number of internal dependencies in one system. This method should:
1) Describe the dependence and relations among residential places in one region.
2) Determine the degree and importance of a residential place or a set of residential places.
3) Indicate the sensibility of the structure of a residential place in the absence of some specific residential places.
It seems that network analysis method proper for all three above-mentioned points.
The network analysis method is widely used in social sciences and transportation researches but it has been rarely used in determination of key or vital residential places.
The foundation of network analysis is based on analytical data framework, which is dependent to information and hypothesis. Data may include data in the relations as well as action and reaction among people or individual or group attitude. The connection and dependence of two pair is called relation. the relation of data are selected by means of personal studying and negotiating the action and reaction with others. the relations are just between factor pairs and these pairs or binaries are proper units for the analysis of relations.
For example, two cities connected with a road between them and shops with the customer are kinds of pairs. The data in social transaction are put in a matrix, which is calls social matrix. The social matrix indicates sender factors to receiver factors. A social matrix is not a close frame however, the sender and receiver may be different or the same.
There are two basic kinds of relations in network analysis:
1) Bilateral or evaluated
2) Direct and indirect
Bilateral relation (0-1) is the existence of non-existence of relation between two factors or residential places in a residential complex and a value relation concerns intensity and abundance of a relation besides its presence or absence.
A direct relation has a clear origin and end. An indirect relation is not clear in relation with the origins of flow. An indirect relation is usually indicated as an arrow. A line between related factors is not specified by arrowhead. An arrow usually indicates a direct relation specified by arrowhead at the end. For example, if village A sends its student to village B the direction of education relation is from A to B, which reflects the educational.
Based on social network analysis, nodes are very important. There are some criteria to measure the importance of a node, which includes local centralization, Local Credit and General centralization.

Local centralization: Reflect the number of direct transfers and therefore is measured by the external degree of each factor.

Local Credit: indicates the number of direct receiving and is measured by internal degree for each factor.

Whenever the internal degree is zero the and external degree is not zero, a factor is called origin or transfer; which means the local of rows is zero but the linear total has a non-zero factor. If external degree is zero and internal degree is non-zero the factor is called receiver. An isolate factor is the one with both internal and external degree of zero. Following digraph and matrix are a clear example that specifies the relation four nodes:

As we see, A is transferer, B is vector, C is receiver and D is isolated factor. When there is no arc to attach a node to other nodes of the network, the node is called isolated one. The adjacency Matrix for this digraph is as follows which indicates that A is in relation with B, B is in relation with C, C has no relation with outside, and D has no relation with others and is an isolated node (Table 1).

### Table 1: The relation between residences of assumed nodes (Rezvani, 2009, p. 216)

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<tr>
<th></th>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
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</thead>
<tbody>
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</table>

General centralization: if a factor has the shortest distance from other factors, it is called central factor. The distance between factors is measured by nearness. Playing the role of being centre, it is measured by the mean.

Nearness is the opposite of distance. The less the distance of i with other factors is, the more it is near to centre, from mathematical point of view we have:

In which is the shortest distance between i and j in the network and N is the size of network. This criterion depends on the size of network (Rezvani, 2009, 216).

3. RESULT

In order to study the functional role of Sorak (as a small urban center) in giving services to rural regions of the under study rural district, using network analysis method we have studied the flows and service relations which are under study (Clinical-Medical, Educational-Cultural, Telecommunicational-Communication, Agricultural, Commercial-Services, Political-Administrative) in Kooohdasht rural district in two sections before and after Sorak becomes a town. The sum up of all present flows and service relations of the under study region in two chronological sections of Tables 2 and 3 and figures 2 and 3 indicates that:

During the first section almost all of the villages of Kooohdasht rural district have been linked to the city of Sari with the internal degree of 18, however, the village of Sorak with the internal degree of 5 had the least interactions among the rural district (Table 2).
Unlike the first section in which Sorak has been dependent to Sari for under study services, during the second section it had no dependency to Sari (the external degree is zero after becoming a town). Considering flows and relations, Sorak city receives no services from rural points during first and second sections (Table 3).

During the first section considering the centralization of all services in Sari, rural regions of the rural district of Koohdasht had the most dependency to this city and villages Janasem, Usa, Morsam, Sarta and Asram (with external degree of 2) have been dependent to the present town of Sorak besides the city of Sari. But during the second section by centralizing these kinds of services in Sorak (unlike first section), The dependency of the residential places in rural district to Sari has been decreased and just the villages of Kiapi and Esbukola are dependent to the city of Sari considering their low distance to Sari and other rural regions are only dependent to Sorak (Figures 1 and 2). In other words before becoming a town the internal degrees of Sari and Sorak have been accordingly 5 and 18. After becoming a town, it is observed that the internal degrees of Sari and Sorak are accordingly 15 and 2 (Table 2 and 3).

During the first section except for Sorak that had given services to five village, the rest of villages in the studied rural district not only give services to other residential places but were not capable of providing services even to their inhabitants (having internal degree of zero) (table 2).

Also, considering that the total of rows and columns of tables (internal and external degree) is not zero during both sections before and after becoming a town, it is observed that there is no isolated and distinct place during each section in the studied zone and these residential places are the sender of services to other regions or receive services from other regions (Table 5).

Studying the percentage of density in each operation based on table 4 indicates that the density of operations in comparison with the previous section has been improved to some extent and the reason is the establishment and dispersion of these services in rural regions of the rural district and consequently the relations among residential places has been increased comparison with previous section.

Studying the percentage of density of all flows in two sections before and after Sorak becoming a town shows the density of flows in the first section is 4.97 and in the second section is 6.72. Therefore the comparison of density in both sections indicates the improvement of density of flows and the increase of relations between residential places of the studied region (Table 4). Studying the value of centralization (nearness) in the section before and after Sorak becoming a town based on Table 5 indicates that in both section in the studied region, Sorak has had a more closeness to other residential places. Table 6 and 7 depict the level of facilities and services in the residencies of Sorak in the two periods of before and after Sorak transformation. In these tables, the relations in six different forms including 35 parameters are studied: 1- Clinical-Medical, 2- political-Administrative, 3- Educational-Cultural, 4- Telecommunicational-communications, 5- Commercial – Services and 6- Agricultural. As it is clear in the table, the external degree of clinical-medical function has increased from 24 (before transformation) to 38 (after transformation), and the concentration of function has increased from 7.02 to 11.11. The political/administrative function has increased from 21 to 26 in its external degree and its concentration has moved from 6.14 to 7.60. The external degree of educational-cultural function has increased from 42 to 50 and its concentration from 12.28 to 14.62. The external degree of telecommunicational-communications function has increased from 9 to 35 and its concentration from 2.63 to 10.23. The external degree of commercial-services function has increased from 19 to 34 and its concentration from 5.55 to 9.94. The overall view on all functions shows the external degree has increased of 17 to 23 and the concentration from 4.97 to 6.72 (Table 4).
4. CONCLUSION

Utilizing network analysis methodology, this research has been an attempt to analyze the relations and functions of concern before and after the transformation of Sorak into a town in order to study the role and function of Sorak in developing the surrounding villages. The analysis shows that the transformation of Sorak into a town has had a positive effect on providing services to the other residencies such as the residencies of Sorak. Before the transformation of Sorak into a town, it was not able to provide services to the villages, and therefore, all its surrounding residencies in addition to itself were dependent on Sari which is located 12 km away from the Sorak zone.

In this phase, villages Janasem, Usa, Morsam, Sarta and Asram (with external degree of 2) have been dependent to the present town of Sorak besides the city of Sari. But during the second section by centralizing these kinds of services in Sorak (unlike first section), The dependency of the residential places in rural district to Sari has been decreased and just the villages of Kiapi and Esbukola are dependent to the city of Sari considering their low distance to Sari and other rural regions are only dependent to Sorak.

As a result, through analyzing the obtained data and the regional studies in the zone of our concern, we are witnessing that by transforming Sorak into a small urban spot (central location), this city has gained a key role in providing services to its surrounding villages as well as decreasing the dependency of the concerned villages on Sari.

Furthermore, the rural concentration analysis of functions and relations shows that this rate had been 4/97 before the transformation of Sorak into a town and 6.72 after the transformation. This fact simply indicates more links among the rural residencies within the second period.

Thus, it could be concluded that the town of Sorak as the central zone could establish the maximum level of contact to its surrounding residencies, and consequently plays an integral role as a catalyst for rural development and an obstacle to stand against the immigration to larger cities.
### Table 2: Summation and analysis of all flows and relation in the studied zone before becoming a town Sorak

(Research findings, 2015)

<table>
<thead>
<tr>
<th>Residential place</th>
<th>Darabkola</th>
<th>Baziarkhey</th>
<th>Sanahkoooh</th>
<th>Janasem</th>
<th>Usa</th>
<th>Varmi</th>
<th>Morsam</th>
<th>Badele</th>
<th>Esbukola</th>
<th>Anjilnesam</th>
<th>Kiapi</th>
<th>Jamkhaneh</th>
<th>Sarta</th>
<th>Assam</th>
<th>Pilehkooh</th>
<th>Sorak</th>
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**Figure 1:** Diagrams of flows and relations in the studied zone before Sorak became a town

(Research findings, 2015)
Table 3: Summation and analysis of all flows and relation in the studied zone after becoming a town Sorak (Research findings, 2015)

<table>
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<th>Residential places</th>
<th>Darabkola</th>
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Figure 2: diagrams of flows and relations in the studied after Sorak became a town. (Research findings, 2015)
Table 4: The density of operations in the studied region before and after Sorak becoming a town (Research findings, 2015)

<table>
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<tr>
<th>Operation</th>
<th>Total of rows</th>
<th>Total of possible relation</th>
<th>Density(%)</th>
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Table 5: Studying and comparing internal and external degree nearness the level of rural district before and After Sorak becoming a town (Research findings, 2015)

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<th>Residential places</th>
<th>External degree</th>
<th>Internal degree</th>
<th>Total of distances to other resident places Before and After Sorak becoming a town</th>
<th>Nearness before and After Sorak becoming a town</th>
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<td>Before Sorak becoming a town</td>
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Table 6: The rate of facilities and services in the residencies of Sorak in two periods of before Sorak transformation into a town (Research findings, 2015)

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<th>Residential places</th>
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<th>Administrative</th>
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Table 7: The rate of facilities and services in the residencies of Sorak in two periods of after Sorak transformation into a town (Research findings, 2015)

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Nomenclatures

C.M.C  Clinical Medical Centre   P.O  Post Office 
C.H   Clinical House   T.O  Telecommunication Office  
P   Physician   A.P.T  Access to Public Transportation  
M.A.M  Medical Assistant or Midwife  
A.N.M  Access of Newspapers and Magazine  
C.A   Clinical Assistance  
C.R.M  Farming Machines Repair Center  
C.T   Clinical Trainee  
S.C.S.H  Shopping Center of Surplus Harvest  
D  Dentistry  
A.I.S  Agricultural Implements Stores  
PH  Pharmacy  
C.S  Cooperative Stores  
P.S  Primary School  
H.A.S  Home Appliance Stores  
B.E.S  Boy Elementary School 
B.M.S  Building Materials Stores  
G.E.S  Girl Elementary School  
S.S  Stationary Stores  
M.H.S  Males High School  
F.S  Food Stores  
F.H.S  Females High School  
G.S  Gas Station  
M.G  Males Gymnasium  
P.B  Post Bank  
F.G  Females Gymnasium  
I.C.V  Islamic Council of Village  
P.L  Public Library  
B.C  Basij Centre  
P.B  Post Box  
F.O  Police Office  
C.C.V  Corporation Company of Village  

LITERATURE

THE FUTURE OF SOCIAL POLICY IN EUROPE: AN ANALYSIS OF ATTITUDES TOWARD SOCIAL WELFARE

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ABSTRACT

One of the tasks of social policy is to support economic development. Governments invest in social policy to protect citizens from social risks (for instance, in the labor market). In this sense, economic policy and social policy are strongly linked. The different choices governments have with respect to social policy lead to variations in welfare states. Typically, scholars have divided welfare states into three groups: social democratic, liberal, and continental countries.

This study examines citizens’ attitudes toward social policy in 23 European countries, and especially within the three groups of welfare states. Attitudes toward social welfare are divided into two parts: respondents’ opinions regarding national policy and their attitudes toward poverty. The study focuses on the connections between the type of welfare state and its citizens’ attitudes toward social policy. The study also examines whether so-called situational factors (e.g., the level of income inequality, social expenditure, and social insurance) influence the social welfare attitudes of citizens. The data, which were gathered in 2012, are based on the European Social Survey’s (N = 43,897) sixth round.

The results show that the situational factors have an important role, especially in how citizens evaluate national social policy. However, simultaneous analyses of all the situational factors and social welfare attitudes suggest that the situational factors have only an indirect influence on attitudes toward poverty, such that respondents’ opinions of national policy have a mediating role. In this sense, the results support a weak interpretation of the influence of situational factors on attitudes toward social welfare.

Furthermore, the results show that attitudes toward social welfare are connected to the types of the welfare states, in this analysis, especially in the Nordic (particularly Finland, Norway, and Sweden) and liberal countries (particularly Great Britain and Ireland). In these countries, unlike others, respondents’ opinions regarding national policy and attitudes toward poverty are positively related. However, according to a more detailed analysis, the Nordic and liberal countries can be separated from each other. The group of continental countries was excluded from the final analysis because it seemed not to be a coherent group, as the original welfare-state typology indicated.

Keywords: social policy, social welfare attitudes

1. INTRODUCTION

One of the tasks of social policy is to support the economic development to which it contributes, for instance by optimizing the relationship between the citizens and the labor market. Attitudes toward social welfare indicate how citizens appreciate social policy in general, and especially how they evaluate the government’s social-policy measures. In a well-functioning society, citizens’ opinions are taken into account in governmental policies. To be effective, social policy must be accepted by the citizens it is meant to serve. For this reason,
162 scholars have focused their attention on attitudes toward social welfare (Ervasti, 2012; Gërxhani, Koster, 2012; Larsen, 2008; Salmina, 2014; Svalfors, 1997; van Oorschot, 2006). Attitudes toward social welfare are connected to the level of national social policy. For instance, Blekesaune and Quadagno (2003) emphasize the idea that situational factors influence public attitudes toward welfare-state policy. Situational factors refer to the level of national social policy that can be expressed by various social-policy indices (for instance, those related to social expenditures and income inequality).

The study examines citizens’ attitudes toward social welfare in 23 European countries and whether situational factors (the level of income inequality, social expenditures, and social insurance) influence these attitudes, which, in this case, are those focused on poverty and income inequality. The analysis is performed using the framework of the welfare-state typology (Esping-Andersen, 1990).

2. CONCEPTS
2.1. Attitudes Toward Social Welfare

Although an attitude is often understood to be a personal trait, some researchers emphasize it as a social and contextual construct (e.g., de Rosa, 1993). According to Eagly and Chaiken (1993), the various definitions of attitude feature two common properties. First, an attitude refers to an object; this object can be concrete or abstract, specific or general, but in any case, an attitude always has a target. The second aspect of attitude is evaluative; the evaluation can have various dimensions, such as good or bad, harmful or beneficial, pleasant or unpleasant, and likable or unlikable (Ajzen, 2001).

The concept of attitudes toward social welfare has referred to the responsibility of the state (Valdimarsdóttir, 2010), to attributions for poverty (e.g., Blomberg, Kallio, Kroll, 2010), to attitudes toward welfare policy (Bullock, 2004), and to opinions regarding social welfare services and social security benefits (Muuri, 2010). In this study, attitudes toward social welfare focus on those related to poverty and income inequality. Attitudes are studied in two forms: as respondents' opinions regarding national policy and as a general attitude toward poverty.

Previous studies reveal that many factors influence attitudes toward social welfare. Political ideology significantly affects attitudes (e.g., Valmidarsdóttir, 2010). The field of study and level of education also affect attitudes, although the results are contradictory (cf. Pfeifer, 2009). Additionally, studies show that women, more than men, support the welfare state (Blekesaune, Quadagno, 2003). Age is also a significant factor in attitudes toward welfare. (Valdimarsdóttir, 2010). According to Blekesaune and Quadagno (2003), situational (i.e., unemployment) and ideological (i.e., egalitarian ideology) factors influence public attitudes toward welfare state policy.

2.2. Situational Factors

Welfare states can be organized into groups according to situational factors. Esping-Andersen's (1990) classic definition divides welfare states into three groups: the liberal (Anglophone countries), the conservative (continental Europe and Japan), and the social democratic countries (Denmark, Finland, Iceland, Norway, and Sweden). The different groups of welfare states have different strategies for tackling poverty and inequality.

The welfare state is a definition that expresses the level and intensity to which the state acts in the protection and promotion of the well-being of its citizens. The social democratic model emphasizes the state's central role in the society, but the liberal model focuses attention on the individuals' own responsibility and tries to limit the state's role as much as possible. The Nordic model is financed mostly by taxes, but the liberal model favors privately financed
social security. The conservative model is on a level between the Nordic and liberal models (Powell, Barrientos, 2004; Ferragina, Seeleib-Kaiser, 2011).

In his classic welfare state analysis, Esping-Andersen (1990) uses the concept of *decommodification* to express the extent to which the state invests in its citizens’ “immunization from market dependency.” Scruggs (2014) uses the concept of *generosity* for the same purpose: to indicate the level of social security. Both concepts are operationalized by measuring situational factors to indicate the level of social security. Esping-Andersen (1990) calls it the “decommodification index,” and Scruggs (2014) calls it “the generosity indices.” In this study, situational factors focus on social insurance, social expenditures, and income inequality. The factors are viewed as national measures that also indirectly refer to the groups of welfare states: the social democratic model (later in this paper: the Nordic countries), the liberal model, and the continental model.

3. RESEARCH QUESTION, HYPOTHESES, AND METHOD

This study examines citizens’ attitudes toward social policy in 23 European countries. The concept of *attitudes toward social welfare* is divided into two parts: respondents’ opinions about national policy and their attitudes toward poverty. The respondents’ opinions regarding national policy focus on their evaluation of governmental measures against poverty and income inequality. In contrast, the term *attitude toward poverty* refers to poverty and inequality in a more general view, as a democratic value.

The study examines whether situational factors (the level of income inequality, social expenditures, and social insurance) influence citizens’ attitudes toward social welfare. Furthermore, the analysis is done in the framework of the welfare-state typology. The analysis is based on the following hypotheses:

H1: Situational factors influence respondents’ opinions regarding national policy.

H2a: Situational factors directly influence attitudes toward poverty; (or)

H2b: Situational factors indirectly influence attitudes toward poverty via opinions regarding national policy.

H3: The welfare state models differ from each other on the basis of social welfare attitudes.

The analysis was carried out using normal statistical methods. The sum variables were formed using factor analysis (generalized least squares, Varimax with Kaiser normalization). The reliabilities of the sum variables were calculated using Cronbach’s alpha, and the normality of the distributions was examined using the Kolmogorov-Smirnov test. The distributions of variables were not completely normal; however, parametric methods were used because the distributions were nonetheless close to normal and the size of the data set was sufficient. Pearson’s coefficient was used to measure correlations. Statistical analyses were done using linear regression analysis and analysis of variance (one-way ANOVA).

4. PRIMARY DATA: SOCIAL WELFARE ATTITUDES

The primary data, which were gathered in 29 countries in 2012, are based on the European Social Survey’s (ESS) sixth round. In particular, the final selection of the countries was matched to the available data on social policy factors; thus, 23 countries were represented in the final data sample (N = 43,897) (see Appendix 1).

The primary data, which focused on individual public attitudes toward social welfare, are divided into two sum variables:

The sum variable of “attitude toward poverty” was constructed from two items: how important it is to a democracy, in general, for a government to (a) protect all citizens against poverty, and
(b) take measures to reduce differences in income levels. The sum variable is called “attitude toward poverty.”

The second sum variable focused on respondents’ opinions regarding national policy: Specifically, how well do the following statements describe the situation in your country? (a) The government protects all citizens against poverty, and (b) the government takes measures to reduce differences in income levels. The sum variable is called “respondents’ opinions regarding national policy.”

The response categories were based on a 0–10 scale where 0 means “not at all important” and 10 means “extremely important” (77 declined to answer, and 99 stated that they did not know). The reliabilities exhibited a good level for both sum variables. Country-based results in which Cronbach’s alpha was below 0.6 were excluded.

5. SECONDARY DATA: SITUATIONAL FACTORS

Welfare states have access to various kinds of social policy instruments for reducing poverty and income inequality. Typically, the instruments are based on redistribution, social insurance, and social benefits. In this study, the following situational factors are used to describe the level of social policy in each country.

*Economic equality* is a situational factor which typically is measured by the Gini coefficient. It is a relative measure, and its interpretation is therefore controversial; however, it is widely used as an indicator of inequality. The Gini coefficient measures the inequality among values of a frequency distribution (e.g., levels of income). A Gini coefficient of 0 expresses perfect equality, and a Gini coefficient of 1 (or 100%) expresses maximal inequality among values. The data were retrieved from Eurostat (Statistical Office of the European Communities).

*Social insurance* can be defined as a program by which social risks (i.e., unemployment, sickness, and retirement) are transferred to, and pooled by, an organization, often governmental, that is legally required to provide certain benefits. The measure of social insurance is based on the Comparative Welfare Entitlements Dataset, which provides comparable information about national welfare programs around the world (Scruggs, 2014). In this study, the focus is on the following social insurance programs: unemployment insurance, sickness insurance, and public pensions.

*Social (protection) expenditures* can be counted in many different ways, but in this study they are defined as a percentage of gross domestic product. The expenditures comprise the following: social benefits, which consist of transfers, in cash or in kind, to households and to individuals to relieve them of the burden of a defined set of risks or needs; administration costs, which represent the costs charged to the plan for its management and administration; and other expenditures, which consist of miscellaneous expenditures by social protection plans (payment of property income and other). The data were retrieved from Eurostat.

6. RESULTS

6.1. Respondents’ Opinions Regarding National Policy

The respondents’ opinions regarding governmental measures against poverty and income inequality vary significantly between the countries. On a scale of 0–10, the lowest mean of the variable of respondents’ opinions about national policy was in Bulgaria (1.175), and the highest was in Norway (6.282). Furthermore, based on all the data, the sum variable of respondents’ opinions regarding national policy correlates positively with social expenditures \( R = .702** \) and negatively with the Gini index \( R = -.524* \). In this sense, the respondents’ opinions are in a logical relation to the country’s capacity for taking measures against poverty and inequality. The more a country invests in social policy, the higher citizens assess its ability to implement measures against poverty and inequality.
The respondents’ opinions regarding government’s ability to reduce poverty and income inequality was examined in more detail by using regression analysis. It was assumed that situational factors, such as the Gini index, social expenditures, and social insurance, influenced the respondents’ opinions. According to the regression analysis, the respondents’ opinions about government’s ability to reduce poverty and income inequality can be explained by the level of social expenditures and by the Gini index, as the following regression analysis shows (see Table 1).

Table 1 - Regression Analysis of Opinions Regarding Government

<table>
<thead>
<tr>
<th>Model 1</th>
<th>Model 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>R Square</td>
<td>.645</td>
</tr>
<tr>
<td></td>
<td>.642</td>
</tr>
<tr>
<td>F</td>
<td>10.911***</td>
</tr>
<tr>
<td></td>
<td>17.911***</td>
</tr>
<tr>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Constant</td>
<td>2.066</td>
</tr>
<tr>
<td></td>
<td>2.336</td>
</tr>
<tr>
<td></td>
<td>.054</td>
</tr>
<tr>
<td></td>
<td>.030</td>
</tr>
<tr>
<td>Gini</td>
<td>-.402</td>
</tr>
<tr>
<td></td>
<td>-.395</td>
</tr>
<tr>
<td></td>
<td>-.2.739</td>
</tr>
<tr>
<td></td>
<td>-.8.866</td>
</tr>
<tr>
<td></td>
<td>.013</td>
</tr>
<tr>
<td></td>
<td>.009</td>
</tr>
<tr>
<td>Social expenditures</td>
<td>.620</td>
</tr>
<tr>
<td></td>
<td>.619</td>
</tr>
<tr>
<td></td>
<td>4.188</td>
</tr>
<tr>
<td></td>
<td>4.527</td>
</tr>
<tr>
<td></td>
<td>.001</td>
</tr>
<tr>
<td></td>
<td>.000</td>
</tr>
<tr>
<td>Social insurance</td>
<td>-.019</td>
</tr>
<tr>
<td></td>
<td>-.129</td>
</tr>
<tr>
<td></td>
<td>.899</td>
</tr>
</tbody>
</table>

The result is consistent with the theoretical assumption, because the sum variable of respondents’ opinions regarding national policy focuses only on the government’s ability to reduce economic inequality, which can be measured by the Gini index; furthermore, the sum variable focuses on actions against poverty, which governments can reduce via social investments (expenditures). According to this analysis, social insurance is less important than the other two factors.

6.2. Attitudes Toward Poverty

Throughout European countries, respondents shared the view that reducing poverty is an important democratic value. According to the European Social Survey, the mean of the sum variable of the attitudes toward poverty varies between 7.59 (the Netherlands) and 9.11 (Spain) on a scale of 0–10. Although respondents see measures against poverty as a democratic value, it is interesting to note that they correlates negatively with social expenditures (R = -.427*) and positively with the Gini index (R = .430*). This result indicates that citizens in countries with lower social investments and higher inequality levels support measures against poverty and income inequality even more than citizens in countries with higher social investments and lower inequality levels.

The respondents’ attitudes toward poverty were also examined by regression analysis (see Table 2), in which the poverty attitude was explained by situational factors (the Gini index, social expenditures, and social insurance); additionally, the sum variable of the respondents’ “opinions regarding national policy” was taken into account in the analysis.

Table 2 - Regression Analysis of Attitudes Toward Poverty

<table>
<thead>
<tr>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>R Square</td>
<td>.492</td>
<td>.470</td>
</tr>
<tr>
<td></td>
<td>4.122*</td>
<td>5.325**</td>
</tr>
<tr>
<td>Beta</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Constant</td>
<td>7.058</td>
<td>17.545</td>
</tr>
<tr>
<td></td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td>Gini</td>
<td>.185</td>
<td>.861</td>
</tr>
<tr>
<td></td>
<td>.401</td>
<td>.333</td>
</tr>
<tr>
<td>Social expenditures</td>
<td>.270</td>
<td>.243</td>
</tr>
<tr>
<td></td>
<td>.1055</td>
<td>.306</td>
</tr>
<tr>
<td></td>
<td>.243</td>
<td>1.364</td>
</tr>
<tr>
<td></td>
<td>.364</td>
<td>.189</td>
</tr>
</tbody>
</table>

165
According to the results, the sum variable of poverty attitude is the one most influenced by the sum variable of respondents’ opinions regarding national policy. The sum variables are tightly connected to each other, but the situational factors do not directly influence attitudes toward poverty.

6.3. Relationships Between the Sum Variables
Based on all the data, the sum variable of respondents’ opinions regarding national policy correlates negatively with the sum variable of attitudes toward poverty (R = -.145**). This result refers to a situation in which a government’s ability or will to reduce poverty and income inequality is evaluated to be lower than the citizens’ own priorities of reducing poverty and inequality.

On the other hand, in the Nordic and liberal countries, the correlation is positive: 0.119*** in Finland, 0.168*** in Norway, 0.115*** in Sweden, 0.127*** in Britain, and 0.076*** in Ireland. From a social-policy perspective, it is surprising that the liberal and Nordic countries belong to the same group with respect to this dimension. For instance, Britain is typically seen as an example country of liberal social policy, which generally differs significantly from the Nordic countries. However, one needs to be reminded that this analysis focuses only on a portion of the Nordic countries and on a few of the liberal countries.

6.4. Relationship Between the Nordic and Liberal Countries
Although the sum variables of respondents’ opinions about national policy and attitudes toward poverty correlates positively, the Nordic and liberal countries groups were possible to separate from each other by using variance analysis. In the analysis, attention focused on the sum variable of respondents’ opinions regarding national policy. The variance analysis indicates statistically significant differences between the groups (F[4, 10339] = 101.349, p =.000). The Scheffé test was used to find the exact difference (cf. Table 3).

<table>
<thead>
<tr>
<th>Country</th>
<th>N</th>
<th>Mean Subset 1</th>
<th>Mean Subset 2</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Great Britain</td>
<td>2,198</td>
<td>5.131</td>
<td>2.548</td>
<td></td>
</tr>
<tr>
<td>Ireland</td>
<td>2,564</td>
<td>5.166</td>
<td>2.772</td>
<td></td>
</tr>
<tr>
<td>Finland</td>
<td>2,162</td>
<td>5.969</td>
<td>2.026</td>
<td></td>
</tr>
<tr>
<td>Sweden</td>
<td>1,818</td>
<td>6.091</td>
<td>2.572</td>
<td></td>
</tr>
<tr>
<td>Norway</td>
<td>1,602</td>
<td>6.282</td>
<td>2.013</td>
<td></td>
</tr>
<tr>
<td>Sig.</td>
<td>.995</td>
<td>.002</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note. The Scheffé test (subset for d = 0.001).

The liberal and Nordic countries were sorted into separate groups. Great Britain and Ireland formed a coherent group (p =.995), but there were some differences between Finland, Sweden, and Norway although these countries were sorted into the same group (p = .002). Furthermore, it is important to add that Denmark and Iceland, which belong to the group of the Nordic welfare-state group, had already been excluded in the previous phases of the analysis because of weak correlations between the sum variables.

7. CONCLUSION
The study examined whether situational factors (the level of income inequality, social expenditures, and social insurance) influence citizens’ attitudes toward social welfare. Furthermore, the study focused on the connection between the type of the welfare states and citizens’ attitudes toward social welfare. According to the analyses, the following answers can be provided in response to the hypotheses.

First, the assumption that situational factors influence attitudes toward social welfare (respondents’ opinions regarding national policy) is supported. In particular, the level of social investments and economic equality directly influence citizens’ opinions about national policy. In this sense, Hypothesis 1 is supported.

Second, after analyzing all situational factors and social welfare attitudes simultaneously, it seems that the situational factors indirectly influence the sum variable of attitudes toward poverty, such that the sum variable of respondents’ opinions about national policy has a mediating role. Therefore, Hypothesis 2a is rejected, and Hypothesis 2b is supported. In addition, the result emphasizes a weak interpretation of situational factors’ influence on attitudes toward social welfare (cf. Blekesaune, Quadagno, 2003).

Third, the welfare-state models differ from each other on the basis of attitudes toward social welfare. In the Nordic and liberal countries, the sum variables of “respondents’ opinions regarding national policy” and “attitude toward poverty” were positively related; this was in contrast to the other countries, in which they were negatively related. However, according to a more detailed analysis, the Nordic and liberal-country groups can be separated from each other. The group of continental countries was omitted from the final analysis, since much further analyses are needed before the results can be reported. In this respect, Hypothesis 3 is supported.

In general, situationality influences citizens’ satisfaction with governmental measures against poverty and inequality, which is indirectly (negatively) related to the notion on how important the government’s measures against poverty and income inequality are viewed among citizens. From a social policy perspective, this presents a positive opportunity: Concrete social problems create dissatisfaction with the government, which increases the citizens’ opinion about the significance of social policy. Furthermore, it can be assumed that in a democratic society, citizens’ opinions also influence the implementation and practice of social policy. That is, the situationality of attitudes toward social welfare implies a certain kind of self-correction mechanism in social policy. However, the mechanism of self-correction requires a well-functioning democracy, in which citizens’ opinions are taken into account in governmental policies; on the other hand, it also requires financial resources, which the government can use for social policy reforms.

Situationality might also mean that citizens’ satisfaction with governmental policies may lead to a decline in the significance of social policy and consequently to a gradual reduction of social policy. If social policy is taken for granted, it may become less meaningful among citizens. However, according to this study, satisfaction with governmental policies in the Nordic and liberal countries did not negatively influence attitudes toward poverty; on the contrary, it positively influenced them. Thus, social policy seems to be on solid ground, and citizens’ satisfaction does not erode the welfare-state’s attitudinal base.

There were some limitations with respect to the results of this study. First, the fact that welfare-state attitudes were approached only on a general level was a limitation of this study. In addition, individual situational factors and analyses were excluded from the presentation. Second, the analysis is based on two sum variables, which are constructed from only two items. Third, the sum variables focused narrowly on poverty and inequality, although social-welfare attitudes can also be seen as a broad phenomenon. There are many other factors that influence attitudes toward social welfare. Therefore, much more research and social analysis is needed.
required to demonstrate the relationships between social-welfare attitudes and social factors. However, the data are comprehensive, and their reliability is good.

**LITERATURE**


**APPENDIX 1.** Material: List of accepted countries.

<table>
<thead>
<tr>
<th>Country</th>
<th>N</th>
<th>alpha &gt;.60 (Sum variables)</th>
<th>Social insurance</th>
<th>GINI</th>
<th>Social expenditure</th>
<th>Accepted</th>
</tr>
</thead>
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<tr>
<td>Albania</td>
<td>1200</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Belgium</td>
<td>1859</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>2218</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Switzerland</td>
<td>1460</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Cyprus</td>
<td>1115</td>
<td>x</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Czech</td>
<td>1966</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Germany</td>
<td>2950</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
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<td>1619</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
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<td>x</td>
<td>x</td>
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<td>x</td>
<td>x</td>
<td>x</td>
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<tr>
<td>Finland</td>
<td>2163</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>France</td>
<td>1960</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Britain</td>
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<td>x</td>
<td>x</td>
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<tr>
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<td>x</td>
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<td>x</td>
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<td></td>
<td></td>
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<td>x</td>
<td>x</td>
<td>x</td>
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<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
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<td>x</td>
<td>x</td>
<td>x</td>
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<td>x</td>
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<td>x</td>
<td>x</td>
<td>x</td>
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<td>Norway</td>
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<td>x</td>
<td>x</td>
<td>x</td>
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<td>x</td>
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<td>x</td>
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<td></td>
<td></td>
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<tr>
<td>Sweden</td>
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<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
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<td>1217</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Slovakia</td>
<td>1824</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Ukraine</td>
<td>2177</td>
<td>x</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Kosovo</td>
<td>1297</td>
<td>x</td>
<td></td>
<td></td>
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<tr>
<td><strong>Total</strong></td>
<td>54676</td>
<td></td>
<td>43897</td>
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TOO BIG TO BE BAD? IMPLICATIONS FOR THEORY AND REVIEW OF RESEARCH ON CRIMES, VICES, AND MISDEEDS IN THE CASINO CULTURE OF MACAU

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ABSTRACT
This is a review of research published in English that focuses specifically on casino-related crime in Macau, the largest venue for legalized gambling in the world. It suggests rich possibilities for further research and theoretical thinking into the globally relevant, yet locally specific features of this Special Administrative Region of China. Following studies that identify residents’ perceptions of how their once-quiet enclave has changed under the impact of recent phenomenal growth in the casino industry, it includes discussion, not just of crimes, but of a range of undesirable roles, acts and outcomes currently supported and encouraged by Macau’s casino culture and its position as a border state of China. A structural tension is identified between gambling as the main source of government revenue and the need to control and enforce regulation of unsavory acts and their consequences, both legal and illegal. It presents a typology of socially defined roles and processes within this environment that permit such activities to continue even across, and sometimes because of, the borders of different governmental jurisdictions. It suggests that a theoretical approach that gives broad attention to social harm rather than specific, legally defined casino-related crimes may be the most appropriate way to study negative social impacts in this and other communities dominated by casino-related economies.

Keywords: casinos, crime, culture, social harm, Macau

1. INTRODUCTION
People commit crimes in and around casinos for the same reason that they rob banks: because that is where the money is. But just as banks may no longer provide incentives for financial crimes that involve stockpiles of material cash, so too the relationship between casinos and crimes is no longer clear, simple or easy. The flow of cash in and around casinos, offering as it does “a portfolio of anonymous expenditure” (Skolnick 1978: 45, quoted in Pontell et al 2014: 1) provides not only an attractive lure to criminal activity and a challenge to theory, but also a spark to the imagination. Popular assumptions about what certainly must go on in casinos – especially in Asia – linger on in many media-induced memories and thoughts. But how much illegality is really involved in the world of gambling and how much is imagined? How should it be studied and dealt with? We are just beginning to find out.

2. CHAPTER 1
Casinos provide venues for financial transactions that are outside the realm of most people’s everyday experience; that is why casinos exist. They create new, unusual, and sometimes even extreme contexts for the reconfiguration of how we use, earn, and think about money. Free at last from such burdens as hourly wages, bosses, or even heady calculations of unearned income
from returns on investment, let’s put our money down and make those wagers or at least imagine pictures of those who do. That is why gambling is so exciting and so dangerous: it is outside the bounds of what everyone and everything tells us should be done with our cash. Governments too, and perhaps especially, are in on the game as an apparently easy and lucrative source of revenues when other means fail. The heated attention that arises from casino development is also why casinos and gambling are subject to regulation and control – to keep the danger at bay, prevent it from spreading throughout society at large and also, perhaps, to make sure work by all parties is honest. An honest day’s pay for an honest day’s work? Hah! Unfortunately that scenario does not add up to much of a story in today’s world. But at what point does actual crime enter the gambling picture and does it always need to enter? Popular imagination says it does.

Fueled by sensationalist news reports, books, films, and television shows about casinos, both fiction and non-fiction, and produced it seems by or about every society or jurisdiction where gambling is traditional or legal, the world of casino gambling is widely assumed to foster a hotbed of vice. Glamour and glitz color the portrayal of casinos as dens of iniquity responsible for a wide spectrum of unregulated vices as well as downright illegal acts. Casinos provide home bases for a swirling nexus of cash, jewels, drugs, shady characters, beautiful women, fallen men, ill-gotten gains and, of course, luck. Such a cast of characters and the props and scenes associated with them are the stuff of great and colorful stories about what really boils down to the eternal struggle between good and evil. We all think we know where to go to see the action: just somewhere at or around the craps or baccarat tables. James Bond and Martin Scorsese are both right: Dress up (or down), go to a casino, and you are sure to find your fill of both bad guys and compelling narrative hooks. Such scenarios play off popular and deeply engrained sentiments that gambling itself is just plain bad – and that therefore, by simple logic, a casino must be even worse.

Whether or not anything strictly illegal happens or must happen in a casino may not really be much to the point in the court of public opinion, and here is where issues of theory arise: Putting aside questions of much-needed jobs and public revenue, wouldn’t a town, a city, a society – a people -- be good, or really better off, without any officially recognized venues for gambling? Such doubts and suspicions are why communities think long and hard before legalizing gambling and allowing casinos in their midst. The financial benefits of legalization, in the form of increased revenues to local governments, additional job opportunities, and cash infusions to the economy may be more than clear, but so much else comes along with a casino that is widely considered to be shady and not all good. The implication for theory is that perhaps attention to a broader spectrum of acts than those legally defined as crimes is what is called for here.

3. CHAPTER 2
This paper reviews the current state of research, in English, on casino-related crime and other related undesirable acts and outcomes as they occur in the specific context of Macau, a Special Administrative Region of the People’s Republic of China and the only place in China where gambling is legal. Recognizing a Chinese love of gambling and affirming the financial benefits of casinos if properly controlled, the mainland PRC government nevertheless pushes this vice to the margins of the nation and away from its center and its capital to a region long known and identified for its difference from the rest of China. Macau was administered by Portugal for hundreds of years before its return to China in 1999, but it has a long tradition of casino gambling. Apart from opium smuggling and other illicit trade, such as in gold and arms, and its historic role as a base for the launch of Christianity in Asia, gambling has long been one of the activities that put Macau on the map as far as outsiders were concerned (Hao
2011: 73-81). By one account “before it reverted to China, Macau was best known as a backwater gambling enclave whose casinos provided the major source of the colony’s revenues” (Pontell et al 2014: 4). The first “modern” casino, in terms of a full range of games offered, the Lisboa, opened in 1970 under an exclusive, government-granted license. This monopoly thrived until 2002, when the market was opened to additional operators, and the Sands, the first Western-owned venue, opened in 2004. Additional sub-concessionaires quickly followed. Throughout all these key events, the casino business has boomed, but especially since the liberalization of the industry to outsiders which has brought massive foreign investment and an exponential increase in both visitor numbers and revenues. Macau is now the most lucrative venue for casino gambling in the world, with gambling revenues far exceeding that of Las Vegas, but research into what is going on has only just begun. A new era of global gambling, marked by new casino developments and transnational flows of capital around the world (cf. Kingma 2010) calls for some new research frameworks as well.

The current paper reviews only the limited number of academic research published in English; there are not very many -- less than ten. This handful of recent empirical studies represents a necessary first step toward any further thinking, and it is hoped that their contextually specific findings outlined here will entice other researchers to continue to elaborate and to study Macau. The theoretical implications that are certain to arise from such work involve dynamics that are both global and local: A basic structural contradiction exist, here and elsewhere, in that the government, as a key regulator (others are the casino corporations themselves), is itself in on a highly lucrative game that harbors a host of unsavory acts and undesirable outcomes that many local residents deem morally objectionable, whether or not they are legally classified as crimes. This situation thus poses a series of questions. How to research and to regulate that whole range of behaviors and outcomes found in and around casinos, some of which may aid and abet actual crimes and some of which may not but are nevertheless still morally or ethically dubious and therefore socially undesirable? Without reducing explanation to any simple level of psychology or morality and without relinquishing judgment to any court of public opinion, how are we to research and to understand – and those in charge hopefully to manage – this entire range of behaviors and their contexts that work off each other and that together constitute what could be called “casino culture”? There is much ahead to do.

The gist of current “Occupy” social movements, initiated first by Occupy Wall Street in New York and subsequently spread throughout the world, most recently in Hong Kong, is basically a popular declaration that law has not kept pace with the development of public moral sentiment. Analogously, academic disciplines pertaining to law and to criminal justice systems therefore also need to catch up. Within the domain of law and crime, highly relevant to the discussion here is Beyond Criminology: Taking Harm Seriously (Hillyard et al. 2004) and the subsequent theoretical debate it inspired (Friedrichs and Schwartz 2007, Hillyard and Tombs 2007, Matthews and Kauzlarih 2007, {Pemberton 2007). In their article “From ‘crime’ to social harm?” Hillyard and Tombs (2007) argue that “a disciplinary approach organized around a notion of social harm may prove to be more productive” than previous criminological approaches specifically or narrowly directed toward issues defined by legality/illegality and that such a shift of focus “may have the potential for greater theoretical coherence and imagination, and for more political progress” (Hillyard and Tombs 2007: 9). They go on to state that many events and incidents which cause serious harm are either not covered by criminal law or, if they could be or are encompassed within its ambit, are either ignored or handled without resort to it: corporate crime and state crime are obvious, heterogeneous categories of offence that remain largely marginal to dominant legal, policy, enforcement, and indeed academic, agendas, while at the same time creating widespread harm (Hillyard and Tombs 2007: 12).
This could be a description of the situation in Macau. An approach to the complexity of its casino culture that attends, of course, to legally defined crime but also broadens its concern to encompass a larger moral compass of “social harm” appears to be the way to go. How else to say “boo” to the many stakeholders profiting, both legitimately and illegitimately, from the many legal, quasi-legal, illegal, but nevertheless all potentially undesirable activities and socially negative outcomes of large-scale casino gambling in Macau? This is a place where, given such high financial stakes, “looking the other way”, not least of all by government regulators, is now an entrenched cultural tradition, deeply rooted within a well-organized, cultural-organizational fabric that would rather not rock the boat of any cash cow that works so well for so many. To what extent is this stance of avoidance – toward crimes, perhaps, but also toward other, less clear-cut, literally shady categories of acts and outcomes -- prevalent, desirable, or even necessary to keep the multi-billion dollar revenues flowing? These are the key theoretical questions in and for Macau, and they demand further empirical study to be worked out. In other words, and in what ways, is casino gambling in Macau now perhaps too big to be bad?

4. TOO BIG TO BE BAD?

Questions only are offered here -- no answers -- with the larger goal of inspiring future researchers to probe further, both empirically and theoretically, into these and additional questions about questionable activities. Many Macau residents, both native and foreign, whom I have spoken with over the course of years interpret the basic geopolitical dynamic to be one of China pushing something widely recognized as undesirable and as a vice -- but a highly profitable one -- to the margins of the nation. It is not for nothing that gambling is not permitted anywhere near the nation’s capital or center. It is also not for nothing that identity cards and passports are checked and stamped continually in this part of China when different jurisdictional borders are crossed, even though all this movement and flow of bodies and types of citizens occur here within the same nation state. In this view, legalized gambling is somehow thought to be a “dirty” industry, something to be wary of and watch out for: dirty not in the material sense of the industrial pollution for which the current Chinese economic miracle is also now famous (Zabielskis 2014a) but in the disquieting, intangible sense of a certain lack of moral cleanliness. This is popularly thought to be the reason why gambling is prohibited in every other part of China. It is also why legalization is also a rather special and restricted, limited-edition phenomenon in other parts of the world, especially in the United States, despite recent phenomenal growth of the industry throughout the world. Like it or not, the result of this characterization of gambling is that Macau must now include “casino culture” as part of its identity on a world global stage, together with everything that entails. What all that really means is not yet fully understood.

Global casino culture (Kingma 2010), which Macau now represents in spades, marks its turf in a new global economy, but this is a difficult and somewhat uncomfortable hook upon which to hang a people’s self-esteem or identity, and any community coherence or pride in the sense of belongingness and place attachment (Clayton 2009; Miu and Bing 2004; de Pina-Cabral 2002). The implication, of course, is that residents should perhaps look to indicators other than economic to meet this basic human need for cultural distinction, but this is not how the world works. The new global economy is international, transnational and its players – like those in Macau -- regularly move across various borders as well as within and between political, ethnic, religious, moral and linguistic frameworks with cash either in hand or in mind. People in Macau have lived in the midst of such economic and cultural complexity for centuries and the particularity of this history is key to the difference from China that Macau continues to represent. Like any culture anywhere, Macau’s casino culture is the same -- and different --
from the casino cultures found in other parts of the world. It brings with it some of the same, but also different problems. This is a culture worthy of concerted and continued examination in its own right, not only for the local uniqueness of some of its expressions, but also for its global implications, as legalized casino gambling continues to rise in economic prominence throughout the world.

“Casino capitalism” (Lo 2009a) and the “casino state” (Leong 2001) are two terms that have been coined in reference to the fact that much more than a lion’s share of Macau’s GDP derives from casino-related industries -- currently more than 90% -- and its government is dominated by large and powerful casino interests (Siu 2006). “Casino culture” is used here as way to call attention to the texture of the realities of life amidst such a large, and dominantly powerful industry. The term is formulated in response to recently burgeoning research endeavors that aim to track the impacts of casinos on residents of Macau, for whom crime is but one item on a long list of consequences, both negative and positive, of the recent spectacular growth of the industry (Du Cros 2009; Kong and Wan 2011. Vong 2004, 2008, 2009; Vong and McCartney 2005; Wan 2012; Yu 2008). These effects include the prevalence of both morally and legally questionable activities, vice as well as crime, socially irresponsible behavior, actions with clear criminal intent, as well actions of commission or omission that result in some unintended negative consequences which may be bad but also legal. These items of concern articulated by residents are not confined to the subject domains of any particular academic or professional discipline and include such things as problem gambling, domestic violence, lack of interest in education when casino jobs are so readily available, corruption, congestion, pollution, and inflation. Without articulating which of these are more or less directly related to the rise of casino gambling, whether or not a particular crime is genuinely “casino-related” or not (meaning that it would not have occurred without the presence of a casino), and leaving aside discussion of the overall social, environmental, and economic effects of legalized casino gambling as separate but related topics, one goal of the review here is to identify items of current moral concern in the casino culture of Macau, whether or not they are officially designated as crimes.

The recent financial crisis, starting in 2008, and the subsequent bailout of banks by the U.S. government, led to the popular trope “too big to fail” -- clearly a morally questionable stance in that size, hence power, should not rightly be a criterion by which to judge failure or success. The current paper asks specifically if the casino industry in Macau is now “too big to be bad” -- meaning that, as far as local residents are concerned, perhaps the size and power of the casino industry in Macau acts as a kind of moral blinder that prevents participants and stakeholders in the industry -- in one way or another all the residents of Macau and even Macau itself -- from being as good as anyone wants, imagines, or expects the people and the place could or should be. With hundreds of millions of dollars of casino capitalist cash weighing in the balance, perhaps the “bad” lurking in some of the details is a non-issue and it is in everyone’s interest to look the other way — perhaps with some regret, but perhaps not. Calculating by dollar amount the total social cost of gambling (Cheng 2011) in Macau – including such things such as problem gambling, efforts at its prevention and treatment, gambling-related criminal behavior and the legal costs of police and courts, etc. (an incomplete list at best) -- a recent research study concluded that this social cost of gambling in Macau rose by 163% from 2003 to 2007, from US$ 40 million to US$ 106 million, in the years immediately following the opening up and expansion of the industry (Fong et al 2011). In financial terms, however, perhaps this is not very significant if, during the same period, net income from gambling was in the hundreds of billions. Chalk it up to the cost of doing business? But the significance of the problems in question may lie in terms other than financial.
In one sense, thinking about legally defined crimes may be the easiest way of thinking about the downsides of casino culture: a criminal justice system of deterrents, arrests, courts, and sentences exists to deal with the problem, could perhaps solve many of them, and this system can be improved. But moral undesirability that is less definable as crime, and more softly understood as “vice”, which may be legal, illegal or neither, may be more deeply embedded in casino culture than any positivist approach could imagine and therefore harder to manage, control or reduce. Zhao notes a worldwide trend to conduct “evidence-based scientific research to evaluate the effectiveness of various programs or initiatives” (Zhao 2014: 339) but she also notes that such research is largely lacking in Macau where understanding which programs work and which do not work to reduce crime is still unknown (Zhao and Liu 2011). Perhaps approaches that address multiple fronts are called for, with the collection of basic information an important and necessary first step.

For the time being at least, research on crime and criminal justice in Macau is “largely descriptive in nature” (Zhao 2014: 339). This pattern of beginning with descriptions first will be followed here. The current paper pieces together what small bits of descriptive information are available to describe the most popular types of infringements, whether or not they fall under the legal definition of “crimes.” Included are some short descriptions of the most common types of characters involved – a rouge’s gallery if you will – consisting of standardized social roles filled by different individuals over time within what is now an institutionalized casino culture largely unique to Macau. This approach thus continues to be descriptive – a typology of common crimes/ves/moral infringements, together with descriptions of some of the requirements or behaviors expected of the social players who enact them, plus discussion of some of the current political, legal, and customary structures that make it all possible. The picture presented in both the current paper and the works it reviews is partial and preliminary at best. It can provide introductions to locally-specific domains ripe for further empirical study as a well as continued discussion about what next to do, both methodologically and in terms of theory, object, and goals of investigation.

5. REVIEW OF THE RESEARCH
A few things should be noted about sources. Many writings about Macau, on any subject, both academic and popular, frequently mention a number of familiar tropes of background information thought important for outsiders to know: Macau has a long history as a place where East meets West and the point from which Christianity introduced to East Asia; gambling has a long history there; the history of large-scale, legalized casino gambling is more recent; and the opening of the casino market to additional operators is more recent still and set in motion a phenomenal growth in revenues for all concerned. If authors continue with additional summaries of what Macau is all about by commenting on the impacts of this success, which are both positive and negative, many tend to uncritically reproduce, often in only very brief discussions, popular assumptions about the prevalence of an expected intimate link between casinos and crime. Similarly, in the absence of other sources of in-depth information, academic writings that specifically discuss casino-related crime in Macau frequently rely on newspaper reports for quotes and even basic information about incidents. This practice may be unavoidable pending additional first-hand field research, but it is also subject to the same biases and assumptions mentioned above as journalists and editors often choose to publish only the most sensational and shocking, or conversely, expected and typical incidents. The descriptive typology tentatively offered here is based primarily on academic publications and avoids citing newspaper and popular magazine articles, but it does discuss academic works that use these sources and whose authors unanimously agree that additional first-hand research is necessary. The goal is not to outline any definitive state of study about
casino-related crimes in Macau – no such state has yet been reached – but rather it seeks to encourage more detailed future research about each of the topics or themes mentioned by broadening the scope of what is examined to include activities beyond, or not yet encompassed within, what are clearly and legally defined as crimes.

To this author’s knowledge, only four authors or teams have published research findings in English that specially address gambling-related crimes as the occur specifically in Macau (Kuan 2013, Li 2014, Leong 2001, 2002, 2004, Pontell et al 2014). These works share a common methodological framework in that they are largely qualitative and rely heavily on both personal interviews and newspaper and other popular media reports. Reliable quantitative data regarding casino-related crimes is difficult to obtain both because of ambiguities or lack of clarity in defining what constitutes a casino-related crime, incomplete reporting, and a simple lack of research. Macau’s Judiciary Police have been collecting and publishing data since 2004 but without detailing much information on the type and nature of offenses it officially calculates as “gambling related” (Li 2014: 317). Studies that attempt to include quantitative as well as qualitative data thus tend to include calculations of crime in Macau in a more general sense, leaving open the question of whether or how these offenses may or may not be casino related (Kuan 2013, Leong 2001, Li 2014).

A comprehensive analysis of U.S. census data from 1977 to 1996 that assessed the impact of casinos on crimes such as murder, rape, robbery, aggravated assault, burglary, larceny and auto theft concluded that the presence of casinos in the United States increased all crimes except...
murder (Grinols and Mustard 2006; see Pontell et al 2013). In terms of murder, at least, reports from Macau are consistent with these results in that they indicate no increase in murder concurrent with the rise of the casino industry; Macau currently has a very low murder rate (Li 2014: 312). Research findings about rates of other crimes specifically due to casinos, however, are inconsistent internationally and are yet to be determined in Macau.

Macau’s overall crime rate is now “historically low” (Li 2014: 321) -- consistently lower in recent years than that in the United States for such crimes as homicide, robbery, theft and arson (Li 2014: 322). Despite its millions of visitors and the vastness of its current casino operations, Macau is considered “a relatively safe city” (Zhao 2014: 338; Zhao and Liu 2011). In a recent survey of 12,000 residents, confidence in public safety was ranked highest among nine public administration indices (Zhao 2014: 338-339). In this sense, Macau appears to conform to studies conducted elsewhere that found either no clear connection between legal casino gambling and crime, an inverse relationship (Albanese 1999, 2008), or only a spurious one (Chang 1996). Others elsewhere, however, have found that casinos do indeed increase crimes other than murder (Grinols and Mustard 2006, Stitt et. al. 2003; Wheeler et. al. 2008). Despite popular tropes in films worldwide that depict heavily armed, gambling-related heists or threats of physical coercion, most casino-related crimes are financial rather than violent. A host of other problems remain, however, and perhaps Macau is still at an early stage in its development of casino-related, white-collar crime.

The authors of the U.S. study note that casinos may initially have ameliorating effects on crime, including increased employment opportunities and wages for low skilled labor. . . . [but] gambling-related factors that increase crime begin to dominate and show effects a few years after casinos open and include problems related to the soon-to-be-depleted resources of problem and pathological gamblers, non-residents who visit casinos who may be both victimizers and victims, and negative changes in population and development” (Pontell et al 2014 citing Grinols and Mustard 2006: 17).

Much of this resonates with the situation in Macau, where casino revenues only very recently (2014) have declined, but Macau has a different history that may result in a different dynamic. Some things may be the same as elsewhere but a safer assumption, pending further investigation, is that they are only similar and likely significantly different.

As the tourism slogan has it, Macau’s attraction is that it is “a world of difference -- the difference is Macau.” In many ways Macau is not following the example of Las Vegas, where total revenue from retail and entertainment now exceeds that from casinos. Unlike Las Vegas, direct revenue from gambling itself has not peaked and then permanently declined; growth has been continual and only time will tell if a current dip will be long-lasting. With a potential customer base of more than one billion people just outside its gates, a safe bet is that any downturn will follow its own trajectory with different characteristics than Las Vegas or Atlantic City. official government policy holds that it would be desirable to diversify Macau’s economy in the direction of more family entertainment, middle-class consumption, and even cultural tourism (du Cros 2009), but the current structure that sees most business and government revenues deriving more or less directly from gambling is so lucrative that there is little motivation to change. Yet the dubious achievement of sustaining longer than anywhere else a spectacular economic growth based almost exclusively on what has been called “legalized vice” (Pontell et al 2014: 7) remains a queasy thought: concerns persist over both the creation and sustainability of a milieu still widely believed to facilitate both actual criminal offences and a “range of deviant behavior” (Pontell et all 2014: 1). The question is how to think and study further and deeper about such things. One researcher, citing inconsistent, incomplete, and sometimes ambiguous classification and recording of criminal offenses in Macau, plus the fact that many crimes within casinos go unreported, states that there is
currently “no data that can be used to test the relationship between gambling and crime in Macao” (Li 2014: 320). This observation lends further support to basic description as a necessary next step in investigation, despite Macau’s current experience of safety and wealth.

7. CASINO CULTURE AND QUALITY OF LIFE
Research attention to Macau residents’ attitudes and concerns about a wide range of casino-related impacts is further along the descriptive trail than research about casino-related crime in Macau. Many of these studies of local quality of life have the benefit of being on-going and longitudinal (see, for example, Vong 2009), and they use both quantitative and qualitative methods. The gist of their findings is that actual casino-related crime is somewhat far down on residents’ lists of concerns about the effects of casinos, which include such things as congestion, environmental degradation, inflation, problem gambling, domestic violence, divorce, bankruptcy, increased likelihood of dropping out of school, drug and alcohol abuse, risky or illicit sexual behavior, and prostitution, in addition to more “traditional” casino-related misbehaviors such as money laundering, loan sharking, cheating, theft, and extortion (Wan 2012). Not everything on this list is a crime and not all are even vices. Some are just problems or negative impacts, both social and environmental, even if all of them may be economic in origin. In one way of thinking -- which seems to be the point of view of much of the Macau public -- does it really matter which is which? Behaviors legally designated as crimes may be the simplest or clearest tip of the iceberg in that they can be controlled, at least in theory, by the criminal justice system; but such crimes are usually closely linked to other behaviors and outcomes less clearly defined as criminal but also undesirable. All of these need to be addressed as broader issues of social harm and not just as crimes; they affect not only life in Macau but also popular perception abroad.

Local concerns resonate with and are relevant to the sustainability of the public face that a newly prosperous China is presenting to the world. What happens in Vegas may stay in Vegas, but it has been duly observed that “what happens in Macau leaves Macau and commands heavy global media attention” as part of “China’s wager on Macau” (Pontell et al 2014: 5). Some of the undesirable acts, traditions, and implications presented below are unique to Macau and some are common to other gambling venues (Nichols et al 2002, Park and Stokowski 2011). Each can be placed along a continuum of related behaviors that range from crimes, vices and ills at the blackest end of the spectrum, though to more gray areas of morally questionable acts, social problems, and other undesirable, unforeseen and/or unintended negative consequences, both material and social. This approach may no longer lie squarely in the domain of criminology (Friedrichs and Schwartz 2007) but strict definitions are not the point. In describing aspects of Macau’s casino culture, the goal is not only to encourage future empirical research about culturally rich behavior but also to provide grist for the future building of theory as to what casino cultures and their possible side effects are all about. The effort is to articulate, as a necessary first step, perception and atmosphere rather than direct cause and effect in the many opportunities casino culture presents for undesirable activities.

8. AN INTRINSIC STRUCTURAL TENSION
As previously mentioned, research results are controversial regarding the effect, if any, that legalized gambling has on numbers of crimes and crime rates per capita. Contradictory results have been obtained, even when case studies do not lack hard statistical data. Another approach is suggested. Casinos bring both good and bad. The good can perhaps be easily measured in terms of per capita incomes and the bad can sometimes play out with great drama, but it is not for nothing that both good and bad are also very much matters of perception. Good can quickly turn bad and vice versa. That dynamic is intrinsic to what gambling is all about and is
perhaps the source of its interest and excitement. But this is also a dynamic within which both legal and moral culpability, perhaps by necessity, can remain cloudy. The perception is that casinos may not be bad -- how could they be since they are sanctioned by the state? -- but they are also not good (Kwan 2004).

Chinese people may not be subject to the same level of official religious approbation of gambling as members of Western cultures (Pontell and Geis 2008) but even so, gambling for them is still not all good. China has therefore kept its mixed blessing of this activity at an official arm’s length by pushing its only legal venue to its periphery, the Macau SAR, where both players and staff are mostly drawn from all three regional Chinese “nationalities” – the mainland PRC, and the Hong Kong and Macau SARs – each of which involves a somewhat different civic identity and a different identity card. Large scale “integrated casino resorts” serving predominantly mainland customers have thrived spectacularly as a result and are now mainstream culture in Macau. Such enterprises provide entertainment and income for both locals and foreigners alike and, directly or indirectly, are responsible for a lion’s share of Macau’s public infrastructure development.

This near exclusive economic dependence upon “legalized vice,” however, remains worrisome to all concerned – to the mainland and Macau governments, as well as to residents -- for whom it can be understood to provide a somewhat dubious focal point for pride in economic accomplishment. Unlike their Western counterparts, Chinese gamblers may prefer the sociability of table games over the individualized anonymity of slot machines (Lam 2005), but many still prefer that a wider social world not really know what they are doing. VIP gamblers, or high rollers, usually from the mainland, who commonly risk a minimum of 100,000 Hong Kong dollars per session and who have provided Macau with more than 70% of state revenue, thrive on enjoying this anonymity and the lack of any paper trails recording their gambling activities or debts in ways that might get back to the people at home, let alone trigger any questions of legality (Wang and Zabielskis 2010). The system itself is not illegal – the VIP rooms and the loans they offer are sanctioned by the state – but it can easily provide occasions and venues for other unsavory activities, including, famously, infiltration by organized crime. Mainland and Hong Kong based triads once moved freely in and out of Macau as a kind of magnet or headquarters for many of their illicit activities. Though now much reduced by stricter border controls after the handover to China, the activities fostered by the criminal attractiveness of Macau remains an unsettling theme in the historical memory of many residents (Zabielskis 2014b); it perhaps explains the continued need for different identity cards with differential entry requirements despite both locals and visitors being mostly from the same “one country.”

The short version is that the state – the Macau SAR as backed by the PRC -- is in the same business as the casinos; when push comes to shove there is at least some theoretical value for both in an ability to look the other way at morally, even legally dubious activities in their midst. Casinos regularly under-report illegal activities within their domains, including theft and cheating, preferring to deal with it as an internal matter (Pontell et al 2014: 4); and the state is understandably concerned about doing anything that might compromise its ever growing flow of revenue (Lo 2005, 2009). Yet legalized casino gambling creates an atmosphere for certain parasitical behaviors -- “a range of criminal activities and related behaviors that fall under the heading of ‘vice’ (Pontell et al 2014) -- that at some point need to be controlled. This is the source of a structural tension or conflict inherent within the institution of legalized gambling itself. In terms of policing, it is the challenge of “the generic regulation paradox that tactics featuring leniency can at times prove more productive than those taking a more confrontational stance” (Pontell et al 2014: 4). Government officials “must walk a fine line,
enforcing the law, yet not so vigorously as to bring into question the legitimacy of the gambling industry itself” (Pontell et al 2014: 3).

Undoubtedly this dynamic should rightly include cause and effect sequences whereby criminal activities result in arrest, conviction and punishment, but right does not always prevail in the real world. Casinos create atmospheres in which public perception counts for quite a lot. The public perceives them to be dens of iniquity that the authorities must be perceived to have under control. Legalized gambling in any venue anywhere must deal with this common and familiar historical pattern, buttressed by popular perceptions of gambling itself: Gambling is not good; in the dark days of the past it may have been controlled by organized crime but now a different organization is in charge -- the government. But has the activity itself or the culture of casino gambling ever gotten much better or morally upstanding over time under the rationalizing umbrella of increased government or corporate involvement? “Corruption,” in the sense of officials accepting bribes, kickbacks and amassing or laundering dirty money, is too simple a descriptor for all that goes on, but not all of it is strictly illegal. Perhaps the public thinks, and prefers to think, in terms of morality rather than legality. This is what a student at the University of Macau seemed to be saying in an essay in which she stated that “to me, Macau is now a rotten city disguised in the look of prosperity.” Law addresses only part of the problem and perhaps just the final fruits, not the seeds of wrong doing. A team of more seasoned scholars of Macau observe it this way: Underneath the rather positive exterior of a booming local economy and related material and symbolic benefits, there exists the inescapable truth that the same gambling houses that bring prosperity undoubtedly will, without stringent regulation, encourage further corruption, not only locally but on the mainland.” (Pontell et al 2014: 6)

Put another way, things that are not illegal are not thereby always or necessarily good. Researchers, concerned citizens, and film script writers take note: Detailed knowledge and description of the following list of some of what happens in Macau has only just begun.

9. HANDOVER WOES AND PUBLIC PERCEPTIONS

Gambling has been popular in Macau for centuries but most observers of its recent history identify distinct eras defined by certain key events: The period before the opening of the first modern, large scale casino, the Lisboa, by Stanley Ho’s STDM in 1970 under a state sanctioned monopoly license; a period of intense triad-related violence just before the handover of Macau to mainland China in 1999; the post-handover liberalization of gambling that saw the granting of new casino licenses in 2002 to additional operators; and what some would say is the current era of increased corporatization marked by exponential growth rates in both visitor arrivals and casino revenues. Current numbers for both are inconceivable elsewhere, and their impact multiplies exponentially when considered against Macau’s relatively small population. The current level of lucre, however, has been somewhat hard won since the period of the handover, when both visitors and casino revenues declined along with an increase in murder. “China’s wager on Macau” would have been seen as especially risky on the world stage at this time if the rash of gangland violence sweeping the territory and international media at the time had not been brought firmly under control. This was an era of extreme violence as organized crime syndicates, or “triads”, fought turf wars for control over the VIP rooms – the most lucrative part of the business. Macau had never seen a higher murder rate but, as previously noted, it has since plummeted (Li 2014). In some instances machine-gun-wielding assassins on motorcycles gunned down their prey and sped away, disappearing unchecked across the border to China. Arrests were made, order was eventually restored, and public confidence in Macau as a “safe and cheerful holiday destination” (Pontell
et al 2014: 6) was eventually established as a matter of political, face-saving necessity for the PRC, whose influence in Macau rationalized much of the enclave’s administration, especially border and customs controls (Zabielskis 2014b).

A full history of this period in Macau’s history is yet to be written. Most existing scholarly accounts themselves rely on the many sensationalized magazine and newspaper stories, ubiquitous at the time, as perhaps the only readily available source of information. Publications appearing close in time to this era and without the benefit of much hindsight are sometimes marred by replicating this tone of popular sensationalism and the assumption of illegality and corruption as a kind of default mode (Leong 2001, 2002, 2004, Maxwell 1999/2000). But the designation of culpability and clear criminal intent is not that simple, especially given the concurrent and contradictory need of the government to “stand by with folded arms” to some extent. What is clear is that in the aftermath of the handover, casino-related crime reinvented itself and went underground so to speak, at least in terms of its public prominence. Out of the glare of the public eye, it became more strictly financial and less physically violent.

Macau has often, perhaps even always, been portrayed as the meeting point -- a crossroads -- between East and West. It was an early and enduring location for European penetration into the businesses, religions, and public affairs of East Asia. In this case, casino-related crime felt the pinch from both sides at once. China would not tolerate public displays of violence upon Macau’s return to the motherland and sent in the PLA just to make the point perfectly clear. After new casino licenses were issued and foreign investment commenced, the American companies had to abide by Nevada and New Jersey gambling commission regulations and could not easily operate in Macau in the same casual way that had been a Macau tradition (Wang and Zabielskis 2010). Casino-related crimes thus became more white-collar financial, less foot-solider violent, in the current era of transnational corporate consolidation and growth.

10. MONEY LAUNDERING AND ITS CROSS-BORDER NEXUS

Cleaning up ill-gotten gains, or “dirty money,” so to speak, is the crime that most often comes to mind in even cursory treatments of casino-related malfeasance, and this is due to the nature of the casino beast itself: Anyone’s money, which can easily extrapolate to mean any kind of money, is welcome exchange for chips in “the world of gambling [which] offers a portfolio of anonymous expenditure” (Skolnick 1978, quoted in Pontell et al 2014: 1). These chips, purchased by anyone without question and used or not in actual gambling play, can then be exchanged for a different, perfectly clean, kind of money. But what more can be said about how or why this happens in Macau? A range of diverse behaviors and points of social and political organization, spanning a complete scale of moral shades, need to be included in the story.

Mainland China strictly limits that amount of cash that a departing national can carry out; it limits access to foreign banking by nationals; and Chinese government officials are forbidden to place bets in Macau’s casinos. Do the math. Does this scenario conform to what some -- perhaps many people -- want, need, or hope to do? The greater part by far, more than 70% (Wang and Zabielskis 2010) of Macau’s casino revenue, hence Macau SAR government revenue, comes from its VIP rooms for high rollers, where standard traditional practice mandates a willingness to wager at least an initial 100,000 Hong Kong dollars. Where does all this money come from? No one need ask. Mainland players now far outnumber those from Hong Kong, and they do not need to come up with any cash right away. That is the beauty of a system that encourages more and more betting. As noted below, VIP players are normally bankrolled by handshake loan agreements, with the inevitable paying up of debts arranged in China without any paper or even anything at all, except people and desire, crossing the border.
Sources of the funds used for eventual repayment on the mainland can remain secret – an additional inducement to play fast and loose.

Gambling play in Macau’s casinos, both wagers and wins, is usually all in Hong Kong dollars, and whether one wins or loses is irrelevant as far as cash disposal is concerned. Mainlanders simply open bank accounts in Hong Kong dollars rather than bring any of it back to China, a further incentive not only to gamble but to circumvent China’s strict currency export and banking regulations while at the same time enjoying the added convenience of money laundering if necessary. A justice official in Zhuhai, a mainland city just a walk across the border from Macau, has observed that four main triads (organized gangs) from Macau – 14K, Water Gang, Great Ring Gang, and Wo Shing Yee -- are active on the mainland. Operating either directly or through associates, one of their main businesses is the collection of VIP debts incurred in Macau, should any persuasion in the form of muscle be required (Varese 2011: 167). It is a lucrative business. Fees for triad debt collection services are typically as high as 30% (Varese 2011: 159; 168), but it is a system that works. Legal proceedings, not to be relied on in any case since enforcement of mainland court judgments leaves much to be desired (Varese 2011:155), are completely out of the question here since such debts are not legally recognized on the mainland, even if there had been a paper trail of official bank or casino loan approval (Wang and Zabielskis 2010). It appears that most potential deadbeats do pay up simply upon presentation of the threat of violence and do not wait for its actualization. Once received, the funds could then be returned to Macau through a network of underground banks and legitimate businesses (Varese 2011:167). Reputation is everything here. The debtor knows what the collector is capable of and his own face is on the line should his activities be publicly revealed (Wang and Zabielskis 2010). The rule of thumb in all this appears to be that, if you know the right people, cash or bets crossing the border never needs to be a problem.

Betting by telephone is illegal in Macau, but asking someone else actually present in the casino to bet on your behalf is neither regulated nor scrutinized, hence the ability of Chinese government officials to play in Macau’s casinos without the need to be physically present. Even if they are present in the casino, something which is officially designated as a no-no, they can feel free and easy to partake in the proscribed activity of gambling since the busy comings and goings of millions of people into and out of casinos each year provides cover for both anonymous expenditure as well as the ability to fit anonymously into the crowd.

Such restrictions and counter arrangements directly facilitate a thriving ancillary industry which is another ancient tradition and of course is not illegal: The pawnshop business. Pawnshops with the familiar bat-shaped motif on their signage surround every casino and slot machine hall. When I first came to Macau and perused their glittering shop windows I was puzzled to observe that all the brightly lit watches and jewels seemed brand new. I had assumed that pawnshops were the last resort of the desperate down on their luck at the tables: Pawn grandma’s brooch to make some final bets hoping to win it all back or buy a ticket home. But such is not the case. Those who want to bring more than the allowed amount of cash out of China have several options: Wear some bauble, newly purchased in China, when you cross the border and you can always pawn it later in Macau -- either to gamble or to open a bank account. Or better yet. use a credit card to buy one already in a pawnshop and immediately sell it back to the pawnshop for cash, less the usual rate of 10% (Lages 2013: 108). A related technique, recently reported in the public media, involves the rigging of machines issued by a certain credit-card company to record all transactions in the mainland only, with no record of any point of sale in Macau – another way of flaunting cross-border financial controls. Middle-class or mass market gamblers thus have access to their own social institutions or traditions parallel to those whereby VIP players can circumvent China’s cash flow restrictions. So the RMB 20,000 maximum allowed to be carried out of China and the maximum of RMB 10,000
per day allowed for ATM withdrawals may be regulations that are effective only on the levels of theory and sentiment -- the official story rather than the reality.

Is all this legal or illegal? Is it smuggling? Money laundering? Corruption by government officials? Does it matter? Regulated or unregulated, nice or not, good or bad, it exists and is currently part of the economic profile of Macau, the Pearl River Delta and even a larger part of China. What happens in Macau is not just about Macau. Does the possibility and availability of such “asset processing” in Macau aid and abet or even simply encourage actual crime and corruption in the mainland? It is perhaps not a question that can fully be answered.

11. CASINO INFRASTRUCTURE DEVELOPMENT AND IMMIGRANT LABOR CONTROL CRIMES
With so much potential profit at stake, corruption cases arise that involve payoffs, bribes, and kickbacks, in matters of infrastructure development, including such things as land sales, the construction industry, and undocumented labor, as well as the actors and agencies responsible for planning, licensing, and permissions necessary to build the casinos. Long-standing patterns of secrecy and non-transparency fuel this fire but an important lid was blown off the problem in 2007 when Ao Man-Long, Macau’s appointed Secretary for Transport and Public Works, was accused of accepting more than US$ 100 million in kickbacks and bribes for manipulating government control of land sales and approval of hotel and casino construction. (Lo 2009b: 137-138, Pontell et all 2014). His arrest, conviction on 57 out of 76 counts, and sentencing to 27 years in prison, triggered a series of street protests against corruption that, by Chinese standards, bordered on serious social unrest. The affair has been deemed one of the “systemic and generic problem areas that feed into unacceptable levels of corruption that eats away at the integrity of the social fabric” (Pontell et al 2014: 9). As Steve Vickers, a leading security expert puts it, “In the end, corners get clipped or trimmed to move the show along . . . The reality is that through poor planning and administration in Macau it’s very difficult to adhere to the law in all respects and get the job done” (quoted in Pontell et al 2014: 9-10).

It takes more than a village both to build and to staff new casino resort developments in Macau, some of the biggest of which are the size of small cities. The Venetian is one of the world’s largest buildings and the group of hotels that includes the Conrad in Cotai Central is thought to be the largest hotel complex in the world. Staffing these and other projects still in development with local labor is never enough to get the job done. Contractors and hotel staff managers claim that government allotments of foreign workers, most of whom are from the mainland, are not enough either to start or to keep the ball rolling, resulting in illegal hiring, unfair wage differentials, a potential for unsafe work conditions, and resentment and unrest by local workers and labor unions. The easy availability of relatively unskilled but highly paid casino jobs has been blamed for an increase in the numbers of young people no longer wanting to stay in school, or at least public perception that the casinos are root cause of this and other problems, such as congestion (du Cros 2009), pollution (Kwan 2004, Vong 2008, Wan 2008, Yu 2012), and a negative impact on small businesses (Kong and Wan 2011).

12. USURY: RIDING THE DRAGON, FORCED DETENTION, AND STEALING FROM THIEVES
Much of the following information comes from recent work by Andy Chi Chong Kuan, himself a judiciary police officer in the Gaming-related and Economic Crimes Investigation Department (DICJE). Recognizing the paucity of hard quantitative data to analyze, much of what he reports is based on years of personal experience as well as additional qualitative interviews. He lists 14 types of casino related-crimes as defined in the Macau Penal Code (Decree no. 58/95/M). These are theft, illegal possession of lost property, usury to gaming,
fraud, contravention to enactment, physical injury, abuse of trust, usury with imprisonment, invasion of official property, illegal gaming, illegal immigration and stay, misuse of other’s documents, threats to life, and “other” (Kuan 2013: 18). Without going over each of these in turn, many items on the list can be discussed in terms a criminal nexus centered on the crime of usury.

Illegal loans at exorbitant interest rates are perhaps the most widespread form of casino-related crime in Macau and perhaps the crime most clearly and directly linked to casinos as sources of criminal activity. The logic here is that desperate people, even those who may not have considered committing crimes elsewhere or otherwise, resort to illegal behavior in attempts to recover gambling losses. This idea is backed by the observation that in many cases, their financial criminal involvement extends only to the amount of their losses and no further (Kuan 2013: 78). An informant tells me that these crimes are so common that local newspapers no longer report them since it is old news: Most people have heard the story many times before and it follows a familiar pattern. The following is the basic structure of how it works.

On the mass-market level, an observant operator, whether working within an organized crime syndicate or not, will target apparently distressed losing players and offer them loans to win it all back. At this level, the amount offered is generally under 100,000 Hong Kong dollars and often about half as much, or less. Various interest rates can be calculated in different ways but the rate offered generally means an arrangement that makes it impossible for the player actually to win back any losses. Interest can total as much as 100% within a few days’ time, but the story usually does not even take that long to play out. Not one to tolerate making any risky investments himself, the loan shark takes part of his fee upfront, usually deducting 10% from the initial amount loaned. The shark then proceeds to “ride the dragon (騎龍).” Standing by during the debtor’s play, he deducts an additional amount of interest, also usually 10%, on each bet placed. This amount is collected beforehand whether the player wins or loses. In either case, soon the total amount of the loan is lost and repayment is demanded. If payment is not made more or less immediately to the satisfaction of the loan shark, the debtor’s passport or identity card may be confiscated and, under threat of violence, he or she (many of the victims are women) may be subject to illegal forced detention by being imprisoned in a hotel room until family members are contacted to pay up. At this point some victims manage to escape and call the police. Similar situations occur with much higher stakes among high rollers in the VIP rooms, minus the forced detention (Lam 2010). In this case the threat of violence and of exposure to possible loss of face play out in the gamblers’ hometowns on the mainland, where social losses may be even more extreme (Wang and Zabielskis 2010).

A cross-border, legal structural problem complicates these scenarios. Loans made for the purpose of gambling are not legally collectable in mainland China and thus no one can make any claim in a court of law. Operating with this bit of legal information under their belts, members of organized syndicates from the mainland sometimes press the issue even further and “steal from thieves (黑吃黑)” [literally “black eats black” or “a con within a con”] and pose as distressed gamblers. No Robin Hoods here, these guys arrange loans for themselves with other syndicates and, after a few rounds of play, working with their own organization of cohorts, manage to escape from the gambling table under some pretext such as going to the toilet, thereby escaping from the loan shark and defrauding the usurious syndicate by stealing the amount of the loan. When this happens both sides know, of course, that no legal recourse is possible (Kuan 2013: 66-67), but ultimate escape may not be so simple. Like banks, crime syndicates can sell outstanding debts to other crime syndicates (Kuan 2013: 69) who may be better equipped to collect by wielding more locally relevant clout, regardless of borders. In such cases borders themselves, and legal differences between opposite sides of them, may actually facilitate the need for such extra-legal financial activities.
13. ESTABLISHED ROLES: BATE-FICHA GUYS, MOOCHERS, HEADRESTS AND PARACHUTES

Colorful terms have been created for the roles and activities that have become tradition in Macau’s world of gambling. Leader of the pack is the “bate-ficha guy,” or “rolling chips person (賭場扒仔).” This has become an established management position in Macau’s highly lucrative VIP or junket operator rooms as they are now called. Casinos elsewhere have systems of markers or loans to gamblers in order to encourage play and increase the amounts wagered, but in Macau this has taken on a unique formulation. It would be wrong to characterize what these guys do as illegal. It is not, but it is codified by tradition even if it is not much regulated by the Casino Gaming or Betting Credit Legal System Law (no. 4/2004).

“Bate-ficha” is a Portuguese colloquialism made up by some local Portuguese police officials (Leong 2004: 306, n.8); “bate” is a verb meaning to bear, shake, hit, or strike and “ficha” means chip. The Cantonese term is “dap-ma” meaning clay, mud or dead chip. These are chips that are not exchangeable for cash; they can only be used in gambling play. These guys work for VIP or junket operators, who buy them at a discount in large guaranteed monthly amounts, and they earn their keep by “rolling” them, i.e., exchanging them for ordinary chips which are fully redeemable at face value. What VIP rooms do is loan them to mainland and other non-local players, eliminating the need to bring cash across the border. Conceivably everyone wins in what is really a local marketing system with a brilliant reach that is simultaneously regional, cross-jurisdictional, and linguistically specific in that players are recruited and entertained by guys from their own home region who speak their own language.

The casino is assured that player losses and a lack of cash will not disrupt continued gambling play and it also benefits from the certainty of a guaranteed minimum monthly income: the bate-ficha guys get income by rolling chips purchased at a discount – payoff for winning and dining the high-rollers they have cultivated. Such “entertainments” can include paying for players’ trips to Macau and fulfillment of other desires, such as for drugs and prostitutes. The players have the convenience and anonymity of paperless loans and access to a range of other ancillary services all provided in their own dialect from their home region of China and the flow of gaming tax to government coffers continues unabated and uncompromised by any regional cultural or social differences that “working” and “playing” in Macau – a place far from home – might conceivably present. (Wang and Zabielskis 2010).

The problem is that this highly lucrative business, with no paper trails, blessed by inexact accounting methods, and notwithstanding the strong possibility of less-than-wholesome debt collection methods, is ripe for infiltration by organized crime (Leong 2002, 2004; Kuan 2013). Bate-ficha guys sometimes offer usurious loans, extort tips, steal chips from players, and with the help of gangsters, track winners outside the casino to rob them (Kuan 2013: 15). But the basic process of granting loans in this way and the rolling of clay chips for a profit is legal and well established. Like so many other aspects of Macau’s casino culture, it may not in itself be criminal or corrupt but it is part of a nexus of behaviors that commonly include crimes. Given that outsourced junket operations, some of which are now listed on the Hong Kong shares market, and the VIP rooms that they staff provide so much of Macau’s casino revenue, further research, as well as additional regulation and enforcement of controls such as background checks, would certainly be in order.

Rounding out the colorful cast of well-established roles is a lesser tier of characters consisting of “moochers,” “headsets” and “parachutes.” Sometimes these roles overlap with each other and with other roles. A “casino moocher (賭場扒仔)” is someone who hangs around players at a table, cheers for them, and begs for tips from winners. Typical tips range from HK$100 to HK$200. If these are not forthcoming threats may be made, and to avoid this players often just
pay them to go away (Kuan 2013: 15-16). Moochers also offer to match up losing players with loan sharks, for which service their referral or finder’s fee is usually 10% of the loan (Kuan 2013: 62). A similar scenario occurs in VIP rooms, with bate-ficha guys becoming moochers themselves when they beg for chips or offer to arrange cash loans when they themselves are not the loan sharks. Higher stakes mean a more formal payment demand for tips -- usually 10% -- for example HK$5,000 if the win has been HK$50,000. Deadbeats reluctant to tip may find themselves surrounded by the bate-ficha guy’s business “associates” and thus, perhaps wisely, feel compelled to pay up (Kuan 2013: 60). A “headrest (墊頭)” is someone who physically places a bet on behalf of someone else via telephone. Again, this could be a bate-ficha guy and, again, is not something that is illegal in Macau. The crime is usually perpetrated by the person on the other end, usually someone in the mainland and often a government official who is prohibited from gambling (Kuan 2013: 16). Finally a “parachute (降落傘)” is someone who steals chips on a table through sleight of hand, either from the house or other players (Kuan 2013: 16).

14. THE OTHER SIDE OF THE TABLE: ILLEGAL GAMBLING, THEFT, CHEATING AND TAX EVASION
Classic casino-related crimes familiar in other venues are not without perpetrators in Macau, and the modus operandi involved are limited only by the imagination and ingenuity of criminal intent -- plus the skills with which they are realized. These include rigging slot machines, bribing dealers, hiding tiny cameras up sleeves, creating distractions as covers for theft of chips from both dealers and other players, and slipping additional chips onto winning bets after play has been completed (Kuan 2013: 16-17). Active wherever there is money around, simple crimes of theft, such as of cash or chips, pickpocketing and purse snatching are prevalent, but since “the majority of victims of individual gaming-related crimes do not report violations of their legal interest voluntarily” (Kuan 2013: 9), official statistics can misrepresent the extent of what really goes on. As previously mentioned, one reason is that visitors to Macau, who make up the bulk of its casino’s patrons, do not want to bother with sticking around or returning to pursue legal redress. Another reason is that the casinos themselves have a vested interest -- as does the government -- in presenting casinos as safe and fun places to visit and therefore discourage negative publicity. In years of reading Macau’s newspapers almost on a daily basis and watching hooded suspects of a range of offenses regularly being dragged before TV cameras by the judiciary police, the author has only rarely encountered reports of direct casino-related crimes in the form of cheating at games. This is not because casinos tolerate such behavior but because of a casino preference to deal with such matters internally without ever letting them see the light of police day. Like other gambling venues elsewhere, profiles of known cheats are created and lists maintained as matters of internal security necessity, and the offending individuals are prohibited entry to the private spaces of certain casinos even though they may be allowed entry into Macau.

The only crimes committed on their own turf that the casinos are willing to own up to with any regularity usually involve theft of chips by croupiers or other casino staff. These commonly involve a dealer working with a friend posing as a player or some mismanagement of chips-handling arrangements, but both of these instances are apparently easily caught by surveillance cameras. The public dissemination of information about such crimes serves as a warning and possible deterrent to all other staff and even future potential employees who might contemplate similar moves. The back story here is that casino staff themselves, familiar and conversant with the flow of easy money, are themselves perhaps especially vulnerable to problem gambling and its consequent desperate need for cash (Cheng 2011).
Finally, “playing on the underside” or from “under the table,” perhaps only possible within the relative seclusion of VIP rooms, is a method of tax evasion whereby players and dealer “unofficially” agree that each amount “officially” wagered is actually worth a higher amount. This is a way for both player and dealer to avoid paying out to the government its substantial tax on every sum wagered. Similarly, illegal games themselves -- usually poker rather than the baccarat that is most popular in the casinos themselves -- are sometimes arranged in hotel rooms with the government seeing no revenue from the activity (Kuan 2013: 65).

15. CONCLUSION

Legalized casino gambling brings with it many advantages in terms of financial prosperity but also many negative effects. The downsides are the result of multiple behaviors and traditions that span an entire range from innocent and legal to clearly illegal at each extreme, with every shade of moral questionability in between. Legal activities support illegal activities and vice versa. Some aspects of what happens in and because of casinos are global in their similarities, but others are more locally specific in their details. The patterns and traditions of casino culture in Macau, currently the world’s number one casino gambling venue in the world, are especially fascinating and they have been the subjects of only a very limited amount of investigation. A key factor to consider in this particular environment is that Macau is at the crossroads of multiple jurisdictions of Chinese governance, whose borders actually create both the need and opportunities to move various financial instruments – cash, loans, debts – across them in attempts to bypass regulation and enforcement.

Rather than sort out every legal nuance before acting either to research or regulate – difficult enough even within a single jurisdiction -- this article has suggested a different approach in its review of what has already been investigated: there are multiple benefits to be gained by a broad approach that attends to social harm rather than a narrow look at only crime itself, especially given such cross-border legal complexities. But there is also an additional possible benefit in doing so: the possibility of a renewed articulation of that much abused concept “community,” which has all too often been left undefined in so much research practice, so much so as to have become an empty term devoid of any real meaning or relevance to how groups of people actually see themselves. The notion of a “harmed community,” however, may have greater theoretical and methodological, even political salience, especially in today’s environmentally challenged world and in light of the many newly emerging forms of regional and global consciousness that now underpin new forms of localized action. In this sense, the point of origin of the term “community” – a particular geographically defined territory – may yet again be relevant, even in a corporatized and globalizing world.

The place-based community discussed here is the greater Pearl River Delta region and, specifically and particularly, the Macau SAR -- a place where nearly every aspect of its political economy, at a range of scales, and where whatever social coherence as a community it has managed to muster, is marked in some way, directly or indirectly, by events and behaviors facilitated by the dominance of the casino culture in its midst, completer with all the social harms, potential or already realized, that these actions entail. Such a case can serve as an example of what Hillyard and Tombs have in mind when they note that despite the “enormous ideological baggage” that has followed the idea of “community,” the idea of a “harmed community” could be used to embrace “groups of people in some form of collectivity who are physically or financially harmed by whatever means” (Hillyard and Tombs 2007: 16).

Ethnographic research in many parts of the world reveals that perception of shared harm can be a great “community” unifier of disparate social and economic interest groups vis-a-vis the state, especially in multiethnic urban settings whose transnational residents who have
prior and longstanding traditions of sticking largely to their own kind when seeking social redress (cf. Zabielskis 2008). It is a type of self-identifying and self-conscious social coherence that works and that can accomplish something at a broader level than particular interest groups; it is, in fact, a touchstone for a majority of citizen protests in China and key to efforts to develop civil societies worldwide (Zabielskis 2014a). The salience of harm done – and recognition of the effects of harm -- crosses many boundaries. Hillyard and Tombs go on to note that perhaps the greatest benefit of an analysis of harm is that it would be the basis for developing a much more accurate picture of what is most likely to affect people during their life cycle. Harm could be charted and compared over time. While crime is charted temporally and, increasingly spatially, it is seldom compared with other harmful events. Hence crime statistics produce a very distorted picture of the total harm present in society, generating fear of one specific type of harm and perpetuating the myth of crime. A comparative and broader picture would allow a more adequate understanding of the relative significance of the harms faced by different groups of individuals. Finally, a stress upon social harm would also facilitate a focus upon harms caused by chronic conditions or states of affairs... as opposed to the discrete events (Hillyard and Tombs 2007:18).

Such an approach would embrace criminology and existing disciplinary attention to crime, law, and criminal justice systems, but merely as some of its facets; others could include the methods, concerns and objects of every other social science. Such interdisciplinary ingenuity may well be just what is called for in any attempt to describe, understand, and deal with (in roughly that order), the color and creativity at work in such long-entrenched, but also less than savory, traditions and roles as “riding the dragon,” “parachutes”, “moochers,” and all the other assorted ills, misdeeds, crimes, vices and other deleterious behaviors and outcomes that have long been supported in the casino culture of Macau.

**Figure 1**

**Gambling-related crimes in Macau 2004-2012**

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Gambling-related crimes</th>
<th>% of all crimes</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>823</td>
<td>8.41%</td>
</tr>
<tr>
<td>2005</td>
<td>1,093</td>
<td>10.37%</td>
</tr>
<tr>
<td>2006</td>
<td>979</td>
<td>9.02%</td>
</tr>
<tr>
<td>2007</td>
<td>1,279</td>
<td>9.90%</td>
</tr>
<tr>
<td>2008</td>
<td>1,506</td>
<td>10.86%</td>
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<tr>
<td>2009</td>
<td>1,601</td>
<td>12.91%</td>
</tr>
<tr>
<td>2010</td>
<td>1,655</td>
<td>14.21%</td>
</tr>
<tr>
<td>2011</td>
<td>2,028</td>
<td>16.21%</td>
</tr>
<tr>
<td>2012</td>
<td>2,070</td>
<td>16.32%</td>
</tr>
</tbody>
</table>

Source: Judiciary Police, Macau SAR

**LITERATURE**


THE INTERDEPENDENCE OF GDP PER CAPITA AND FOREIGN DIRECT INVESTMENT IN THE TRANSITIONAL ECONOMIES OF CENTRAL AND EASTERN EUROPE

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ABSTRACT
The paper studies the influence of the GDP per capita on foreign direct investments (FDI) in transitional economies of Central and Eastern European states. In the literature devoted to the influence of FDI on economies, the research about the determinants of the geographical pattern of FDI distribution usually focuses on the factors that determine why some states manage to draw FDI in higher levels than some other states. However, not many studies deal with the GDP per capita as a determinant why some states (i.e. their economies) are more attractive to the FDI than others. Our research focused on the transitional economies of Central and Eastern Europe. Among the states studied, we have equally studied the EU members from Central and Eastern Europe, as well as the non-EU members. By using two variables, FDI and GDP per capita, this research will determine how much FDI correlate to the standard of living represented through GDP per capita for each state surveyed. Research results will show if FDI and GDP per capita are positively correlated, which represents our research hypothesis no.1 and if that correlation is more significant in non-EU states, which represents our hypothesis no. 2. States surveyed in this research were put into three geopolitical groups: two groups of non-EU states compared to a group of more recent EU states. The methodology is based on the calculation of Pearson’s correlation matrix of GDP per capita and FDI for each state and the comparison of median correlation results between the mentioned groups of states. The period surveyed was between 1994 and 2013. We have tried to find similarities and differences between these two groups of states in order to determine the influence of EU membership on the correlation between FDI and GDP per capita.  
Keywords: foreign direct investment (FDI), GDP per capita, transitional economies, Central and Eastern Europe, correlation.

1. INTRODUCTION AND METHOD
An important aspect of the former is the possibility of reintegration into Europe symbolised for many countries by prospective membership of the European Union (Grabbe, Hughes, 1998; Mayhew, 1998). Integration into the world economy, notably through trade and capital flows, is a crucial and related element of the latter. Foreign direct investment (FDI) is a particularly important element of economic integration, because it opens possibilities for accelerated growth, technical innovation and enterprise restructuring, as well as capital account relief (Garibaldi et al, 1999; Holland, Pain, 1998). EU membership can be viewed as a determining
element of the operating business environment, and this may directly influence the rate of FDI flows.

Most studies generally indicate that the effect of FDI on growth depends on other factors such as the degree of complementarity and substitution between domestic investment and FDI, and other state-specific characteristics. Buckley, Clegg, and Wang (2002) argue that the extent to which FDI contributes to growth depends on the economic and social conditions in the recipient state. States with a high rate of savings, an open trade regime and high technological levels would benefit from increased FDI to their economies. However, FDI may have a negative effect on the growth prospects of the recipient economy if they result in substantial reverse flows in the form of remittances of profits, and dividends and/or if the multinational corporations (MNCs) obtain substantial or other concessions from the host state. Bengoa and Sanchez-Robles (2003) argue that in order to benefit from long-term capital flows, the host state requires adequate human capital, sufficient infrastructure, and economic stability and liberalized markets.

In the literature devoted to the influence of FDI on economies, the research on the determinants of the geographical pattern of FDI distribution usually focuses on the factors that determine why some states manage to draw FDI in higher levels than some other states. However, not many studies deal with the GDP per capita as a determinant why some states (i.e. their economies) are more attractive to the FDI than others when it comes to the size of the economy itself. This paper studies the interdependence of the gross-domestic product (GDP) per capita and foreign direct investments (FDI) in transitional (i.e. post-communist) economies of Central and Eastern Europe. The economies of Central and Eastern Europe were picked and grouped as follows: 11 current post-communist EU member states (Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia), six states of the current Western Balkans (Albania, Bosnia-Herzegovina, Kosovo, Macedonia, Montenegro, Serbia), and three Eastern European states, members of the Commonwealth of the Independent States (Belarus, Moldova, Ukraine)

Among the states studied, we have equally studied the EU members from Central and Eastern Europe, as well as the non-EU members. By using two variables, FDI and GDP per capita, this research will determine how much FDI correlate to the standard of living represented through GDP per capita for each state surveyed. Research results will show if FDI and GDP per capita are positively correlated, which represents our research hypothesis no.1 and if that correlation is more significant in non-EU states, which represents our hypothesis no. 2. In order to see the correlation between the growth of the GDP per capita (taken from the web pages of the World Bank) and the FDI for each year surveyed, Pearson’s correlation matrix of GDP per capita and FDI for each state was used and a comparison of median correlation results between the mentioned groups of states was done. The period surveyed was between 1994 and 2013. The data used were collected from webpages of the World Bank. We have tried to find similarities and differences between these two groups of states in order to determine the influence of EU membership on FDI and how it correlates with the size of the state’s economy. Tables below show yearly GDP per capita and FDI values for each surveyed state, from 1994 until 2013.

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5 Russia was excluded from the research since it represents a state of continental size and almost three quarters of its territory are geographically located in Asia. States of the Transcaucasia (Azerbaijan, Georgia, and Armenia) were also excluded since they are not unequivocally located in Europe. Many geographical definitions put whole of their territory or parts of it in Asia.

6 GDP per capita is gross domestic product divided by midyear population. GDP is the sum of gross value added by all resident producers in the economy plus any product taxes and minus any subsidies not included in the value of the products. It is calculated without making deductions for depreciation of fabricated assets or for depletion and degradation of natural resources. Data are in current U.S. dollars. http://data.worldbank.org/indicator/NY.GDP.PCAP.CD/countries.
9th International Scientific Conference "Economic and Social Development"
Istanbul, 9-10 April 2015

Table 1. GDP per capita, CEE EU states, in current US dollars
Year

Bulgaria

Croatia

Czech
Republic

Estonia

Hungary

Latvia

Lithuania

Poland

Romania

Slovakia

Slovenia

1994

1.149

3.135

4.449

2.725

4.049

2.008

1.903

2.813

1.323

3.686

7.231

1995

1.555

4.722

5.596

3.031

4.411

2.107

2.178

3.603

1.564

4.710

10.524

1996

1.063

5.194

6.291

3.342

4.454

2.273

2.340

4.057

1.562

5.078

10.635

1997

1.210

5.140

5.771

3.609

4.522

2.521

2.833

4.066

1.565

5.023

10.282

1998

1.582

5.578

6.204

4.039

4.671

2.746

3.171

4.472

1.871

5.431

10.974

1999

1.611

5.068

6.045

4.132

4.714

3.049

3.113

4.340

1.584

5.550

11.250

2000

1.579

4.862

5.734

4.063

4.543

3.309

3.267

4.477

1.662

5.330

10.045

2001

1.729

5.192

6.301

4.495

5.175

3.557

3.503

4.979

1.834

5.637

10.290

2002

2.031

5.974

7.691

5.310

6.535

4.032

4.114

5.184

2.116

6.442

11.600

2003

2.642

7.690

9.348

7.182

8.247

4.889

5.449

5.675

2.756

8.530

14.607

2004

3.249

9.237

11.177

8.830

10.085

6.081

6.710

6.620

3.533

10.438

16.944

2005

3.733

10.090

12.738

10.264

10.937

7.165

7.851

7.963

4.652

11.415

17.855

2006

4.313

11.229

14.491

12.473

11.174

8.986

9.250

8.958

5.789

12.842

19.406

2007

5.581

13.372

17.524

16.405

13.535

13.073

12.170

11.157

8.170

15.649

23.462

2008

6.917

15.694

21.708

17.786

15.365

15.464

14.833

13.886

9.949

18.201

26.990

2009

6.524

14.044

18.881

14.542

12.635

12.082

11.714

11.295

8.069

16.196

24.126

2010

6.453

13.327

18.950

14.295

12.750

11.447

11.852

12.304

8.139

16.151

22.942

2011

7.286

14.372

20.585

16.982

13.784

13.827

14.228

13.385

9.064

17.760

24.478

2012

7.022

13.159

18.690

16.887

12.560

13.947

14.172

12.721

8.437

16.893

22.059

2013

7.296

13.530

18.861

18.478

13.134

15.375

15.538

13.432

9.499

17.689

22.729

Source: Authors’ calculation of GDP per capita based on World Bank data, in current U.S. $

Table 2. GDP per capita, CEE and SEE non-EU states, in current US $
Year

Albania

BosniaHerzegovina

Kosovo

Macedonia

Montenegro

Serbia

Belarus

Moldova

Ukraine

1994

619

343

n/a

1.717

n/a

n/a

1.460

461

1.012

1995

761

530

n/a

2.262

n/a

n/a

1.371

477

936

1996

951

799

n/a

2.239

n/a

n/a

1.452

462

873

1997

698

1.038

n/a

1.875

n/a

2.795

1.397

528

991

1998

872

1.131

n/a

1.774

n/a

2.141

1.512

449

835

1999

1.105

1.249

n/a

1.806

n/a

2.338

1.210

321

636

2000

1.193

1.436

1.088

1.748

1.610

809

1.273

354

636

2001

1.335

1.482

1.490

1.664

1.897

1.518

1.244

408

781

2002

1.458

1.707

1.588

1.828

2.098

2.014

1.479

459

879

2003

1.863

2.148

1.970

2.286

2.784

2.614

1.819

548

1.049

2004

2.476

2.579

2.135

2.644

3.373

3.169

2.378

721

1.367

2005

2.799

2.822

2.194

2.864

3.665

3.391

3.126

831

1.829

2006

3.077

3.200

2.279

3.133

4.371

3.943

3.849

951

2.303

194


<table>
<thead>
<tr>
<th></th>
<th>Albania</th>
<th>Bosnia-Herzegovina</th>
<th>Kosovo</th>
<th>Macedonia</th>
<th>Montenegro</th>
<th>Serbia</th>
<th>Belarus</th>
<th>Moldova</th>
<th>Ukraine</th>
</tr>
</thead>
<tbody>
<tr>
<td>1994</td>
<td>53</td>
<td>n/a</td>
<td>n/a</td>
<td>24</td>
<td>n/a</td>
<td>63</td>
<td>11</td>
<td>12</td>
<td>159</td>
</tr>
<tr>
<td>1995</td>
<td>70</td>
<td>n/a</td>
<td>n/a</td>
<td>9</td>
<td>n/a</td>
<td>45</td>
<td>15</td>
<td>26</td>
<td>267</td>
</tr>
<tr>
<td>1996</td>
<td>90</td>
<td>n/a</td>
<td>n/a</td>
<td>11</td>
<td>n/a</td>
<td>0</td>
<td>105</td>
<td>24</td>
<td>521</td>
</tr>
<tr>
<td>1997</td>
<td>48</td>
<td>n/a</td>
<td>n/a</td>
<td>16</td>
<td>n/a</td>
<td>740</td>
<td>352</td>
<td>79</td>
<td>623</td>
</tr>
<tr>
<td>1998</td>
<td>45</td>
<td>n/a</td>
<td>n/a</td>
<td>150</td>
<td>n/a</td>
<td>113</td>
<td>203</td>
<td>76</td>
<td>743</td>
</tr>
<tr>
<td>1999</td>
<td>41</td>
<td>n/a</td>
<td>n/a</td>
<td>88</td>
<td>n/a</td>
<td>112</td>
<td>444</td>
<td>38</td>
<td>496</td>
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<td>2000</td>
<td>143</td>
<td>146</td>
<td>n/a</td>
<td>215</td>
<td>n/a</td>
<td>52</td>
<td>119</td>
<td>128</td>
<td>595</td>
</tr>
<tr>
<td>2001</td>
<td>207</td>
<td>118</td>
<td>n/a</td>
<td>447</td>
<td>n/a</td>
<td>177</td>
<td>96</td>
<td>55</td>
<td>792</td>
</tr>
</tbody>
</table>
2. RESULTS AND DISCUSSION

2.1. Methodology

The methodology is based on the statistical correlation between FDI in current US dollars and GDP per capita in current US dollars (World Bank data) for each represented state (as seen in Table 2.), through the surveyed period from 1994 until 2013. The statistical correlation matrix (Pearson method) determined whether any correlation between FDI and GDP p/c exists for each state surveyed, and also if the median value of the individual correlation is higher or lower in non-EU states in comparison to EU states. All surveyed states are put into 3 groups (CEE EU states, CEE non-EU states and SEE non-EU states). It must be mentioned that this research has unavoidable limitations in the surveyed period of years. Less than 35 years were surveyed because there is not enough historical data. Along with that, Bosnia-Herzegovina, Kosovo and Montenegro have insufficient data, because of which their P-value was not significant and the NULL hypothesis was accepted. Finally, research results provided in this paper do not show any cause-consequence relation between FDI and GDP p/c. Any conclusion like that would be false, for example if one wants to conclude that FDI affects the standard of living represented through GDP p/c. A statement like that cannot be concluded because far more variables would have to be considered first.

Research base-points:
Research Hypothesis No.1: In average, a positive correlation between FDI and GDP p/c exists among surveyed states.
Research Hypothesis No. 2: Non-EU states have, in average, a stronger correlation between FDI and GDP p/c than EU states.
The NULL Hypothesis: FDI and GDP p/c are unrelated among surveyed states.

2.2. Research results

Research results show that, for most states (14 out of 20), the NULL Hypothesis can be rejected, which means that FDI and GDP p/c ARE RELATED among surveyed states. In addition, in average, we can accept research hypothesis no. 1 and conclude that there is a somewhat positive correlation between FDI and GDP p/c (standard of living) among the surveyed states, which is shown in Table 5.

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI</th>
<th>GDP p/c</th>
<th>EU</th>
<th>Non-EU</th>
<th>EU</th>
<th>Non-EU</th>
<th>EU</th>
<th>Non-EU</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>135</td>
<td>268</td>
<td>n/a</td>
<td>106 n/a</td>
<td>567</td>
<td>247</td>
<td>84</td>
<td>693</td>
</tr>
<tr>
<td>2003</td>
<td>178</td>
<td>382</td>
<td>n/a</td>
<td>118 n/a</td>
<td>1.406</td>
<td>172</td>
<td>74</td>
<td>1.424</td>
</tr>
<tr>
<td>2004</td>
<td>341</td>
<td>710</td>
<td>n/a</td>
<td>323 n/a</td>
<td>1.028</td>
<td>164</td>
<td>88</td>
<td>1.715</td>
</tr>
<tr>
<td>2005</td>
<td>262</td>
<td>624</td>
<td>134</td>
<td>145 n/a</td>
<td>2.051</td>
<td>307</td>
<td>191</td>
<td>7.808</td>
</tr>
<tr>
<td>2006</td>
<td>325</td>
<td>846</td>
<td>370</td>
<td>427 n/a</td>
<td>4.968</td>
<td>357</td>
<td>259</td>
<td>5.604</td>
</tr>
<tr>
<td>2007</td>
<td>652</td>
<td>1.804</td>
<td>603</td>
<td>733</td>
<td>3.432</td>
<td>1.807</td>
<td>536</td>
<td>10.193</td>
</tr>
<tr>
<td>2008</td>
<td>1.241</td>
<td>1.005</td>
<td>537</td>
<td>612</td>
<td>2.996</td>
<td>2.188</td>
<td>727</td>
<td>10.700</td>
</tr>
<tr>
<td>2009</td>
<td>1.343</td>
<td>139</td>
<td>408</td>
<td>260</td>
<td>1.549</td>
<td>1.936</td>
<td>1.877</td>
<td>315</td>
</tr>
<tr>
<td>2010</td>
<td>1.089</td>
<td>444</td>
<td>487</td>
<td>301</td>
<td>1.340</td>
<td>1.393</td>
<td>202</td>
<td>6.451</td>
</tr>
<tr>
<td>2011</td>
<td>1.049</td>
<td>469</td>
<td>546</td>
<td>495</td>
<td>2.700</td>
<td>4.002</td>
<td>276</td>
<td>7.207</td>
</tr>
<tr>
<td>2012</td>
<td>920</td>
<td>350</td>
<td>293</td>
<td>283</td>
<td>355</td>
<td>1.464</td>
<td>185</td>
<td>7.833</td>
</tr>
<tr>
<td>2013</td>
<td>1.478</td>
<td>322</td>
<td>343</td>
<td>376</td>
<td>1.377</td>
<td>2.233</td>
<td>251</td>
<td>3.771</td>
</tr>
</tbody>
</table>

Source: World Bank data, current U.S. million $
### Table 5. FDI to GDP p/c correlation between CEE EU member states, CEE non-EU member states and SEE non-EU member states (Belarus, Moldova, and Ukraine)

<table>
<thead>
<tr>
<th>COUNTRIES</th>
<th>Pearson Correlation value (r) between FDI and GDP p/c</th>
<th>P-value</th>
<th>NULL Hypothesis at P=0,05:</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CEE EU states</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bulgaria</td>
<td>0.498</td>
<td>0.025</td>
<td>rejected</td>
</tr>
<tr>
<td>Croatia</td>
<td>0.606</td>
<td>0.005</td>
<td>rejected</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>0.340</td>
<td>0.142</td>
<td>confirmed</td>
</tr>
<tr>
<td>Estonia</td>
<td>0.658</td>
<td>0.002</td>
<td>rejected</td>
</tr>
<tr>
<td>Hungary</td>
<td>0.431</td>
<td>0.058</td>
<td>confirmed</td>
</tr>
<tr>
<td>Latvia</td>
<td>0.622</td>
<td>0.003</td>
<td>rejected</td>
</tr>
<tr>
<td>Lithuania</td>
<td>0.557</td>
<td>0.011</td>
<td>rejected</td>
</tr>
<tr>
<td>Poland</td>
<td>0.555</td>
<td>0.011</td>
<td>rejected</td>
</tr>
<tr>
<td>Romania</td>
<td>0.614</td>
<td>0.004</td>
<td>rejected</td>
</tr>
<tr>
<td>Slovakia</td>
<td>0.631</td>
<td>0.003</td>
<td>rejected</td>
</tr>
<tr>
<td>Slovenia</td>
<td>0.265</td>
<td>0.258</td>
<td>confirmed</td>
</tr>
<tr>
<td><strong>MEDIAN</strong></td>
<td></td>
<td>0.608</td>
<td></td>
</tr>
<tr>
<td><strong>CEE non-EU states</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Albania</td>
<td>0.932</td>
<td>0.000</td>
<td>rejected</td>
</tr>
<tr>
<td>Bosnia-Herzegovina</td>
<td>0.302</td>
<td>0.295</td>
<td>confirmed</td>
</tr>
<tr>
<td>Kosovo</td>
<td>0.327</td>
<td>0.390</td>
<td>confirmed</td>
</tr>
<tr>
<td>Macedonia</td>
<td>0.641</td>
<td>0.002</td>
<td>rejected</td>
</tr>
<tr>
<td>Montenegro</td>
<td>-0.232</td>
<td>0.616</td>
<td>confirmed</td>
</tr>
<tr>
<td>Serbia</td>
<td>0.582</td>
<td>0.015</td>
<td>rejected</td>
</tr>
<tr>
<td><strong>MEDIAN</strong></td>
<td></td>
<td>0.641</td>
<td></td>
</tr>
<tr>
<td><strong>SEE non-EU states</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Belarus</td>
<td>0.851</td>
<td>0.000</td>
<td>rejected</td>
</tr>
<tr>
<td>Moldova</td>
<td>0.597</td>
<td>0.005</td>
<td>rejected</td>
</tr>
<tr>
<td>Ukraine</td>
<td>0.857</td>
<td>0.000</td>
<td>rejected</td>
</tr>
<tr>
<td><strong>MEDIAN</strong></td>
<td></td>
<td>0.851</td>
<td></td>
</tr>
</tbody>
</table>

**MEDIAN Correlation: ALL non-EU** | 0.746

**MEDIAN Correlation: ALL** | 0.612

Source: Authors’ research and calculation based on World Bank data, FDI and GDP p/c in current US$
Among the surveyed states, the ones that statistically do not have a relation between FDI and GDP p/c (confirmed the NULL hypothesis) are the Czech Republic, Hungary and Slovenia. States that have insufficient data to determine a statistical correlation between FDI and GDP p/c are: Bosnia-Herzegovina, Kosovo and Montenegro.
All other surveyed states have rejected the NULL hypothesis. Out of the states that have rejected the NULL hypothesis, the authors can conclude that the median correlation values between FDI and GDP p/c among non-EU states are higher than among EU-states.

**Table 6. FDI/GDP p.c. correlation median between three groups of countries:**

<table>
<thead>
<tr>
<th></th>
<th>Median value of Correlation between FDI and GDP p/c</th>
</tr>
</thead>
<tbody>
<tr>
<td>CEE EU states</td>
<td>0.608</td>
</tr>
<tr>
<td>CEE non-EU states</td>
<td>0.641</td>
</tr>
<tr>
<td>SEE non-EU states</td>
<td>0.851</td>
</tr>
</tbody>
</table>

Source: Authors’ research and calculation based on World Bank data, FDI and GDP p/c in current US$

Based on data from Table 6, the authors can conclude that, in average, Non-EU states have a stronger correlation between FDI and GDP p/c than EU states surveyed, which confirms Research Hypothesis no. 2.

**3. CONCLUSION**

Research results have obviously shown and proven that there is a relation between FDI and GDP per capita. Although it would be difficult to prove that it is a causal relation (it would not be statistically correct) one can notice that there is some influence between FDI and GDP per capita when the size of the economy (measured in GDP) is taken into consideration. If one lived, for example, in Belarus, his or her standard of living might be more related to FDI than, for example, if he or she lived in Poland. The main point of this argument can be seen above in Table 6, in which smaller, non-EU Central and Eastern European economies have a higher correlation, or simply stronger connection between FDI and GDP per capita (standard of living) than larger, mainly EU economies.

**LITERATURE**

RUSSIA AS THE INITIATOR OF REGIONAL AND GLOBAL CHANGES

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ABSTRACT

In March 2014, Crimea together with Sevastopol became a new administrative entity which was included into the Russian Federation. The process which led to this outcome was of an extremely dramatic nature. It should be noted that the previously planned actions which took place at that time were marked both by exceptional predetermination and remarkable efficiency. From that moment on, the events that have been taking place in the local and international systems, triggered by the largest country in the world in terms of its territory, began to draw the attention of politicians, businessmen and the general public. It has become clear that, regional in their nature, interventions of Russia in the Crimea and in eastern Ukraine are part of a long-term Russian strategy calculated for many years. The current foreign policy of Russia is based on all available instruments. Moscow, to attain its goals, with great precision uses political, financial, military, and economic tools. For example, it is tightening economic cooperation with China, is seeking an agreement with Germany and France, and is holding talks at the G20 summit in Milan. At the same time, it is fostering the conflict in Ukraine and is destabilizing the economic situation in Lithuania, Estonia, Latvia, and Poland. Through trade restrictions it skilfully aggravates the tensions between the European Union governments. In the meantime, it is trying to gain allies in the Balkans and in the Mediterranean area, and it is making new global alliances. It is clear that thanks to its activity in many fields, Russia has become the initiator of major political and economic transformations on a transnational scale. It is also an important player in the international arena. Here, some questions need to be asked. The key ones are as follows:

1) What is the direction of the policy of the Russian Federation?
2) Are the goals set by the Moscow authorities feasible?
3) What will be the cost of the Kremlin’s actions on a regional, continental, and global scale?

Finding answers to these questions will help predict and understand the scale of the transformations that may soon occur. This will also allow to estimate the resources that will be necessary in the process of the forthcoming changes.

Keywords: initiator, policy, process, Russia, strategy.

1. INTRODUCTION.

The beginning of the year 2014 was marked by events which apparently started a new chapter in the modern history. By forcibly incorporating Crimea together with Sevastopol into the Russian Federation, Moscow authorities challenged the existing European balance of power. Soon after that, the Kremlin-inspired pro-Russian forces instigated an armed rebellion on the Eastern fringes of Ukraine. A new war began, bloody and prolonged. The resources involved and the scale of the events discussed let us venture to say that what we are witnessing is the creation of a “new order” on the Old Continent and maybe even on the entire globe. The main initiator behind the changes observed is Russia, which is currently facing many internal problems. Not so long ago downgraded and reduced to the role of a second-rate regional power, it forcefully strikes back as one of the main players holding all the cards in the world.
politics. Its actions on the international arena astound everyone. Unpredictable and erratic moves made by Moscow are becoming daily bread for the European Union, the USA, and their allies. It is next to impossible to guess at this point what actions and measures the Kremlin will take in the near future. In practice, none of the economic theories or political premises and predictions keep pace with the reality being shaped by the Russians. This, in turn, raises reasonable concerns as to the outcome of the potential East-West conflict. The thought which gnaws at the minds of many, that developed countries might possibly be defeated in the clash with a sophisticated Russian strategy implemented on an ongoing basis, has turned into an obsession which is becoming more and more consuming.

1) Even so, is it possible to attempt at defining a long-term strategy which was adopted by the ruling team of Vladimir Putin?
2) Is it also possible to determine long-term goals which motivate the Kremlin administration?
3) Is there a way to assess the feasibility of the intentions of Moscow and, assuming they are implemented, the results they may bring upon on the regional and global scale?

The answer to all of the above is affirmative. In other words, based on the existing facts, the knowledge of history, economic premises, political situation, and responses of the parties involved in the confrontation, we are able to predict with a good degree of confidence the events which may unfold in the near future.

2. REBUILDING THE SUPERPOWER

All measures taken by Moscow on the international arena reveal its effort to rebuild its geopolitical position of a superpower. Ruling Kremlin authorities openly aim to restore Russia’s status of a superpower whose strategic importance and influence extend far beyond the borders of Europe and Asia (Friedman G., 2007). Russia first gained its position of a prominent power when the country was ruled by the Romanov family. During the reign of Peter the Great (1672-1725), it became a power on the European scale, which resulted directly from the great military victory in the Great Northern War (1700-1721) and gaining access to the Baltic Sea (Przybylo L., 2014, p. 69). Within 200 years of the reign of the House of Romanov, Russia extended its boundaries and became the largest country in the world. At the peak of its territorial growth, the country stretched from Poland to Alaska and from the coast of the Black Sea to the frosty backwoods of Northern Siberia (Zawadzki T., 2014, pp. 33-34). The country became the second superpower in the world after the US during the rule of the Soviets, after the Second World War. It successfully maintained this position for a few decades, consistently strengthening its political and economic influence not only on the Old Continent, but also in the Middle East, Latin America, and South-Eastern Asia. The decline of Russian position as a global superpower was marked by the collapse of the USSR. Due to the turbulent regime changes and the delineation of new borders, the country lost almost 24% of its territory and more than a half of its population (Przygoda M., 2014).

What could be the main stimulus motivating Russian expansion in terms of its direction? Reasons for territorial growth changed in time, backed complemented by different factors and their resultants, depending on the existing conditions and the potential which could be assured by the country itself. However, nowadays, we should conclude that the continued Russian expansion throughout the centuries was mainly driven by the country’s desire of the access to the sea. A glance at the map explains the whole complexity of the problem, revealing that the biggest country in the world has no free access to a big, open body of water. The
Russian fleet cannot enter the Atlantic because of the Danish straits. Another exit for the Atlantic Ocean, through the warm-water port of Murmansk located at the Barents Sea, is more than troublesome. More often than not, in order to leave this young city founded in 1916, it is indispensable to use heavy icebreakers. The gate to the Black Sea is barred by the Bosporus and the Dardanelles belonging to Turkey. The Montreux Convention of 1936 essentially limits the freedom of navigation in the Turkish Straits. If Turkey goes to war, the passage of military fleet of any country will require the consent of the authorities in Ankara. One should note that, traditionally, their attitude towards Russia is rather unfriendly. The Caspian Sea is an enclosed body of water with no connection to any ocean. Therefore, it has no strategic advantage. Vladivostok, situated more than 9,250 km from Moscow, is the most important Russian port with the access to the Pacific Ocean. Together with the neighbouring port in Nakhodka, they constitute “two little windows to the world” of Russia in the whole Far East. Their drawback is the fact that the entry onto the Pacific Ocean is blocked by the Japanese Isles and the Korean Peninsula. Both South Korea and the Empire of Japan remain allied with the United States. American troops are stationed in both countries since the Second World War. The only harbour of any strategic importance – Port Arthur on the East China Sea – had been leased to Russia by China in 1898 for a period of 25 years and became a base for stationing vessels of the Russian Far-East Fleet. After the Russian defeat in the war against Japan in 1905, Port Arthur came under the administration of the Land of the Rising Sun. When the Japanese were pushed back from Manchuria by the Red Army in 1945 and the war came to an end, the USSR was granted the right to keep a navy base in the port. The base was liquidated under an agreement with China entered into in 1955 (Wortzel L. M., 1999, p. 207). It should also be noted that due to the prolonged conflict of Russia and Japan over the Kuril Islands, no peace treaty has been signed between the two countries since the Second World War. Thus, both sides are officially in the state of war. There is also what is called the Northern Sea Route – a water passage connecting Europe with the Pacific Ocean, running from the Barents Sea along the northern coasts of Eurasia to the Bering Strait. Although starting 1935, Soviet and then Russian icebreakers allow to maintain navigation on those waters all year round, the route is of no real importance, taking into account the load of cargo transported. An analysis of the said facts shows that, for strategic and economic reasons, striving for access to the “open sea” became almost an obsession of the successive rulers and then the teams governing the largest country in the world.

Territorial expansion of Moscow was also driven by another factor: the aggressive, possessive, and ruthless colonialism. Since the reign of Peter the Great until the reign of Nicholas II, it caused Russia to expand by nearly 8 million km$^2$ of land extorted from other countries. Even though the Russians prefer those actions not to be compared with British, French, or Dutch colonialism of the same era, resemblances between the resources used and measures taken in all those cases are striking. To free the Russian Empire from such accusations, propagandists of the contemporary Russia got instructions from Vladimir Putin himself during a special conference which took place in Kremlın on 16 January 2014. The president gave the following message: “Non-Russian nations annexed to the empire were always supposed to benefit from joining Russia.” However, a nagging question follows: “Why so many of the conquered peoples showed their ingratitude by conspiring, rebelling, and taking the benefits for granted?” (Nowak A., 2014, p. 41).

Usually, the origins of the current conflict in Ukraine are traced back to the ambition of the Russian Federation to maintain the existing sphere of influence. In terms of its location on the map, Ukraine surely constitutes the soft underbelly of the European part of Russia. Moscow authorities cannot have NATO troops in such a vulnerable location. Allowing to exclude
Ukraine from the Kremlin’s sphere of influence would be a sign of total lack of imagination or sheer daftness on the part of the ruling team of president Putin. However, some analysts point to a whole other reason why the conflict in Ukraine came into being. It is neither the territory, the protection of Russian minority, nor anything of the sort. Pro-Russian separatists aim to tear off Eastern Ukraine and annex it to Russia, primarily due to the fact that the Donbass region is particularly rich in shale gas and natural gas. Most of the gas fields are located in the vicinity of what is traditionally regarded as the Donets-Kharkov axis.

Natural resources were also the true reason behind the incorporation of Crimea. Research reveals that the area near the town of Faros in the southern part of the peninsula holds especially abundant underwater gas resources. Another Ukrainian region abounding in gas is the so-called Skifska field which stretches from Crimea to the Romanian border. However, the incorporation of Crimea, the increased Russian control over the Black Sea coast, and the aggressive measures taken by special forces of the country, combined with the activity of the diplomacy and politicians helped by radical environmental organisations, blocked exploitation in the area. One may suppose that such a situation is going to last only until the Skifska field is handed over to the Russian administration (Szymowski L., 2015, pp. X – XI). According to some forecasts, due to the progressing depletion of natural resources, only big countries having access to a wealth of natural resources will play any major roles in the international politics in the coming years. 2030 is supposed to be the critical year when the world will face the pressing problem of shortage of energy resources. Some of the superpowers existing at the time may intend to take control over oil and gas resources by force. We will witness a real strife for resources. Apparently, thinking ahead, Russia has already begun to fight in order to assure itself the best possible position and security in this respect, as confirmed by the increased presence of Moscow in the Arctic. This region on the northern fringes of our globe is not only of great strategic importance, but holds 15% of world oil resources and nearly one third of yet unexplored gas fields, according to the estimates of the US Geological Survey. The Arctic has a great possible economic value. All those factors gain in importance with the melting of ice caps, which opens the northern sea passages. The Kremlin plans to construct as many as six new military bases in the Arctic. It also intends to establish there a military command structure consisting of two mechanised infantry brigades supported by hovercrafts and snowmobiles. The Russian ministry of defence declared that a new base had been created on the Wrangel Island, which is a nature reserve on the Arctic Ocean near Alaska. The construction of a similar base located on Cape Schmidt on the Chukchi Peninsula and made of prefabricated modules is almost completed. Those actions symbolise an important stage in the Russian militarisation of this region, which stopped being an area of interest for the USSR as long ago as in the 1980s. Near Murmansk, at the Barents Sea, Moscow intends to additionally create permanent “Arctic forces” in the number of 6 thousand soldiers and equipped with radar guidance systems. In 2014, Moscow re-opened the base on the New Siberian Islands, closed at the final stage of the cold war, where 10 warships and 4 icebreakers are currently anchored. Moreover, the Kremlin plans to re-establish seven polar routes. The Russian defence industry has already been told to carry out research in order to develop weapons which could be used in the extreme weather conditions of the Arctic. Note that in 2007 Russia sent to the region of its continental shelf in the Arctic two miniature submarines, which put a one-meter high national flag at the bottom of the sea, symbolically confirming Russian rights to the area. Claims of Russia regarding the Arctic and its energy resources clash with the ambitions of Canada, Denmark, Norway and the US. Thus, the region may become one of the most disturbed areas in the world (Franchetti M., 2014). Therefore, only bold moves on the part of the Russian Federation, securing its interests along all borders, may guarantee the country’s survival in the future. In order to rebuild the position of a world superpower, it is becoming necessary to use both diplomatic measures and
the Russian military potential. In the light of the energetic crisis and the threat of a conflict over resources impending in the coming years, Russia with its immensurable natural riches is a tempting target for the US and their Western allies, less endowed with natural resources. In this context, events in Ukraine gain an entirely new dimension. Observing the whole matter from the Russian perspective, the intervention in Donbass and the incorporation of Crimea are nothing but preventive measures and a dire necessity. In the face of a unified policy of the EU and the US, targeted at making Ukraine a part of the Western world, Russia is forced to defend its current position. Any deviation from this course would result in a dramatic reduction of possible capabilities of the Russian Federation in the future. Therefore, assuming that Moscow intends to remain an active player in the next few hands of the game, Kremlin authorities have to act vigorously, with all determination they can muster, making no concessions to maintain its current possessions. Only such international policy will offer Russia any chance in the clash with the existing coalition of powerful opponents, united in the effort to marginalise the importance of the country, weaken its potential and then overtake its wealth of natural resources.

3. RUSSIA AS THE INITIATOR OF CHANGE

The current situation of Russia on the international arena must be described as complex and extremely difficult. Low prices of energy resources, including oil and natural gas, which have set in globally for some time have largely undermined the condition of foreign-exchange reserves of the country. The standard of living of the Russian Federation inhabitants deteriorated as well, just like the purchasing power of the rouble. Economic sanctions imposed by the US and member states of the EU sent prices soaring and caused a shortage of some foodstuffs which had earlier been generally available on the market. In the second quarter of 2014, Russia adopted a rigid and quite risky course of politics, which it has been since then following without fail. One might wonder why the country is consistently pursuing the path of confrontation with the so-called “developed countries”, even though it is aware of the objections from the Western public opinion, when as recently as in February 2014 everyone was delighted with the 22nd Winter Olympic Games in Sochi. The small “thaw” which accompanied the events also gained much praise. The thaw resulted in the release from prison of a few dissidents, including the most famous one, Mikhail Khodorkovsky. Other changes for the good ensued as well. The year 2014 marked the first race of the Russian Grand Prix, which is a preliminary race for the Formula One World Championship. Note that the last time when race was previously held in Russia was in 1914, just before the outbreak of the First World War. Much earlier, in December 2010, Russia was entrusted with the organisation of the prestigious 2018 World Football Championships Even at the beginning of the second decade of the 21st century, Russia was becoming an increasingly interesting target for investors, as well as a popular destination for tourists who flocked to the country in greater and greater numbers. What made the Kremlin authorities dramatically break all ties with the West?

The reason for it all was the uncontrollable state of the Euromaidan in Kiev that was ever-changing in a way that was completely unacceptable from the Russia’s point of view. In order to be entirely objective in one’s observations, one must now recall the two existing and parallel versions of events that were taking place in the capital of Ukraine.

The first story tells us of the spontaneous veto of the people, who did not accept the policy pursued by the Ukrainian President of that time, Viktor Yanukovych. What served as an excuse for the revolutionary outburst was the decision to put off the signing of the Ukraine–European Union Association Agreement, while the will of the nation was entirely different. Mass protests of the people in favour of the integration with the EU soon followed, swiftly and effectively backed up by the opposition parties.
Second version of the events is the so called “Moscow version” that views the Maidan Revolution as a result of financing the most radical Ukrainian organisations with the money coming from the funds of NATO’s secret services. In this vision the main role is played by the United States. According to the unofficial information, provided by the Ukrainian Secret Service, the broad public has received information that a sum of 20 million dollars was coming in every week to the US Embassy in Kiev, which in turn was distributing the money to the central offices of “Svoboda” and “Batkivshchyna” that were supposedly later spending this money to support the Euromaidan (Konarski L., 2014). Even though this way of funding “democracy” in Ukraine by the USA and Western Europe has been known for many years now, it was not touched upon by the “progressive” media. A statement of Victoria Nuland, the US Secretary of State for European and Eurasian Affairs, can be treated as a hint as to how the things may have looked like in reality: “since 1991, the US Government has invested $5 billion in the development of Ukrainian democratic institutions.” More information on the subject can be found in her speech, which may be viewed and listened to on Youtube.7 Were the second version even partially true, it would mean that the member states of NATO under the US leadership forced, in fact, the Russian authorities to carry out this disastrous intervention in Eastern Ukraine. An assumption that Russia had already been expecting such a turn of events cannot be ruled out. Perhaps they even had counteractions planned. However, the response to the events that were taking place must have been thought through earlier than it had been originally expected. That is why the first part of the now implemented scenario, i.e. the annexation of Crimea was carried out much swifter than the improvised part two – war in Eastern Ukraine. Somehow unwillingly, Russia has become the initiator of changes on a grand scale while striving to defend its vital interests. The very existence and future of the entire country have been seriously threatened. In order to ensure their survival, the Russian authorities were forced to quickly think of an entirely new strategy, thus creating the long-term plan which is now being put into motion. It comprises two key elements:

- The disunity of the European Union.
- The dissolution of NATO.

Each of the aforementioned elements is to occur in numerical order after a certain part of the previous element would have been implemented. Each and every issue is in some way the consequence of the other and complements each other. In order to understand the Moscow’s strategy for the years to come, one must at least briefly discuss the two elements.

4. The disunity of the European Union.

The Ukraine crisis has polarised the behaviour of the EU leaders towards Russia. Without previous arrangements or coming to a prior understanding, the Federal Republic of Germany one-sidedly “hijacked” for itself the dominant position within the EU. Germans utilise the highly favourable financial results of their economy, striving for an economic expansion of the grand magnitude. German banks, thanks to their credit policy, are the creditors of governments and private entrepreneurs in other countries within the EU. Although there is the Presidency of the European Union Council institution, its real power has been limited to “sham” operations as well as ones being mostly honorary in character. Theoretically, the reduction of the role of the Presidency was supposed to be balanced by significant strengthening of competencies of the High Representative of the Union for Foreign Affairs and Security Policy – a position which was established in 1999. It is the High Representative who was supposed to have the right to represent the EU on the international arena, the right hitherto reserved for the leader of

7 See: https://www.youtube.com/watch?v=dexrP27MMdU
the country holding the presidency. At the moment, the position of the High Representative is held by Federica Mogherini from Italy. She is an agreeable blonde who at the end of the eighties and at the beginning of the nineties was an activist in the youth communist branch. For two terms of office she was a member of the Italian Parliament. Her biggest achievement was holding the office of Minister of Foreign Affairs in the government of Prime Minister Matteo Renzi, an office which she held for almost 9 months. Later on, in next to no time, she took up one of the most important posts in the European Union. Taking this turn of events into consideration, one cannot be surprised that Chancellor Angela Merkel, who is a very experienced politician, took on her shoulders the international affairs of the Union. Behind her, deep in her shadow, treads the President of France François Hollande. What I cannot stress enough is that there is no official EU document that grants Mrs. Chancellor and her French colleague special prerogatives when it comes to representing the EU. The reality is quite different though. The Merkel-Hollande duo, according to the “Norman procedure”, met on 11 February 2015 with the President of Russia Vladimir Putin and the President of Ukraine Petro Poroshenko. Officially, they were discussing the topic of restoring peace in Donbass. However, some suspect that the real subject on the table was the renewal of the informal agreement between Moscow and Berlin about areas of influence and condominiums (Rybczynski A., 2014, p. 64). Under the provisions of this agreement, Berlin would come closer to fulfilling the Bismarck’s dream of a German economic empire, extending from Central Europe to the Eastern Mediterranean region. Moscow, on the hand, would have its way with Ukraine, Baltic states, Belarus, and Finland (Mojsiejewicz M., 2012). Germans would have an absolute control over the Member States of the European Union and subjugate those belonging to the Eurozone. Not everyone, however, agrees with the “written in Berlin and accepted in Minsk” scenario. There are countries whose rulers strive to take advantage of the political and economic potential of Russia in order to break free of the German domination, thus playing a dangerous game between the two European hegemons. The example of such a country is Hungary. Its prime minister Viktor Orbán has for some time now been conducting a pro-Russian policy that is independent from the EU – and he benefits from it. On 17 February 2015, Vladimir Putin met with Viktor Orbán in Budapest; it was decided that a loan to Hungary of EUR 10 billion would be provided for the development of a nuclear power plant in Paks. Favourable gas supply conditions were also agreed upon. A most intriguing consequence of Putin’s visit to Budapest was Viktor Orbán’s arrival in Warsaw. The Hungarian Prime Minister pressed the Polish authorities for the meeting to happen as soon as the talks with the President of Russia had ended. He paid Poland a visit two days later on 19 February 2015. It seems that he was a messenger of the Kremlin leader and came to Poland on a “last chance” mission. Russia used Orbán as an intermediary, seeking contact with high-ranking Polish officials, something they had been lacking for nearly 2 years. The direct result of Orbán’s mission was a visit to Warsaw by Vladimir Titov, Deputy Head of the Russian Ministry of Foreign Affairs, on 23 February 2015. It turned out to be a yet another failure and an official statement on the course of talks was not even issued. “Failure” is the right word, seeing as Russians had already tried to win Poland over to their side. In 2008, Vladimir Putin was talking to the then Prime Minister Donald Tusk about the partition of Ukraine. He put forward the arguments that Ukraine is an artificial country and Lvov is in fact a Polish city. Such claims were expressed in the interview of the American portal Politico\(^8\) with Radosław Sikorski, the Polish Minister of Foreign Affairs.

Another European country that breached the isolation of the Russian Federation was Greece, deeply immersed in the financial crisis. The ultra-left and nationalists’ government, which very recently took over the power in Athens, declared its pro-Russian inclinations. It was the Russian Ambassador who was the first to be hosted by Aleksis Cipras, the Greek Prime Minister, immediately after he had assumed his post. Soon after that Sergei Lavrov, while hosting Nikos Kotzias, the Greek Minister of Foreign Affairs, underlined that Russia appreciates the “constructive” approach of Athens in regard to the EU and his country. Nikos Kotzias expressed his gratitude by declaring that when it comes to international relations, sanctions are never a proper method of resolving disputes. The European Central Bank bowed to the pressure of these events and announced a new tranche of the long-awaited loan for Greece, amounting to EUR 7 billion.

The third EU country that openly declared its open and friendly relations with Russia is Cyprus. There have been rumours of an about-to-be-opened Russian military base on the island. The topic itself was already under discussion a year earlier, when Nicosia struggled because of the deficit of the national budget and was counting on financial aid from Russia. In the end, no loan or agreement were decided upon. At the moment, Cyprus is in need of cash flow due to its current acute savings therapy. It is only this year that Cyprus will have emerged from the recession. However, its GDP is expected to grow by a mere 0.4% and this increase will probably not be sufficient to reduce the unemployment rate, amounting to a record 16.5%. It could be that the dissemination of rumours regarding the Russian military base is nothing but an attempt to soften the foreign creditors, who have already lent Cyprus EUR 10 billion (Kokot M., 2015). There has been a split in the very bosom of the European Union. Some of its members strongly advocate further sanctions against Russia. These are the following: Czech Republic, Estonia, Denmark, the Netherlands, Lithuania, Latvia, Poland, Sweden, and the UK. The harm of further tightening of sanctions is emphasised by (Szymanowski, M., 2014, pp. 58-59): Austria, Bulgaria, Cyprus, Greece, Spain, Portugal, Slovakia, Hungary, Italy, and through the mass media and unofficial non-governmental sources also France and Germany. Other countries belonging to the European Union openly express their doubts as to the validity of restrictions and they have not taken a clear common stance in relation to the existing situation.

5.1. The Dissolution of NATO.

The only thing that stops Russia from acting even more radically is the visible presence of NATO. In this predicament, however, Russia has found itself a most unexpected ally. An expansive and at the same time short-sighted policy of Germany has driven the United States out of Europe. USA is the NATO’s strongest link. The presence of Americans on the Old Continent has until recently guaranteed the maintaining of the existing status quo when it comes to the safety of the region. These times are long gone though. The Americans are now struggling to preserve their influence in the Middle East and wonder how long they can keep protecting Israel, their most trusted ally in this region. The problems of Central and Eastern Europe have been put aside. In the light of these facts, Russia that keeps aggressively pushing towards the heart of the Old Continent is not perceived as dangerous as for example China that keeps gaining new outposts on the Pacific Ocean. The liquidation of majority of the American military bases in Europe, giving up on building an anti-missile shield on this continent, and financial problems have weakened the impact of NATO in this region of the world. It is hard to judge how serious this phenomenon is. Russia has for a few years now been testing the readiness for war and the state of military preparation of certain NATO members. Each month the mass media report that some Russian fighter airplanes or strategic bombers have brushed up against the borders of the member states. Many times “unidentified” submarines have breached the territorial waters of potential NATO candidates, namely Finland and Sweden.
Russia has put an effective stop to Georgia’s and Ukraine’s efforts to join the Treaty by initiating military conflicts. Russia’s acquisitive gaze is also turned on tiny Moldova, which has Russian minority on its territory. The lack of any decisive action or even any kind of consistent counteraction strategy of the members of the North Atlantic Pact in Georgia and Ukraine stimulates Russia to undertake steps that are becoming more and more bold. This is shown in the increased activity of the Russian intelligence, waging the so called “hybrid war”, creating “little green men”, as well as in the statements of certain Russian politicians, who were referring to the possibility of nuclear weapons being used in local conflicts. The biggest threat to the “free world” was the declaration of Vladimir Zhirinovsky, the vice-president of the Russian State Duma, where he stated that the decision to trigger the Third World War had already been made (Baliszewski T., 2014). All these actions share one goal: to intimidate and paralyse the broad public. What Russia hopes to accomplish through that is the world’s submissiveness and aceptation when it comes to absorbing Ukraine, Belarus, later Lithuania, Latvia, and perhaps Finland and a part of Poland just to keep the world peace. One should however realise that striving to retain the peace “at all costs” brings catastrophic consequences each and every time. It has been demonstrated on many examples, even in the relatively recent past.

6. CONCLUSION
Is the disunity of the European Union and dissolution of NATO the ultimate goal, to which Russia aspires? The answer is “absolutely not!” The long-term objective that inspires all the initiatives and actions of the present authorities of the Russian Federation is to reshape the current world order and to do so in a matter of just a few or a dozen or so years. By destroying the now-existing “old order”, the United States of America and their allies would be made subordinate countries at most. On every continent, the main role would be played by the new world superpowers, such as: Brazil, India, China, or South Africa. It is the intention of the decision-makers in the Kremlin that a powerful and reborn Russia be the one who leads and guides this entire “reshaping” process. Russia is, in their minds, supposed to be one of the “arranging” and world-dividing countries – and not the country that is the subject of division. Should those plans succeed, the highest price would be paid by societies undergoing the reconstruction – and the losses would not be purely material and moral. One can presume that the modern way of life and even the very values we live by would be dramatically changed. Also, the popular to such a large extent word “democracy” would acquire a completely different, narrower, and more shallow meaning. Judging the situation from a today’s perspective, it seems that Russia still has the initiative. The thing that might interrupt the current relations though are people and the media serving them – belonging to the civilisation of the “free world” – that are rather quickly getting aware of the present state of affairs.

LITERATURE
THE INFLUENCE OF OIL EXPORTS’ DEPENDENCE ON CORRUPTION AND POLITICAL FREEDOMS IN THE COUNTRIES OF THE GULF OF GUINEA REGION

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ABSTRACT
The paper explores the topic of the oil exports’ influence on the corruption of the public sector, and the degree of political freedom in the Gulf of Guinea region. The main thesis of the paper is that a higher level of dependence on oil exports for a country from the Gulf of Guinea region means a higher level of corruption and a lower level of political freedom in the society. The most important natural resource by far that is being exploited in the region is oil. So the pattern mentioned can be found in all of the states of the region that are dependent on oil exports. This is actually the real meaning of the term “the curse of oil” or the “oil curse”. A large proportion of the oil rents simply “disappears” through the corruptive behaviour of the political and military elites. Therefore, the overwhelming majority of the population in the countries of the Gulf of Guinea region spends their lives in poverty. Societies that exist in the Gulf of Guinea region states would be better off without the oil and that oil is the real “curse” of this region. The research of the human development index, the corruption perception index, and the degree of political freedoms and civil liberties, done on the countries from the Gulf of Guinea region, has shown that the main hypothesis is valid. Dependence on oil exports for a country from the Gulf of Guinea region means a propensity towards a higher level of corruption of the public sector and a lower level of political freedom and civil liberties in the society.

Keywords: natural resources, oil, Gulf of Guinea region, democratization, corruption, diversification of economy.

1. INTRODUCTION: THE “CURSE OF OIL” IN THE GULF OF GUINEA REGION
Natural resources are increasingly becoming the factors that inflate the instability in certain regions of the world, as well as the instability and slower (or non-existent) democratization of the countries that are dependent on the natural resource exports. Among these natural resources, oil plays the most important, but not the only role. Control over natural resources is a key factor that ties politics (distribution of wealth) and economy (normally production of wealth, but in oil exports dependent states a natural resources rent), especially through the subsidies and patronages that supplement most of the tax revenues that would have to be collected without the rents. The influence of natural resources on the economic growth is especially dependent on the institutional framework in which these resources are exploited9.

9 More in:
Certain regions of the world, such as the Broader Middle East Region and the Sub-Saharan Africa, are the best examples of the regions in which the “oil curse” has the strongest effect. Parts of these regions are very rich in oil.

The main aim of this paper was to verify its main hypothesis that a clear connection exists between the dependence on oil exports of the countries in the Gulf of Guinea region\(^\text{10}\) and the slowing down or complete absence of the democratization processes, and a higher level of corruption in the public sector. This connection is the real cause of the so-called “curse of oil”. The first hypothesis, therefore, was that the countries in the region have some basic common features that were interesting to us, such as a very low level of economic development, measured by GDP per capita, a high degree of corruption, a low human development index and a very low level of political freedoms\(^\text{11}\). However, it has to be noted that a high level of dependence on oil exports does not necessarily mean political instability and internal conflicts. Gabon and Equatorial Guinea have stable regimes, while at the same time having a very high-level corruption perception and a very low level of political freedoms (among the lowest in the world). Regimes in these states use the oil rents to finance the repressive apparatus and social care programs (in Gabon). The fact that the population of these states is small (Gabon 1.6 million, Equatorial Guinea less than 0.8 million) and oil deposits are abundant (in comparison to the population) makes it easier for these regimes to finance the repressive apparatus of the state. The regimes are “demotivating” the population to seek a higher level of political freedom and civil liberties (and of course, to pose the question where a high proportion of the money from the oil rents actually ends up). The indicator that confirms this claim is the percentage of GDP spent on the military and state security apparatus. This percentage is from two to ten times higher in the countries that are economically dependent on oil exports (an average of 2.6 percent) than in the countries that are not (an average of less than 1 percent) (Schubert, 2006: 10-11). In the Gulf of Guinea region, countries that are not dependent on oil exports enjoy a higher degree of freedom in the society, a lower level of corruption in the public sector and a higher degree of political stability.


\(^{10}\) For the purposes of this paper, we have defined the Gulf of Guinea region and studied it here, as a region that comprises the following countries: Ivory Coast, Ghana, Togo, Benin, Nigeria, Cameroon, Equatorial Guinea, Gabon, Republic of Congo, Cabinda (Angola’s exclave), Democratic Republic of Congo, and Angola. The coasts themselves, the parts of these countries that are in the proximity of the coast, as well as the Gulf of Guinea as a body of water, are strategically and economically the most important parts of the region. A large portion of oil deposits lies near the coast or below the seabed. Therefore, offshore drilling has been developing rapidly.

\(^{11}\) The Democratic Republic of Congo is abundant in natural resources and torn apart by conflicts connected with the exploitation of natural resources. However, minerals and ores (and not oil) are the primary commodities that are being exported. The deposits of minerals and ores mostly lie deep in the interior of this large state (primarily in the Shaba region) and not along the coastline, that is in fact only about 37 kilometres long. Ghana and Benin were also not the primary focus of our interest. They are interesting because they represent the only countries that differ from the majority of the countries in the region in their political stability and the degree of political freedom. Of course, they are not dependent on the oil exports.
2. METHODOLOGY

The paper represents a case study of one particular region with a focus on certain common aspects of politics and political economy in one particular, defined geographical area. Once we defined the region, the main criterion was, besides the fact that all countries have a coastline on the Atlantic coast of Africa (Gulf of Guinea is a part of the Atlantic Ocean), the importance of the country regarding its overall confirmed crude oil reserves and its current oil exports. The Gulf of Guinea region, as a part of Sub-Saharan Africa, comprises five important oil producers and exporters: Nigeria, Angola, Gabon, Republic of Congo, and Equatorial Guinea. These countries were studied in particular. The two countries, Nigeria and Angola, were the most important for our research, since they are the biggest exporters of oil from the region and members of OPEC. The main indicators that were followed, were found for every country in the region, and compared. The data on the human development index (HDI)\textsuperscript{12} were taken from the official UNDP classification. The countries positioned from 1\textsuperscript{st} to 47\textsuperscript{th} place in the world are considered to have a very high HDI, the countries from 48\textsuperscript{th} to 94\textsuperscript{th} place have a high HDI, the countries from 95\textsuperscript{th} to 141\textsuperscript{st} place have a medium HDI, and finally, the countries placed from 142\textsuperscript{nd} to 187\textsuperscript{th} place have a low HDI. The data on corruption perception for each country were taken from the Transparency International report that comprises the data for the perception of corruption. The scores below 35 were considered as high level of corruption perception, scores from 35 to 50 were considered to be a medium level of corruption perception, and scores from 50 to a maximum of 100 (in theory, in reality, Norway is best placed among the countries studied with the score 85) were considered to represent a low level of corruption perception. The data on the level of political freedom were found in the official classification of the Freedom House, which classifies the societies into free, partly free, and not free, depending on the scores into the categories of political freedoms and civil liberties. The score of 1 represents the best, and the score of 7 represents the worst result.

\textsuperscript{12} The human development index (HDI) is a combination of four indicators that relate to population: life expectancy, average duration of education, expected duration of education and gross domestic product per capita. In theory, the highest value of HDI is 1.
3. THE IMPORTANCE OF OIL FROM THE GULF OF GUINEA REGION AND OIL EXPORTING COUNTRIES

Nigeria, Angola, Gabon, Republic of Congo, and Equatorial Guinea are the five most important oil-exporting countries in the region. The importance of their confirmed and estimated oil fields makes them unavoidable for the developed countries and emerging economies that import large quantities of oil. The importance of the region as a whole and especially of these five countries for the world’s oil supply is very high. The confirmed, mostly offshore oil reserves in the region are over 52 billion barrels. The oil from the region is of a high quality, contains a small proportion of sulphur and is much closer to the United States of America by sea than the oil from the Persian Gulf.

<table>
<thead>
<tr>
<th>Country</th>
<th>Confirmed oil reserves, billions of barrels</th>
<th>Percentage of oil reserves in the total oil reserves in the region</th>
<th>Daily production of oil, millions of barrels</th>
<th>Percentage of oil production in the total oil production in the region</th>
<th>Oil reserves per inhabitant, barrels*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
<td>9.5</td>
<td>18.1</td>
<td>1.8</td>
<td>33.8</td>
<td>442.5</td>
</tr>
<tr>
<td>Cameroon</td>
<td>0.2</td>
<td>0.4</td>
<td>0.06</td>
<td>1.0</td>
<td>9.2</td>
</tr>
<tr>
<td>Congo, Republic</td>
<td>1.6</td>
<td>3.1</td>
<td>0.29</td>
<td>5.5</td>
<td>368.7</td>
</tr>
<tr>
<td>Equatorial Guinea</td>
<td>1.1</td>
<td>2.1</td>
<td>0.31</td>
<td>5.8</td>
<td>1486.5</td>
</tr>
<tr>
<td>Gabon</td>
<td>2.0</td>
<td>3.8</td>
<td>0.24</td>
<td>4.5</td>
<td>1227.0</td>
</tr>
<tr>
<td>Ghana</td>
<td>0.7</td>
<td>1.3</td>
<td>0.08</td>
<td>1.7</td>
<td>31.5</td>
</tr>
<tr>
<td>Ivory Coast</td>
<td>0.1</td>
<td>0.2</td>
<td>0.04</td>
<td>0.7</td>
<td>5.04</td>
</tr>
<tr>
<td>Nigeria</td>
<td>37.2</td>
<td>71.0</td>
<td>2.5</td>
<td>47.0</td>
<td>220.3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>52.4</strong></td>
<td><strong>100.0</strong></td>
<td><strong>5.32</strong></td>
<td><strong>100.0</strong></td>
<td>/</td>
</tr>
</tbody>
</table>

*represents merely an approximation calculated by dividing the estimated oil reserves and number of inhabitants of each country for 2012

Sources:
http://www.eia.gov/countries/index.cfm?view=reserves
http://data.worldbank.org/indicator/SP.POP.TOTL/countries

Table 2 shows oil reserves and oil exports, as well as the relative importance of particular countries from the region. It is clearly visible that Nigeria and Angola are two by far most important oil rich and oil exporting countries in the region. Almost 90 percent of confirmed oil reserves in the region lie in Nigeria and Angola, and Nigeria alone holds over 70 percent of the region’s oil reserves.

Control over Nigeria’s oil reserves therefore represents a primary goal of any Nigerian government. Cooperation with the Nigerian government on the goal of oil exploitation and exports is a highly valuable strategic prize for the great powers (in this case predominantly the U.S.A.). When it comes to daily production, Nigeria and Angola are also by far the most important states in the region, producing about 80 percent of oil produced in the region. Due to the more recent beginning of the oil exploitation (on and offshore), and the prospective potential offshore oil fields (especially in Angola, Republic of the Congo and Equatorial
Guinea), the geostrategic and geo-economic significance of the region is on the rise. The People’s Republic of China has made huge gains in the region, when it comes to oil imports, primarily from the two already mentioned countries, Angola and Equatorial Guinea.

Tab. 3: The data about the dependency on natural resources and mineral fuels (mostly or exclusively oil) from the states of the region

<table>
<thead>
<tr>
<th>State</th>
<th>Percentage of rents from the natural resources exports in total GDP (2012)</th>
<th>Percentage of mineral fuels, lubricants and related materials in total merchandise exports (2012)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
<td>42.5</td>
<td>n/a</td>
</tr>
<tr>
<td>Benin</td>
<td>4.9</td>
<td>0 (2010)</td>
</tr>
<tr>
<td>Cameroon</td>
<td>11.1</td>
<td>56</td>
</tr>
<tr>
<td>Congo, Democratic Republic</td>
<td>33.4</td>
<td>n/a</td>
</tr>
<tr>
<td>Congo, Republic</td>
<td>73.4</td>
<td>68 (2010)</td>
</tr>
<tr>
<td>Equatorial Guinea</td>
<td>51.9</td>
<td>n/a</td>
</tr>
<tr>
<td>Gabon</td>
<td>46.7</td>
<td>83 (2009)</td>
</tr>
<tr>
<td>Ghana</td>
<td>18.7</td>
<td>39</td>
</tr>
<tr>
<td>Ivory Coast</td>
<td>8.8</td>
<td>31</td>
</tr>
<tr>
<td>Nigeria</td>
<td>17.3</td>
<td>84</td>
</tr>
<tr>
<td>Togo</td>
<td>9.0</td>
<td>2</td>
</tr>
</tbody>
</table>


The connection between the huge oil deposits and instability, often followed by internal conflicts or wars is a fact that is accepted in the scientific community. In certain regions of the world, oil deposits are directly connected with the struggles for control over oil exploitation and with the interference of great powers in conflicts that are results of the quests for oil. In the Gulf of Guinea region, the presence of oil is usually the reason for violence to occur. The second effect caused by oil, besides violence, is a false sense of their own total security and enormous wealth, which oil gives to the elites (and the portions of “ordinary” population) of the countries that export it. However, the two trends are concurrent in this region: a higher level of the countries’ dependence on oil export rents means a higher level of corruption and a lower degree of political freedoms and civil liberties. In Nigeria, the situation is even worse and complex, since this country has over 170 million inhabitants and the population continues to grow rapidly. Corruption takes away a large portion of oil export rents.

Besides the previously mentioned aspects of problems that are the product of oil rent use and distribution, an internal aspect that should not be forgotten is the internal geographical distribution of oil rents. The geographical distribution of oil rents in the countries of the region is highly uneven and unfair. The making of political decisions regarding the distribution of oil rent money is highly centralised. The population that lives in the areas where oil is actually exploited usually gets less than 10 percent of oil rent money. This problem of unfair distribution is especially visible in Nigeria, a multinational and multi-confessional country, with a long history of conflicts in the main oil-producing region, the Niger Delta. In the three

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According to: http://data.worldbank.org/indicator/TX.VAL.FUEL.ZS.UN.
states in which most of the Nigerian oil is produced (Rivers, Bayelsa, and Delta) the share of oil rent money returned to the population is only about 5 percent. Minority nations that live in the Delta area (Ogoni people and other nations) feel completely used and left out. Their demands were often crushed with brutal force throughout history. The rebellions against the central government in the Niger Delta are therefore a rule, and not an exception.

By comparing the data on the production of oil and the corruption perception index, we can see that Ghana, the best-placed country according to the corruption perception index and the Freedom House score that measures freedom in the societies, exports oil in almost negligible quantities. The second best placed (by the same criteria) country in the region, Benin, exports even less oil than Ghana and its oil reserves are negligible. The countries in the region that are not highly dependent on oil exports (or not dependent at all) have a greater chance to develop as free societies, and have a lower level of corruption, than countries dependent on oil exports. This rule is also valid for the countries in the Sub-Saharan Africa that are highly dependent on mineral and ore exports, such as the Democratic Republic of Congo.

Table 4 shows that the countries that have a small population and have managed to sustain longer terms of political stability and growth, have been able to raise the quality of life. These countries are Ghana, Gabon, and Equatorial Guinea. The Gulf of Guinea region countries (Ghana, Benin) that are not highly dependent on oil exports to sustain their economies have a much better chance to democratize their societies. Ghana is, according to the data from Table 4, in contrast to the other two oil exports dependent countries, a free and a much less corrupt society 14.

14 Benin is highly dependent on the agricultural products exports, and so is Togo. Cotton makes 80 percent of Benin’s export earnings. Cocoa is the main export commodity of Togo. Nevertheless, these states show a much
4. NIGERIA: A COUNTRY COMPLETELY DEPENDENT ON OIL EXPORTS

In 2012, Nigeria was the 13th producer of oil in the world. It has been for four decades and still is a country critically dependent on oil exports. Nigerian dependency on the export of only one export product (actually a commodity) has risen to an unprecedented level. Nigeria is highly vulnerable to shocks tied with the price of oil in the world market and highly prone to instabilities, coup d’états, civil wars, and the influence of great powers (mostly the U.S.A.15).

The Niger Delta is the most important oil producing area in Nigeria and in the whole Gulf of Guinea region. The Delta has about 70 thousand square kilometres in nine Nigerian federal states (Abia, Akwa Ibom, Bayelsa, Cross River, Delta, Edo, Imo, Ondo, and Rivers)16. Port Harcourt, the capital city of the Rivers state, has a large harbour that is a key point for the export of oil from the Niger Delta. The rebels from the Niger Delta started an uprising in the early 2000s, against the environment devastation that has been occurring in the Delta for decades (oil spills, burning of natural gas as a co-product of oil exploitation). Their uprising was also targeted against the highly uneven and unfair distribution of oil rents, which are distributed solely by the central government of Nigeria17. All of the oil producing federal states of Nigeria that are located in the Delta receive only a small portion of oil rents from the central government. The three states that produce most of the Nigerian oil, Rivers (until the split of this state into two states, Rivers and Bayelsa, it produced about 40 percent of all oil from Nigeria), Bayelsa and Delta (it produces about 35 percent of all Nigerian oil)18 receive an especially small proportion of oil rent money from the central government. These states are continuously punished for having such abundant quantities of oil. At the same time, they represent a centre of activity (violent and non-violent) directed towards the demands for regional autonomy and more even distribution of oil money. The political goals and ideology of the rebels from the Niger Delta quite rapidly gave way to interests that wanted only one thing: more money from the oil that would be distributed among local authorities and clans, which started to fight among themselves about the participation in the “protection” of oil fields. Until 2004, the rebels managed to decrease the production of oil in Nigeria by 40 percent. They forced the central government of Nigeria to recognize them as a party in negotiations (Collier, 2006: 3).

More than 70 percent of the population lives with less than one US dollar a day19, although the Nigerian state has received more than 270 billion US dollars merely from oil exports since the 1960s20 (Watts, 2004: 51). Other estimates, that take into account the inflation, put the earnings from oil rents to one billion US dollars21.

15 Oil originating from Nigeria accounts for more than 5 percent of all oil spent and more than 10 percent of all imported oil in the U.S.A. The strategic value of the Gulf of Guinea region for the U.S.A. is increasing rapidly since the quantity of oil imported into the U.S.A. from the region is larger than from Saudi Arabia.


20 In 1974, after the first world oil price increase, Nigeria was producing 2.2 million barrels per day. Later in the 1980s, prices and production levels dropped dramatically. By 1980, Nigeria’s revenues from oil rose to approximately 23 billion US$ and the upward trend continued for about two decades before the crash in the prices worldwide and the subsequent global economic meltdown.


21 Seventy percent of Nigerian citizens live below the poverty line despite the nearly 1 trillion US$ Nigeria has made from oil exports alone since the 1970s. The answer to this question for many theorists is simply, corruption.
Since oil is a non-renewable commodity, the long-term sustainability of Nigerian economy is highly uncertain. The dependence on oil export rents has very negatively affected the democratization, human rights and the presence of corruption in Nigeria. Besides the fact that a high proportion of oil rent money simply “vaporizes” through corruption, a significant portion of this money is used to finance the military, in order to keep most of the population “quiet”. Nigeria has a population that is too big to be “bought off” by social programs so the repression is necessary for the system to function in the way it does.

In the last four decades, most of the Nigerian population that reside in the areas where oil is being exploited has not become richer and more educated. It has only become poorer. Environmental degradation continues. At the same time, the central Nigerian government receives about 20 million US dollars every day from oil (Oviasuyi, Uwadiae, 2010: 111-113). Oil money is predominantly used to keep the status quo and to secure exploitation and export of oil in order to receive oil rents. If this status quo continues, secessionist tendencies will probably arise in other parts of Nigeria, not only in Delta. Social stratification will rise, as well as regional inequalities. New instabilities and conflicts could jeopardize the steady exploitation and flow of oil from Nigeria, so we can expect great powers that import Nigerian oil, mainly the U.S.A., to interfere in internal political relations in Nigeria, as well as in the whole Gulf of Guinea region.

5. ANGOLA AND OTHER GULF OF GUINEA REGION STATES HIGHLY DEPENDENT ON OIL EXPORTS: CORRUPTION, POVERTY AND THE LACK OF FREEDOM IN THE SOCIETIES

Angola is the second most important country in the Gulf of Guinea region, according to oil reserves and production, as well as oil exports. It produces about one third of the oil from the region. Angola is a very relevant example of how natural resources (diamonds and oil) have prolonged the ideological conflict that has arisen in the Cold-War era. It is also a relevant example how irresponsible use of oil rents establishes and maintains an economy (and the state) very dependent on the money from oil exports rents. Besides the negative economic effects, political distribution of oil rents and corruption hinder the democratization of Angola.

The political economy and economic geography of diamonds and oil were the key factors that determined the duration of the civil war in Angola. Civil war in Angola therefore should be studied regarding the above-mentioned factors, and not just through the ideological prism and accentuation of ethnical differences and tensions in Angola. Diamond finding sites were primarily in the interior of Angola, then under the control of the anti-leftist UNITA movement (National Union for the Total Independence of Angola), while the oil deposits (near the Atlantic coast of Angola and in the Atlantic ocean) were mostly under the control of the Angolan government, comprised of leftist MPLA (People’s Movement for the Liberation of Angola). Consequently, neither of the warring parties managed to take away the sources of funding from its adversary. The exploitation of oil and diamonds not only financed and motivated military operations (outside of their Cold War and Southern African setting). It also determined the success in legitimizing the government and economy. International corporations and outside powers, for a long period immune from investigations about the ethical dimensions of their interference, acted for decades, providing all parties in this conflict the prolongation of struggle and bloodshed. At the same time, wartime profiteers and

More in:
international corporations earned huge profits, primarily from selling conflict diamonds. Civil war in Angola was much more than just an ideological conflict. It was a natural resource war, since the duration of the conflict and the unwillingness of the warring parties to put an end to war can only be explained through the abundance of Angola’s natural resources. This has brought Angola almost three decades of conflict, economic downturn, enormous human suffering (half a million dead, four million displaced), and a widespread poverty (Hodges, 2001: 1, 167). The impact of predatory motives of the looters of natural resources that cause and/or prolong civil wars has been significant. Most of the rebel groups in countries that are rich in natural resources finance themselves through the looting of the natural resources, particularly in the areas rich in natural resources that they consider as their own. Le Billon (2001), as well as Collier (2004), sees the Angolan civil war through this prism (and not primarily ideological, since the war continued well after the breakup of the U.S.S.R., which supported MPLA).

Angola is also considered to have many features of the so-called “predatory state”, and not so many of a “developing country”, since most of the oil exports rents that do not “vaporize” through corruption) are primarily used to finance the military and state security apparatus. By the early 2000s, the conflict in Angola developed into a pure predatory, brutal struggle behind the confronted elites for control of the natural resources whose exploitation enabled enormous profits. The enormous rise in oil exploitation enabled the government to finance the military expenditures in the struggle against UNITA (Hodges, 2001: 171-172). Ideology (capitalism versus Marxism), as an issue that divided the two sides, by that time became meaningless. If ideology was ever relevant, by the end of the conflict it was completely irrelevant. Similar to Nigeria, secessionist tendencies also occurred in Angola, since most of Angola’s offshore oil deposits lie in front of the coast of Cabinda, Angola’s exclave, separated from the territory of Angola proper by the narrow corridor that provides the Democratic Republic of Congo access to the sea. This corridor is a product of colonial heritage of border creation between the parts of the Portuguese, Belgian and French colonial empire in Africa. Nevertheless, the borders from the colonial era persist, and a secessionist movement in Cabinda occurred decades ago, with demands for secession of Cabinda from Angola. The origins of the movement lie in the fact that oil money (the portion left after the corruption “eats” its part) does not do any good for the people of Cabinda, since it is almost completely seized by the central government, and not used to raise the living standard of the people. Cabinda receives only about 10 percent of oil money rents paid by the foreign oil companies to the central government.

Widespread corruption is also a great problem for Angola. In 2012, Angola was the 157th of the 174 countries for which the research on corruption perception was done. Angola today is a state in which the central government earns 90 percent of its income from oil. At the same time, two thirds of the Angolan population do not have access to clean water. A recent IMF audit revealed that $4.2 billion in oil revenues went missing between 1996 and 2001. When asked, the Angolan government allegedly replied that it was an accounting error; it had simply lost the receipts (Schubert, 2006: 9). Because of the widespread corruption and almost complete dependence on oil exports, Angola is very similar to Nigeria. It is almost a “mono

23 Angolan civil war ended only in 2002, after the leader of UNITA, Jonas Savimbi, was killed by the government forces. Only then could the process of peace-making start.
Washington University Global Studies Review, 4 (3) 700-718.
economy” like Nigeria. Angola represents another example of the “oil curse”. Its population is also rising rapidly, as the Nigerian. The population of Angola should rise from 21.5 million in 2013\(^{26}\) to 54.3 million in 2050\(^{27}\). By that time, if production of oil remains as it is, and new enormous oil reserves are not found, the oil reserves should already be depleted. The Angolan future, like the future of Nigeria, seems completely bleak.

Equatorial Guinea is another example, maybe even the best, of the “oil curse” in the Gulf of Guinea region. It is a state completely dependent on oil exports, with a low human development index, very highly corrupted (163\(^{\text{rd}}\) place of 174 countries on the Transparency International list) and without any political freedoms and civil liberties (score of 7 on the list in the Freedom House report). It is a state without any opposition or even daily newspapers. The overwhelming majority of the population lives in complete poverty, while at the same time, the President, his family and the elite in power spend hundreds of millions of dollars from oil export rents. The fulfilment of key socio-economic rights, such as the right to education and basic healthcare, remains poor, despite significant oil revenues and the country’s small population, which make Equatorial Guinea’s per capita gross domestic product, at approximately US$30,000 according to UN figures among the highest in Africa and the world. Much of the population lacks access to adequate sanitation, potable water, and reliable electricity\(^{28}\). Besides corruption, money is also used for financing the repressive apparatus, in order to crush any notions of opposition. After the unsuccessful coup attempt in the early 1990s, the ruling elite cancelled the cooperation with British and the U.S. oil companies and started developing cooperation with Chinese companies. Therefore, China became the leading importer of oil from Equatorial Guinea. Since Equatorial Guinea has abundant oil reserves in comparison to its very small population, the regime will be able to finance social programs in the future.

Gabon is a country that also has a high level of corruption and the lowest level of political freedoms and civil liberties. Corruption has done its job throughout the decades. A third of all Gabonese still live on less than two dollars a day. Corruption “eats” a lot of the oil money. The Bongo family is alleged to have skimmed off 25 percent of the oil-rich nation’s GDP over the years, and Omar was said to be one of the world’s wealthiest heads of state\(^{29}\).

Significant exploitation of oil in the Republic Congo started a bit later than in the other important oil exporting countries of the region. A couple of civil wars, fuelled by natural resource looting and predation, ravaged the country. It is marked by a low human development index, a high level of corruption, and a low level of freedom in the society.

Oil exports were over seven billion US dollars in 2008, yet the Republic of Congo remains one of the most corrupt and indebted countries in the world and its oil wealth has contributed to several bloody wars. While the majority of the population are mired in poverty, a minority surrounding the family of President Denis Christel SassouNguesso are able to live in luxury\(^{30}\).

Weeks after putting down a rebellion, the government of the Democratic Republic of Congo is

\(^{27}\) http://populationpyramid.net/angola/2050/.
\(^{28}\) http://www.hrw.org/world-report/2013/country-chapters/equatorial-guinea;
\(^{29}\) http://content.time.com/time/world/article/0,8599,1903805,00.html;
preparing new oil laws that could open it up to vast corruption and put its most important nature reserve at risk.\footnote{http://www.independent.co.uk/news/world/africa/a-murky-deal-for-the-congo-as-oil-exploration-threatens-corruption-and-environmental-damage--and-londonbased-soco-international-is-first-in-the-queue-8947899.html.}

6. CONCLUSION: CAN THE “OIL CURSE” IN THE GULF OF GUINEA REGION BE TAMED?

By collecting and analysing the data about the human development index, the corruption perception index, political freedom and civil liberties, a causal connection between the oil exports dependence and the lower human development index, a higher level of public sector corruption, as well as a lower level of political freedoms and civil liberties was proven. Through analysis of the countries from the same region, oil export dependent and the ones that do not depend on oil exports to sustain their economies, clear effects of the “oil curse” unravel. The destiny of every oil exporting country is a product of the stage in which its institutions and the society as a whole were developed at the time when oil exploitation began providing enormous profits, which were not a product of economic development and industrial production, but merely a rent. The Gulf of Guinea countries started exploiting oil at a time when their institutions were not developed. They were neither strong nor independent, so they could not affect the transparency of the public fund spending. Democratic traditions were non-existent. Oil money rents only inflated the amount of money that could be stolen by the ones who were in power and had the opportunity to steal it. Considerable proportions of oil money actually never physically reached the countries from which the oil was exported; they were simply put on the offshore accounts etc. The ruling elites in the Gulf of Guinea region oil exports dependent countries can rule almost without collecting the taxes, since they have enough money from oil rents and the support of the repressive apparatus. High prices of oil in the world markets only mean more and more money that fuels corruption and repression (and in some, rare cases some social programs).

Nevertheless, besides the cases of Venezuela or Nigeria, there are also examples of Norway and Botswana (Robinson et al., 2005: 7). Contrary to the cases of Nigeria, Angola and other countries from the Gulf of Guinea region that export oil, there are examples of Canada, Norway, United Arab Emirates or Qatar. These states are also rich in oil and/or in minerals and ores. However, their populations have many more benefits from the oil money rents. These positive trends are mainly the result of institutions that were already independent and strong (in European and Anglo-American countries) or the result of wise decisions made by the ruling elites when it comes to the use of the oil money rents (in some countries of the Arabian Peninsula and some countries of Latin America).

A key for reducing the dependence on oil exports of the Gulf of Guinea region countries (and therefore for taming the “oil curse”) is, in our opinion, contained in two main goals that these countries should aim to achieve:

1. A sustained policy of reducing, instead of boosting the production of oil, in order to save the oil reserves for as long as possible. Nigeria and Angola are, however, members of OPEC and they have to keep up to the official OPEC quotas. Other countries from the region are not OPEC members so they can boost their production without limits;
2. A more fair and even distribution of oil rent money. That means the containment of widespread corruption.

LITERATURE


7. African Affairs, (100) 55-80.


SUSTAINABILITY REPORTING: POSSIBLE WAYS OF RETHINKING HOSPITALITY ACCOUNTING

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ABSTRACT
The concept of sustainability reporting has emerged from developments in accounting, with roots over a period of the last forty years in a broader sense and in the narrow sense over the last ten years. While the term sustainability accounting is used to describe accounting methods that aim to create and provide high quality information to support a corporation in its movement towards sustainability, sustainability reporting, describes new formalized means of communication, which provides information about corporate sustainability. Sustainability accounting is a framework that can be used to reflect economic, social and environmental impacts and demonstrate their connection.

In order to get an idea of whether sustainability reporting has been implemented in Croatian companies, the purpose of the paper is to investigate the achieved level of sustainability reporting in Croatia. The paper will also critically review previous research results about sustainability reporting in the hospitality industry and develop a framework for hotel sustainability reporting, in accordance with the Uniform System of Accounts for the Lodging Industry – USALI (11th edition, 2014), Global Reporting Initiative (GRI) and the new EU Directive about disclosure of non-financial and diversity information.

Key words: sustainability reporting, hospitality accounting, sustainability accounting

1. INTRODUCTION
Accountability is the duty to provide information to stakeholders who have a right to it and an essential component of sustainability strategies. It is the information related to responsibility and is as much about what has not been done as it is about what has been done. The new challenge of hospitality business is how to be more accountable towards stakeholders.

The hospitality industry is a significant consumer of resources with a considerable impact on natural environments, economies, cultures and societies. Hotel companies are under the pressure from stakeholders and competitors to enhance their sustainability in “every day” business. Therefore, hotel companies that apply sustainable business must provide products and services that people want in order to generate profit, growth and new jobs, while taking into account their social and environmental impact, as a part of ensuring that they generate added value for an organization and its stakeholders (IFAC, 2011, p. 8).

In accordance with that, the triple bottom line (TBL) approach was developed to measure the financial performance, as well as the achieved level of social and environmental responsibility. Of particular interest is also the new EU Directive (No. 2014/95 & 2013/34) which requires obligatory disclosure of non-financial and diversity information by certain large companies.
In a business environment that expects social responsibility of companies and respect for the principles of sustainable development, hotel companies have to find a way to achieve balance between social, environmental and financial performance, and in that process sustainability reporting is of a great importance.

2. FRAMEWORK FOR SUSTAINABILITY REPORTING

Sustainability reporting describes new formalized means of communication, which provides information about corporate sustainability (Schaltegger, Bennett & Burritt, 2006, p. 15). The goal of sustainability reporting is „to inform development of an integrated business strategy for corporate management and assess sustainability risks and opportunities inherent to investment decisions” (SASB, 2013, p. 3). The demands from various stakeholders for increased levels of transparency and disclosure, and also the need for companies to appropriately respond to issues of sustainable development, are the main factors of development of sustainability reporting. Sustainability reporting is a vital step to achieving smart, sustainable and inclusive growth (EUROPE 2020, 2010) that combines long-term profitability with social justice and environmental care (GRI, 2013).

From its origins until today, there were considerable changes and advancements in sustainability reporting, going from standalone environmental and social reports, to triple bottom line (TBL) reports and at the end to sustainability reports. It is important to emphasize the distinction between TBL reports and sustainability reports. Since TBL reports in its essence display company’s results in economic, environmental and social dimensions without showing any connections between the dimensions (Schaltegger, & Burritt, 2010), sustainability reporting presents also the correlations among the three dimensions and interpretation of how it affects their business.

In the interest of delivering sustainability reports that communicate improved performance in the process of defining report content some accounting principles should be followed. According to Lamberton (2005), main sustainability accounting principles are definition, accounting period, scope, materiality, capital maintenance, units of measurement and precautionary principle. In addition to this, content should be transparent, stakeholder inclusive, provide sustainability context and allow auditing (GRI, 2002).

During the last decade number of companies producing sustainability reports has largely increased. According to the 2013 KPMG survey corporate responsibility reporting (that is regarded as sustainability reporting) “is undeniably a mainstream business practice worldwide, undertaken by 71% of the 4,100 companies surveyed, and 93% among the world’s largest 250 companies (G250)” (KPMG, 2013, p. 11), compared to “35% of G250 companies undertaking environmental reporting in 1999” (KPMG, 1999). The high rates of corporate responsibility reporting in all regions suggest that it is now standard business practice worldwide, so the KPMG view is that companies should no longer ask whether or not they should publish a corporate responsibility report but about the quality of the reporting and the best means to reach relevant audiences (KPMG, 2013). According to their research large companies in the electronics and computers, mining and pharmaceuticals sectors produce the highest quality sustainability reports. For large companies sustainability reporting should not represent an additional financial burden.

The incentive for sustainability reporting comes from different national initiatives, professional accountants associations, consultant organizations etc. Current international examples are Global Reporting Initiative (GRI), the principles of the United Nations Global Compact (UNGC), the Standard ISO 26000, OECD Guidelines and the new EU Accounting Directive of disclosure of non-financial and diversity information.
The most representative international initiative is the Global Reporting Initiative. GRI provides sustainability reporting framework to promote usage of environmental, social and economic performance indicators. By using environmental performance indicators organizations worldwide assess their environmental performance, comply with the principles of sustainable development and disclose achieved results. Some countries (e.g. Austria, Belgium, Denmark, Finland, Canada, Netherlands, Germany, Norway, USA, Sweden) officially refer to GRI guidelines in their own guidelines and standards for corporate social responsibility accomplishment and environmental responsibility and/or in their environmental policies. GRI, affiliated with the United Nations Global Compact Initiative (the initiative which also supports business sustainability and sustainable reporting), constitutes the biggest international incentive for promoting corporate sustainability, and sustainable and environmental reporting.

One of the newly emerged tools is Sustainability Balanced Scorecard that is based on the Norton and Kaplan’s concept of Balanced Scorecard but a fifth dimension – the sustainability perspective has been added. Poldrugovac and Tekavčić (2013) found nine different approaches on how to integrate sustainability into Balance Scorecard. So currently, there is no general agreement on what this sustainability perspective should consist of.

There are some other initiatives for sustainability reporting framework development. The International Federation of Accountants (IFAC) together with the GRI and The Prince’s Accounting for Sustainability Project established The International Integrated Reporting Comitee (IIRC), a body to oversee the creation of a globally accepted Integrated Reporting Framework, which combines financial, environmental, social and economic information into a comprehensive format and shows mutual influences. The framework should elicit material information from organizations about their strategy, governance, performance and prospects in a clear, concise and comparable format. The Framework is intended to underpin and accelerate the evolution of corporate reporting, reflecting developments in financial governance, management commentary and sustainability reporting (Integrated reporting, 2011).

Of particular interest today is the latest EU accounting Directive (No. 2014/95 & 2013/34) which includes obligatory disclosure of non-financial and diversity information by certain large undertakings and groups (Directive, 2014) and amends the existing EU accounting legislation to increase the relevance, consistency and comparability of disclosed information. The new legislation introduces additional non-financial disclosure requirements for large public interest entities to include a non-financial statement in their management report containing information on: environmental matters, social and employee-related aspects, respect for human rights, and anti-corruption and bribery issues (FEA, 2014).

According to the new accounting Directive, large public-interest companies with more than 500 employees are required to disclose relevant and material environmental and social information in their annual reports. Member States have to transpose the starting points of this Directive into national law by the end of 2016, and the new provisions have to be applied to all undertakings within the scope for the financial year, starting on 1 January 2017 or during the calendar year 2017. The accounting Directive requires that companies describe their business model, outcomes and risks of the policies on the mandatory topics, and encourages them to rely on recognized frameworks such as GRI Guidelines, UNGC, OECD Guidelines and ISO 26000. It promotes transparency and accountability of the companies and enables managers to use the potential of CSR in order to increase companies’ competitiveness while contributing to sustainable growth in the EU.
3. SOCIAL AND ENVIRONMENTAL REPORTING IN CROATIAN COMPANIES: RESEARCH RESULTS

The research of assessing the environmental and social responsibility of Croatian companies was conducted in spring 2013, and is based on exploring the site of HR BCSD (The Croatian Business Council for Sustainable Development) founded in 1997 as an independent non-profit association. It includes 39 members in total, of which 19 from the industrial sector, 9 representatives of big service industries as tourism, banking and utilities, and others in small businesses, consulting agencies, expert institutions, environmental NGO, media, private business school and one institution from Slovenia (http://www.hrpsor.hr). As not all member companies publish information on sustainability and environmental care, only 23 presented reports of Croatian companies were analyzed.

It is indicative that only 59% of HR BCSD members present their reports for the public use (AGROKOR; Highway Rijeka-Zagreb; Banco Popolare Croatia; Carlsberg Croatia; Coca-Cola Beverages Croatia; DUKAT; Ericsson Nikola Tesla; Farmal; Hartmann Croatia; Hauska & Partner; HEP - Croatian Electric Power Industry; Holcim; Croatian Telecom; INA; Adriatic Galenical Laboratory; Stone Sirac; KONCAR; Koncar - Institute of Electrical Engineering; PLJAVA; PODRAVKA; T-HT group; The Bank of Zagreb; Zagreb Airport). These reports were prepared in the period from 2003 till 2011 and present current state of corporate social responsibility, following experiences and global key trends in environment, supply chain, human rights, engagement in the community, sustainable products and services and others (http://www.hrpsor.hr). This indicates that only a small number of Croatian companies follow trends and experiences of environmental and sustainability reporting, according to accepted standards and principles (GRI, UN Global Compact’s requirements, ISO 14001, EMAS …).

There is no regulation regarding reporting on corporate social responsibility and sustainable development in Croatia (CSR, 2010: 14). The research results indicate that this type of reports is not present in continuous nor in standardized form and content. Some companies present reports mainly every year (Pliva; Highway Rijeka-Zagreb), some every two years (Holcim), some in reports present information for two or more years (Agrokor; Zagreb Airport) and some make combinations between more possibilities (Coca-Cola Beverages Croatia; T-HT group). Some of the companies, which present this type of reports on regular basis (since 2003), others have given up on reporting them (Ericsson Nikola Tesla; Hauska & Partner; INA; Stone Sirač; Podravka; The Bank of Zagreb…), and some have so far released only one or two reports (Agrokor; Banco Popolare Croatia; Dukat; Farmal; Hauska & Partner; HEP; Croatian Telecom; Adriatic Galenical Laboratory, Stone Sirač; The Bank of Zagreb; Zagreb Airport) in the last ten years.

Among 72 different reports presented by HR PSOR, the most commonly used term is “Report of Sustainable Development” (34,7%) followed by the term “Sustainability Report” (22,2%). In previous years the term “Environmental protection report” (15,3%) was used, and in recent years the terms “Report on socially responsible business” (9,7%) or “Corporate Social Responsibility” (6,9%) are becoming more popular. Significantly less in use appear terms “Social report (4,2%), “Annual Report” (4,2), “Sustainability and social responsibility report” (1,4%) or “Progress Report” (1,4%) (http://www.hrpsor.hr).

Regardless to the name of the report, special attention is paid to issues of environmental protection, often referring to ISO 14000ff certification standards, following the national environmental policy (waste, water, CO₂ emissions, gas emissions..) and National Sustainable Development Strategy (SSDC 2009; OG 110/07). This information is also connected with the provisions of the Environmental Protection and Energy Efficiency Fund of the Republic of Croatia (OG 107/2003), structured as an extra-budgetary fund which finances projects and
activities in three basic areas: environmental protection, energy efficiency, and the use of renewable energy sources. The important part of reports’ content is focused on labor and human rights, employee’s satisfaction and education, community involvement and development, organizational governance, as well as communication with the consumers and suppliers in order to be provided with sustainable products and services. Human rights are very important issue in the sustainability and social responsibility report, and in the last years the problem of stress increase at work is highly considered. The companies are trying to be more and more engaged in local communities, by financially supporting local sports clubs, humanitarian projects and activities guided by NGOs or other stakeholders. Orientation on sustainable products and services is also presented in reports, following trends and orientation of the EU and specific needs of particular industries. The frequency and content of items in sustainability reports is presented in table 1, according to the analysis of 11 sustainability reports of Croatian companies, published in the last three years (1) Agrokor; (2) Highway Rijeka-Zagreb; (3) Banco Popolare Croatia; (4) Carlsberg Croatia; (5) Dukat; (6) Hartman Croatia; (7) Holcim; (8) Telecom Croatia; (9) Adriatic Galenic Laboratory; (10) Končar and (11) Pliva - http://www.hrpsor.hr).
Table 1: Content and frequency of items disclosed in the sustainability reports of Croatian companies in the last three years based on the GRI 3.1.

<table>
<thead>
<tr>
<th>GRI - SUSTAINABILITY PERFORMANCE INDICATORS</th>
<th>Companies in Croatia that disclose sustainability reports*</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ECONOMIC PERFORMANCE INDICATORS</strong></td>
<td>1  2  3  4  5  6  7  8  9  10  11</td>
</tr>
<tr>
<td><strong>ECONOMIC PERFORMANCE</strong></td>
<td></td>
</tr>
<tr>
<td>EC1 Direct economic value generated and distributed, including revenues, operating costs, employee compensation, donations and other community investments, retained earnings and payments to capital</td>
<td>X  X  X  X X X X</td>
</tr>
<tr>
<td>climate change</td>
<td>X  X  X X X X</td>
</tr>
<tr>
<td>EC3 Coverage of the organization’s defined benefit plan obligations</td>
<td>X  X  X X X</td>
</tr>
<tr>
<td>EC4 Significant financial assistance received from government</td>
<td>X  X  X X X</td>
</tr>
<tr>
<td><strong>MARKET PRESENCE</strong></td>
<td></td>
</tr>
<tr>
<td>EC5 Range of ratios of standard entry level wage compared to local minimum wage at significant locations of operation</td>
<td>X  X  X X</td>
</tr>
<tr>
<td>EC6 Policy, practices, and proportion of spending on locally-base suppliers at significant locations of operation</td>
<td>X  X  X X</td>
</tr>
<tr>
<td>EC7 Procedures for local hiring and proportion of senior management hired from the local community at locations of significant operation</td>
<td>X  X  X X X</td>
</tr>
<tr>
<td><strong>INDIRECT ECONOMIC IMPACTS</strong></td>
<td></td>
</tr>
<tr>
<td>EC8 Development and impact of infrastructure investments and services provided primarily for public benefit through commercial, in-kind or pro bono engagement</td>
<td>X  X  X X</td>
</tr>
<tr>
<td>EC9 Understanding and describing significant indirect economic impacts, including the extent of impacts</td>
<td>X  X  X X</td>
</tr>
<tr>
<td><strong>ENVIRONMENTAL PERFORMANCE INDICATORS</strong></td>
<td></td>
</tr>
<tr>
<td><strong>MATERIALS</strong></td>
<td></td>
</tr>
<tr>
<td>EN1 Materials used by weight or volume</td>
<td>X  X  X X X X</td>
</tr>
<tr>
<td>EN2 Percentage of materials used that are recycled input materials</td>
<td>X  X  X X X</td>
</tr>
<tr>
<td><strong>ENERGY</strong></td>
<td></td>
</tr>
<tr>
<td>EN3 Direct energy consumption by primary energy source</td>
<td>X  X  X  X X X X X X</td>
</tr>
<tr>
<td>EN4 Indirect energy consumption by primary source</td>
<td>X  X  X  X X</td>
</tr>
<tr>
<td>EN5 Energy saved due to conservation and efficiency improvements</td>
<td>X  X  X X</td>
</tr>
<tr>
<td>EN6 Initiatives to provide energy-efficient or renewable energy based products and services, and reductions in energy requirements as a result of these initiatives</td>
<td>X  X  X X</td>
</tr>
<tr>
<td>EN7 Initiatives to reduce indirect energy consumption and reductions achieved</td>
<td>X  X  X X</td>
</tr>
<tr>
<td>Indicator</td>
<td>X</td>
</tr>
<tr>
<td>--------------------------------------------------------------------------</td>
<td>---</td>
</tr>
<tr>
<td><strong>WATER</strong></td>
<td></td>
</tr>
<tr>
<td>EN8 Total water withdrawal by source</td>
<td>X</td>
</tr>
<tr>
<td>EN9 Water sources significantly affected by withdrawal of water</td>
<td>X</td>
</tr>
<tr>
<td>EN10 Percentage and total volume of water recycled and reused</td>
<td></td>
</tr>
<tr>
<td><strong>BIODIVERSITY</strong></td>
<td></td>
</tr>
<tr>
<td>EN11 Location and size of land owned, leased, managed in, or adjacent to, protected areas and areas of high biodiversity value outside protected areas</td>
<td>X</td>
</tr>
<tr>
<td>EN12 Description of significant impacts of activities, products and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas</td>
<td>X</td>
</tr>
<tr>
<td>EN13 Habitats protected or restored</td>
<td></td>
</tr>
<tr>
<td>EN14 Strategies, current actions, and future plans for managing impacts on biodiversity</td>
<td>X</td>
</tr>
<tr>
<td><strong>EMISSIONS, EFFLUENTS, WASTE</strong></td>
<td></td>
</tr>
<tr>
<td>EN15 Total direct and indirect greenhouse gas emissions by weight</td>
<td>X</td>
</tr>
<tr>
<td>EN16 Other relevant indirect greenhouse gas emissions by weight</td>
<td>X</td>
</tr>
<tr>
<td>EN17 Initiatives to reduce greenhouse gas emissions and reductions achieved</td>
<td>X</td>
</tr>
<tr>
<td>EN18 Emissions of ozone-depleting substances by weight</td>
<td>X</td>
</tr>
<tr>
<td>EN19 NO, SO and other significant air emissions by type and weight</td>
<td>X</td>
</tr>
<tr>
<td>EN20 Total water discharge by quality and destination</td>
<td>X</td>
</tr>
<tr>
<td>EN21 Total water discharge by type and disposal method</td>
<td>X</td>
</tr>
<tr>
<td>EN22 Total water discharge by type and disposal method</td>
<td>X</td>
</tr>
<tr>
<td>EN23 Total number and volume of significant spills</td>
<td>X</td>
</tr>
<tr>
<td>EN24 Weight of transported, imported, exported or treated waste deemed hazardous under the terms of the Basel Convention Annex I, II, III and VIII, and percentage of transported waste shipped internationally</td>
<td>X</td>
</tr>
<tr>
<td><strong>PRODUCTS &amp; SERVICES</strong></td>
<td></td>
</tr>
<tr>
<td>EN25 Identity, size, protected status and biodiversity value of water bodies and related habitats significantly affected by the reporting organization’s discharges of water and runoff</td>
<td>X</td>
</tr>
<tr>
<td><strong>COMPLIANCE</strong></td>
<td></td>
</tr>
<tr>
<td>EN26 Initiatives to mitigate environmental impacts of products and services, and extent of impact mitigation</td>
<td>X</td>
</tr>
<tr>
<td>EN27 Percentage of products sold in their packaging materials that are reclaimed by category</td>
<td>X</td>
</tr>
<tr>
<td><strong>OVERALL</strong></td>
<td></td>
</tr>
<tr>
<td>EN28 Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with environmental laws and regulations</td>
<td>X</td>
</tr>
<tr>
<td><strong>SOCIAL PERFORMANCE INDICATORS</strong></td>
<td></td>
</tr>
<tr>
<td><strong>EMPLOYMENT</strong></td>
<td></td>
</tr>
<tr>
<td>LA1 Total workforce by employment type, employment contract, and region</td>
<td>X</td>
</tr>
<tr>
<td>LA2 Total number and rate of employee turnover by age group, gender and region</td>
<td>X</td>
</tr>
<tr>
<td>LA3 Benefits provided to full-time employees that are not provided to temporary or part-time employees</td>
<td>X</td>
</tr>
<tr>
<td><strong>LABOR / MANAGEMENT RELATIONS</strong></td>
<td></td>
</tr>
<tr>
<td>LA4 Percentage of employees covered by collective bargaining agreements</td>
<td>X</td>
</tr>
<tr>
<td><strong>OCCUPATIONAL HEALTH AND SAFETY</strong></td>
<td></td>
</tr>
<tr>
<td>LA5 Percentage of total workforce represented in formal joint management-worker health and safety committees that help monitor and advise on occupational health and safety programs</td>
<td>X</td>
</tr>
<tr>
<td>LA6 Rates on injury, occupational diseases, lost days and absenteeism and number of work-related fatalities by region</td>
<td>X</td>
</tr>
<tr>
<td>LA7 Education, training, counselling, prevention and risk-control programs in place to assist workforce members, their families or community members regarding serious diseases</td>
<td>X</td>
</tr>
<tr>
<td>LA8 Health and safety topics covered in formal agreements with trade unions</td>
<td>X</td>
</tr>
</tbody>
</table>
### TRAINING AND EDUCATION

<table>
<thead>
<tr>
<th>LA10</th>
<th>Average hours of training per year per employee by employee category</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA11</th>
<th>Programs for skills management and lifelong learning that support the continued employability of employees and assist them in managing career endings</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA12</th>
<th>Percentage of employees receiving regular performance and career development reviews</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X</td>
<td></td>
</tr>
</tbody>
</table>

### DIVERSITY AND EQUAL OPPORTUNITY

<table>
<thead>
<tr>
<th>LA13</th>
<th>Composition of governance bodies and breakdown of employees per category according to gender, age group, minority group membership and other indicators of diversity</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA14</th>
<th>Ratio of basic salary of men to women by employee category</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X</td>
<td></td>
</tr>
</tbody>
</table>

### HUMAN RIGHTS PERFORMANCE INDICATORS

### INVESTMENT AND PROCUREMENT PRACTICES

<table>
<thead>
<tr>
<th>LA15</th>
<th>Percentage and total number of significant investment agreements that include human rights clauses or that have undergone human rights screening</th>
</tr>
</thead>
<tbody>
<tr>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA16</th>
<th>Total hours of employee training on policies and procedures concerning aspects of human rights that are relevant to operations, including the percentage of employees trained</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X</td>
<td></td>
</tr>
</tbody>
</table>

### NON DISCRIMINATION

<table>
<thead>
<tr>
<th>LA17</th>
<th>Total number of incidents of discrimination and actions taken</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

### FREEDOM OF ASSOCIATION AND COLLECTIVE BARGAINING

<table>
<thead>
<tr>
<th>LA18</th>
<th>Operations identified in which the right to exercise freedom of association and collective bargaining may be at significant risk, and actions taken to support these rights</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

### CHILD LABOR

<table>
<thead>
<tr>
<th>LA19</th>
<th>Operations identified as having significant risk for incidents of child labour and measures taken to contribute to the elimination of child labour</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X</td>
<td></td>
</tr>
</tbody>
</table>

### FORCED AND COMPULSORY LABOR

<table>
<thead>
<tr>
<th>LA20</th>
<th>Operations identified as having significant risk for incidents of forced or compulsory labour and measures to contribute to the elimination of forced or compulsory labour</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X</td>
<td></td>
</tr>
</tbody>
</table>

### SECURITY PRACTICES

<table>
<thead>
<tr>
<th>LA21</th>
<th>Percentage of security personnel trained in the organization’s policies or procedure concerning aspects of human rights that are relevant to operations</th>
</tr>
</thead>
<tbody>
<tr>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

### INDIGENOUS RIGHTS

<table>
<thead>
<tr>
<th>LA22</th>
<th>Total number of incidents of violations involving rights of indigenous people and actions taken</th>
</tr>
</thead>
<tbody>
<tr>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA23</th>
<th>Impact assessments</th>
</tr>
</thead>
<tbody>
<tr>
<td>X</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>LA24</th>
<th>Number of grievances related to human rights filed, addressed and resolved through formal</th>
</tr>
</thead>
<tbody>
<tr>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

### SOCIETY PERFORMANCE INDICATORS

### COMMUNITY

<table>
<thead>
<tr>
<th>LA25</th>
<th>Nature, scope and effectiveness of any programs and practices that assess and manage the impacts of operations on communities, including entering, operating and existing</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

### CORRUPTION

<table>
<thead>
<tr>
<th>LA26</th>
<th>Percentage and total number of business units analysed for risks related to corruption</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA27</th>
<th>Percentage of employees trained in organization’s anti-corruption policies and procedures</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>LA28</th>
<th>Actions taken in response to incidents of corruption</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X</td>
<td></td>
</tr>
</tbody>
</table>

### PUBLIC POLICY

<table>
<thead>
<tr>
<th>LA29</th>
<th>Public policy positions and participation in public policy development and lobbying</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X X X</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LA30</th>
<th>Total value of financial and in-kind contributions to political parties, politicians and related institutions by country</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X</td>
<td></td>
</tr>
</tbody>
</table>

### ANTI-COMPETITIVE BEHAVIOUR

<table>
<thead>
<tr>
<th>LA31</th>
<th>Total number of legal actions for anti-competitive behaviour, anti-trust and monopoly practices and their outcomes</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X</td>
<td></td>
</tr>
</tbody>
</table>

### COMPLIANCE

<table>
<thead>
<tr>
<th>LA32</th>
<th>Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with laws and regulations</th>
</tr>
</thead>
<tbody>
<tr>
<td>X X X</td>
<td></td>
</tr>
</tbody>
</table>

230
### Society Performance Indicators

#### Community
**SO1. Nature, scope and effectiveness of any programs and practices that assess and manage the impacts of operations on communities, including entering, operating and existing**

<table>
<thead>
<tr>
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#### Corruption
**SO1. Percentage and total number of business units analysed for risks related to corruption**

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</table>

**SO3. Percentage of employees trained in organization’s anti-corruption policies and procedures**

<table>
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**SO4. Actions taken in response to incidents of corruption**

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#### Public Policy
**SO1. Public policy positions and participation in public policy development and lobbying**

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**SO1. Total value of financial and in-kind contributions to political parties, politicians and related institutions by country**

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#### Anti-Competitive Behaviour
**SO1. Total number of legal actions for anti-competitive behaviour, anti-trust and monopoly practices and their outcomes**

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<th>X</th>
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</table>

#### Compliance
**SO1. Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with laws and regulations**

<table>
<thead>
<tr>
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<th></th>
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<th>X</th>
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<th>X</th>
</tr>
</thead>
</table>

### Products Responsibility Performance Indicators

#### Customer Health and Safety
**PR1. Life cycle stages in which health and safety impacts of products and services are assessed for improvement and percentage of significant products and services categories subject to such procedures**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

**PR2. Total number of incidents of non-compliance with regulations and voluntary codes concerning health and safety impacts of products and services during their life cycle by type of outcomes**

<table>
<thead>
<tr>
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<th>X</th>
<th>X</th>
<th>X</th>
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</thead>
</table>

#### Product and Service Labeling
**PR3. Type of product and service information required by procedures and percentage of significant products and services subject to such information requirements**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
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<th>X</th>
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<th>X</th>
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</thead>
</table>

**PR4. Total number of incidents of non-compliance with regulations and voluntary codes concerning product and service information and labelling by type of outcomes**

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

**PR5. Practices related to customer satisfaction including results of surveys measuring customer**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

#### Marketing Communications
**PR1. Program for adherence to laws, standards, and voluntary codes related to marketing communications, including advertising, promotion and sponsorship**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

**PR2. Total number of incidents of non-compliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion and sponsorship by type of outcomes**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

#### Customer Privacy
**PR1. Total number of substantiated complaints regarding breaches of customer privacy and losses of customer data**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

#### Compliance
**PR1. Monetary value of significant fines for non-compliance with laws and regulations concerning the provision and use of producers and services**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>X</th>
<th>X</th>
<th>X</th>
</tr>
</thead>
</table>

**Source:** Prepared by authors on the basis of GRI 3.1., and content of sustainability reports presented on [http://www.hrpsor.hr/hrpsor/indexes.php/hr/izvjestavanje/popis-](http://www.hrpsor.hr/hrpsor/indexes.php/hr/izvjestavanje/popis-)
It should be noted that for the last three years only about 5% of listed companies in Croatia (11 of 206) disclose their sustainability report for public use on the web pages of HRPSOR (http://www.hrpsor.hr). It can be concluded that this type of information is primarily oriented to satisfy formality, and not to be really involved in the process of achieving the goals of sustainable development presented in National Sustainable Development Strategy. Some activities of The Croatian Business Council for Sustainable Development indicate that improvements can be expected especially through the use of CSR Index to rank companies based on their non-financial impacts and provide input to the environmental legislation throughout the business sector.

Unfortunately, none of the analysed companies that present their reports on the HR PSOR website belongs to the hospitality industry (http://www.hrpsor.hr). It is not in accordance with the possibilities of companies in the hospitality industry, because research results (conducted by authors on the sample of 199 four- and five-stars hotels of Croatian largest hotel companies), indicate that managers are involved in the process of environmental improvement and protection (Janković, Peršić, Zanini-Gavrič, 2012) and introduce sustainability principles (Peršić, M. Janković, S., Bakija, K, Poldrugovac, K. 2013) that are presented in the following table.

Table 2: Sources of information for sustainable reporting in Croatian hotels

<table>
<thead>
<tr>
<th>Tools and sources of environmental data</th>
<th>Accommodation (lodging service)</th>
<th>Food and beverage preparation service</th>
<th>Food and beverage sales service</th>
<th>Other hotel services</th>
<th>Non-commercial and administrative</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reports / statements</td>
<td>73</td>
<td>73</td>
<td>64</td>
<td>64</td>
<td>9</td>
</tr>
<tr>
<td>Questionnaire</td>
<td>73</td>
<td>73</td>
<td>64</td>
<td>27</td>
<td>9</td>
</tr>
<tr>
<td>Budget</td>
<td>73</td>
<td>73</td>
<td>64</td>
<td>27</td>
<td>9</td>
</tr>
<tr>
<td>Environmental protection program</td>
<td>73</td>
<td>73</td>
<td>27</td>
<td>55</td>
<td>9</td>
</tr>
<tr>
<td>Surveys conducted by travel agencies</td>
<td>73</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Eco - use of bed linens</td>
<td>73</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Check list of the different departments</td>
<td>69</td>
<td>73</td>
<td>64</td>
<td>27</td>
<td>9</td>
</tr>
<tr>
<td>Records of waste separation</td>
<td>64</td>
<td>82</td>
<td>64</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Hotel journal</td>
<td>64</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Statistics</td>
<td>36</td>
<td>73</td>
<td>64</td>
<td>64</td>
<td>9</td>
</tr>
<tr>
<td>Service-express</td>
<td>18</td>
<td>27</td>
<td>18</td>
<td>18</td>
<td>9</td>
</tr>
<tr>
<td>Procedures (room service, mini bar..)</td>
<td>-</td>
<td>-</td>
<td>73</td>
<td>18</td>
<td>9</td>
</tr>
<tr>
<td>Information of safety</td>
<td>-</td>
<td>45</td>
<td>64</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Programs for guests (animation…)</td>
<td>-</td>
<td>-</td>
<td>55</td>
<td>36</td>
<td>9</td>
</tr>
<tr>
<td>Waste grease disposal program</td>
<td>-</td>
<td>73</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>
The main reason for applying the principles of sustainable development is to increase their reputation in the eyes of their business partners (100%), loyalty of employees (85%) and provide a competitive advantage to attract investors (67%). The most commonly used sources for financial data in practice are segment reports, as well as budgets, both prepared using same set of rules and supported by specific software. At the same time the Questionnaire is the main source for non-financial data.

4. SUSTAINABILITY REPORTING IN HOSPITALITY INDUSTRY

The hospitality industry has been affected by both the world-wide growth in tourism and the economic recession. In accordance with these changes, hospitality management accounting is of particular importance as a tool for maximizing revenue and minimizing costs and it has been attractive research area. However, many researchers emphasise that the hotel industry lacks properly developed performance measurement system that could provide useful information for short and long term decision-making, and some of them offer a specific model for the hospitality industry. The orientation towards traditional financial measures and slow adjustment to modern trends are very often stressed (Banker et al., 2000; Mia & Patiar, 2001; Brander Brown & Atkinson 2001; Pavlatos & Paggios, 2009). Limited research has been done in the field of hospitality accounting for the needs of sustainability reporting in the hospitality industry (Mihalić et al., 2011).

4.1. Standards for internal reporting in hospitality industry

Regarding the development of management accounting in the hospitality industry, it can be argued that research and development lags behind in comparison to other industry sectors. The existence of Uniform System of Accounts for the Lodging Industry (USALI, 11th edition, 2014) plays an important role in hospitality performance measurement. It enables the widespread use of a standard chart and ensures competitive benchmarking. USALI has resulted in the development of common approaches to ratios and key statistics. According to Geller’s research (1985) the most commonly used performance measures by US hotel companies are operational and financial measures. Similar research carried out in the UK displays almost the same results. Furthermore, CIMA’s study (Collier and Gregory 1995) showed interesting findings. The most common way of measuring performance is by comparing actual with budgeted figures. Among traditional measures such as room yield, profit contribution, occupancy rates and labour cost percentage, some ways of quality measures were remarked. Brander Brown and Atkinson (2001) in their research indicate the predominance of financial and past orientated measures. Atkinson (2006) also noted it their research that not much progress has been done and little evidence exist on the development of new theories. Recent research shows that non-financial measures are being included, especially in the field of corporate social responsibility and corporate environmental responsibility (Mihalić et al., 2012).

Uniform System of Accounts for the Lodging Industry (USALI) presents information on the level of responsibility profit center (revenue, costs and internal results) of all accommodation activities (Schedule 1 - Rooms), food and beverage activities (Schedule 2 - Food and Beverage), sum of market-recognized other hotel services (Schedule 3 - Other Operated Departments) and Miscellaneous Income (Schedule 4) It also presents ten (5 - 14) schedules
for cost centers (Administrative and General; Information and Telecommunications System; Sales and Marketing; Property Operation and Maintenance; Utilities; Management Fees; Non operating Income and Expenses; House Laundry, Staff Dining, Payroll-Related Expenses) and enables comparison among hotels. (USALI, 2014).

The authors have been conducting this research in the Croatian hospitality industry, systematically in the last 15 years, and conclude that USALI standards have been successfully implemented and reporting results improved (Peršić, Poldrugovac, Janković, 2012). At the same time, sufficient degree of harmonization among operating statements based on USALI standards and information disclosed in the notes to the financial statements have not been achieved. Thus, only a smaller number of Croatian hotel companies disclose information on their segments (mostly for two – room, food and beverage) in the Notes to financial statements which is narrower than the possibility of USALI standard framework (CFA, 2013).

It actually opens up the need for supplementing internal reporting system with new reports which will contain relevant information on acquired level of environment care and achieved goals of sustainable development, based on the standards ISO 14000ff and Global Reporting Initiative 3.1. This would provide the starting point for decision making in the field of environmental protection and relations to the community, in a way to ensure uniform system of information from segment to the national level. This would enable the presentation of internally achieved results to external users, in accordance with standards, different requirements, national and regional regulations.

Managers need this type of information to guide their actions towards achieving sustainable development goals, and these requirements, should adjust accounting information system as well as reporting system for internal and external users (Banker, Potter, Srinivasan, 2000; Brander Brown, 1995; Mia, Patiar, 2001; Philips 1999; Oavlotos, Paggios, 2009). In this way it is necessary to conduct specific research to indicate the connectivity of USALI and IFRS 8 standard with the management requirements as well as external users, necessary for the quality of business decisions making and to be able to evaluate the improvement in the relationship to the environment and community.

This approach pointed out the possibility of using proven accounting tools in order to present information for decision making, which besides economic views of development includes also the ethical way of thinking. In the process of business decision-making environmental and sustainability information can no longer be ignored, because of their great importance in the long-term impact on business success. The quality of decisions made is as strong as the weakest element in the global company information system, which should be fully compliant with the requirements of internal (management) and external users (stakeholders) of information for which environmental conditions should be included in companies’ operations.

4.2. Sustainability reporting in hospitality industry

Hotel companies are initiating programs for the implementation of sustainable development into their business. However, the success of such programs will depend on the extent to which national governments encourage sustainable tourism initiatives and their ability to understand how policy impacts the hospitality industry as a whole (UNEP, 2002, p.33-42). Hospitality business influences the environment, economies and society in both positive and negative ways. Today most hotel companies strive towards sustainability, in a manner to manage resources in such a way that economic, social and environmental benefits are maximized both in meeting the needs of the present generation and protecting and enhancing opportunities for future generations (Sloan, Legrand, Chen, 2009).

Previous research has shown that hotels do report about sustainability, but the area of sustainability reporting that seemed to be lacking was environmental (Holcomb, Upchurch and
Okumus, 2007). Han, Hsu, Lee and Sheu argue that eco-friendly attitudes favourably affect hotel guests’ intentions to visit a green hotel, to spread positive word-of-mouth, and to pay more. Respectively, more efforts must be made to communicate green hotel practices to the public in order to assist the selection of green hotels and more active participation for green consumption (Han, Hsu, Lee and Sheu, 2011). As a strategic vehicle for pursuing social and environmental agenda in hospitality industry the triple bottom line framework is proposed (Hong Chung and Parker, 2011). Implementing an environmental management system would make a good starting point, because the existence of ISO 14001 certified environmental management system determines the entities to report voluntarily information related to environmental performance (Ienciu, 2012). Recommendations for future environmental reporting are making data being communicated to stakeholders more transparent (Legrand, Huegel and Sloan, 2013).

Since 1992, the trend in the hospitality and tourism industry has been on focusing on environmental concerns, use of technology, and efficient use of energy (Kalisch, 2002). This emphasis was escalated to an international scale through the implementation of Agenda 21. Agenda 21 as forwarded by the World Travel and Tourism Council (WTTC), the World Tourism Organization (WTO), and the Earth Council set international guidelines relative to sustainable tourism. The WTO established the Global Code of Ethics for Tourism (GCET), which is a “comprehensive set of ten principles whose purpose is to guide stakeholders in tourism development” (World Tourism Organization, 2005). The consumption of energy from non-renewable resources, the consumption of drinking water, as well as the amount of solid waste and waste waters are the biggest generators of environmental costs in hotels. The International Federation of Accountants, therefore, proposes the implementation of relatively simple and inexpensive measures to achieve savings - implementation of systematic monitoring and the control of resource consumption, investment in equipment and plant of lower-energy class and investment in recycling systems (IFAC, 2011).

The Green Globe 21 is a global sustainability benchmarking program designed specifically for achieving the sustainability goals and efforts in tourism and hotel industry (Green Globe 21, 2004). It offers a series of carefully chosen key performance indicators connected to the reduction of carbon emissions, energy efficiency, air quality protection, noise control, fresh water resource management, wastewater management, waste minimization, improved social and cultural relations, land management and ecosystem conservation and management. Declining resources, radical transparency and increasing expectations (Laszlo, Zhexembayeva, 2011) should be interconnected in the hotel business strategies if we want to embed sustainability into practice. The general approach of sustainability should be adjusted to the specifics of the real circumstances of a particular hotel or hotel company to answer to the following questions (Johnson, A. et al. 2003, 17):

- Which natural resources and services are used to produce and offer target product and services? How should the costs and benefits of resource use be measured?
- How integrated are energy, motivation, knowledge, capacity for relationships, and other forms of human capital? What types of and how much direct and indirect value does integration create?
- How do the tourism products and services create value for local individuals, social groups and their relationships, and how can this be measured?
- Can existing manufactured stock and infrastructure be used in way that requires fewer resources and more human creativity? Can these efficiencies and their value be measured?
o Can sustainable business practices be used to create or increase value for a hotel’s or hotel company’s stakeholders?

Well-organized management information system and sustainability accounting play a particularly important role in the process of manager decision-making, focused on the achievement of sustainable development goals in hotels and hotel companies.

Global Reporting Initiative made a comprehensive framework with detailed explanations about the components of economic, environmental and social pillar. (GRI, 2013)

Economic category covers aspects of economic performance, market presence, indirect economic impacts and procurement practices. Economic performance discloses generated and distributed value like revenues and different costs by hotel departments (room, food and beverage, sport, wellness, other operating departments…). From normalized metrics usually is used revenue per available room (RevPAR), average room rate (ADR), division revenue per guest or m2, or daily average meal check. (Wadongo, Odhuno, Kambona & Othuon, 2010).

Environmental indicators represent diverse impacts that a hotel company has on the environment. Subcategories can be divided into materials, energy, water, biodiversity, emissions, effluents and waste, compliance, overall, supplier environmental assessment and grievance mechanisms. Materials are devised on renewables and nonrenewables and are disclosed as paper or cleaning material consumption per room or per guest. Energy consumption can be measured as total or divided by energy sources and is disclosed by room or guest. Regarding the water consumption, it is important to measure percentage of recycled water and percentage of water reduction consumption. Water consumption is usually also shown per room or guest. Within biodiversity the variety of species has to be recorded and the issues that can have influence on them. Potential indicators for measurement are number of protected habitats, number of species or number of planted plants that are adapted to a particular environment.

Emissions include measuring direct and indirect greenhouse emissions, noise and dust emissions, indoor air quality as well as reduction in emissions. Effluents and waste can be divided by type, on hazardous and non-hazardous that is by the disposal methods or whether it is recyclable or non-recyclable. Compliance category comprises issues that arose while the company didn’t respect laws, regulations or standards. It can be measured in number of fines or total cost of fines. Overall category includes costs that are associated with environmental aspects like cost of investment in environmental protection or prevention costs, cost of waste treatment and remediation costs. Supplier environmental assessment category addresses suppliers that have been screened according to some environmental criteria. Different measures can be applied such as number or percentage of suppliers that have environmental management certificates or number of suppliers that deliver organic-certified food or similar. Category environmental grievance represents negative environmental actions that have been reported and resolved (GRI, 2013). All this environmental categories are usually reported by guest or rooms, or by overnights or employee.

Social category is associated with all aspects that influence social system within and outside the company and can be divided in labor practices, human rights, society and product responsibility. Labor category addresses employee and supplier related aspects from employment, training, health and safety to equal opportunities. Human rights category addresses discrimination, oppressions, child and forced labor, freedom of association and can be measured by number of implemented policies, number of actions undertaken and cost of training. Society category can be quantified as number of cooperation’s with municipality and
local residents, community satisfaction, value of political donations, number of incidents of corruption, cost of fines for non-compliance with laws, regulations and standards, number of screened suppliers according to some social criteria. Last category product responsibility includes guest satisfaction scores, overall or divided by different groups like satisfaction with employees, facilities, benefits gained, value for money or number of returning guests, number of customer complaints or similar.

5. CONCLUSION
Contemporary trends in the hotel industry force hotels on changes in their business policy and strategy. Those changes are necessary for implementing sustainability reporting.

For improving the hospitality accounting and adopt to sustainability reporting systems it would be useful to upgrade the well-developed financial reporting system, based on the USALI - Uniform System of Accounts for the Lodging Industry standards, that are compatible with the starting points of IFRS 8, and integrated with the GRI Indicators. The same principles can follow the process of sustainability reporting systems in hotel companies, which will be designed in such a way to highlight the competitive advantage of the hotel company. By using relevant indicators, a possibility of benchmarking within the global hotel industry will be ensured, with a tendency to apply the same assumptions for the other branches. Sustainability accounting has to be established on specific management requirements in order to be a relevant source of decision-making information for evaluating sustainability performance in the specific condition of a particular hotel company.

LITERATURE


THE SOURCES OF EXTERNAL IMBALANCES IN THE INTRA-EURO ZONE FROM 1999 - 2008

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ABSTRACT
This paper gives an overview over the insights into the causes of external imbalances in intra-euro zone countries in period after the formation of European Monetary Union (EMU) i.e. inception of the euro, running up to the 2008. The present debt crisis is partly a consequence of rising external imbalances in this period. According to the largely accepted traditional explanations, the deficiencies in international competitiveness in some countries are subject to interest rate convergence in core and periphery EMU countries. In this paper will be exposed the pre – euro period macroeconomic stylized facts used for creating assumptions for the general equilibrium model evolved by Farmer. The two - country one-good overlapping generations model with production, capital accumulation and public debt, with respect to capital – output ratio and under assumption of international capital mobility will show how financial integration deteriorated the net foreign asset positions of initially low-interest rates, the periphery countries. Theoretical findings will be compared with empirical observations and complemented with other explanations, such as “over-optimism”, “expected growth” and explanations that introduce some global, extra – European Union.

Keywords: external imbalance, overlapping generations model, international competitiveness

1. INTRODUCTION
In course of financial integration, after the inception of the euro in 1999, the current account position of euro-zone countries diverge in two opposite directions. While the northern and center euro countries (Austria, Belgium, Finland, Germany, Netherlands, France), accumulated current account surpluses, above in particular Germany, the southern and western periphery countries (Portugal, Ireland, Italy, Greece and Spain) run large current account deficits. Large amounts of capital inflows to southern and western periphery countries raised prices and costs. This thereby led to deficiencies in international competitiveness that can be attributed to interest rate convergence in core and periphery countries. During the process of financial integration and up the outburst of the global crisis the private debt in peripheral countries, used for financing housing investiments, increased to huge extent (Pisany-Ferry 2012, Figure 4). The large external deficits are “traditionally explained” by financial integration (Chen et al. 2012, p. 6), but there are some other additional explanations such as “over-optimism”, “expected growth” and explanations that introduce some global, extra – European Union. Fagan and Gaspar (2008) found that the development of intra-EMU external imbalances is attributed to North-South differences in time preference, by using a two-good, two-country
overlapping generations pure exchange model without public debt and under assumption of exogenously given and time-stationary capital endowment. (Fagan and Gaspar 2008, p. 13) Farmer (2012) evolved the model that respects changing capital–output ratio, mainly due to housing investments, during the process of financial integration. Although there were empirically observed slight upward and onward changes in public debt to GDP ratios across countries, in this model is public debt to GDP ratio assumed as time-stationary for the sake of simplicity (Farmer, 2012, p. 3). Some other authors emphasize the role of savings-investments balance of individual countries in the current account position, as well. (Giavazzi et Spaventa, 2010, p. 2-3).

2. AN OVERVIEW OVER THE BASIC MACROECONOMIC FACTS IN THE REPRESENTATIVE

In line with Fagan and Gaspar (2008, p. 9), the euro zone countries are separated into two groups based on the criteria of relative interest rates in the late 1990s, i.e. before the euro launch. To the first group, the core countries, belong low interest rate countries: Austria, Belgium, France, Germany and the Netherlands. To the second group, periphery or converging countries, belong the countries which had relatively high interest rates before the introduction of the euro: Portugal, Ireland, Italy, Greece and Spain. While there was a large differential in interest rates, both nominal and real, between core and periphery countries in the pre-euro period (before 1999), this differential has been annulled after the inception of the euro (Fagan and Gaspar 2008, p. 10). Since the differences in the GDP growth have not been changing significantly through financial integration, it leads us to conclusion that the interest rate convergence between euro core and periphery did not have significant impacts on GDP growth differentials (Farmer, 2012, p. 6). The personal savings ratio is continuously and significantly lower in the periphery, especially in the period between 2005 and 2008. While the housing investment (as percentage of GDP) increased to the large extent in the periphery, especially after 2000, it declined in the euro core in the same period (Farmer, p. 2012, p. 7). Such rise of private expenditures, with no adequate rise of output, resulted in net debtor positions. In the same period, euro core countries run current account balance (or surplus) and net foreign creditor position (Figure 1). Finally, the southern hourly labor compensation in manufacturing rose quicker than northern hourly compensation or more precisely: the ratio of southern to northern hourly labor compensation increased from 55% in 1998 towards 63.5% in 2008. (Farmer, p. 2012, p. 8).

Legend: _ _ periphery, _ _ core. Source: Fagan and Gaspar (2008, p. 35) and IMF World Economic Outlook Database 2008

Figure 1: Current account balances (as percent of GDP) in euro periphery and core 1995-2008
3. IMPACT OF FINANCIAL INTEGRATION ON THE INTRA-EURO ZONE EXTERNAL IMBALANCES EXPLAINED THROUGH THE ONE-COMMODITY, TWO-COUNTRY OLG MODEL

In order to deal with the effects of the (housing) capital-output dynamics on the external balances through financial integration, Farmer (2012) developed a model on the base of a one-good, two-country overlapping generations’ (OLG) model with production, capital accumulation and public debt in line with Diamond (1965) and Buiter (1981).

The definition of the real exchange rate was taken over from Lin (1994) and Lundquist (1988), as the ratio of southern to northern (real) wages.

3.1. Basic Model

The Allais – Samuelson – Diamond’s two-country one-good Overlapping Generations Model (Blanchard and Fisher, p. 91) with production, capital accumulation and public debt, with its general assumptions is taken as the basic model.

Model assumes two different groups of countries: South, which represents reduction of peripheral Euro-zone, poorer or catching-up countries, and North, which represents reduction of core Euro-zone, richer countries. For purpose of production, there are in every period $t = 1, 2, \ldots$ labor services $N_t$ $(N'_t)$ and capital services $K_t$ $(K'_t)$ employed. Production function is given by Cobb-Douglas (CD) production function: $M(a, N_t)^{1-a} (M'(a, N'_t)^{1-a'})$ to produce southern (northern) aggregate output $Y_t$ $(Y'_t)$, where $M > 0$ ($M' > 0$) denotes total factor productivity in South (North), $a_t$ denotes the common labor productivity and $\alpha$ ($\alpha'$) with $0 < \alpha < 1$ ($0 < \alpha' < 1$) denotes the capital production share in South (North).

One-period profit maximization by firms in South (North) implies the following FOCs:

\[
    w_t = (1- \alpha)Ma_t \left( \frac{K_t}{a_t N_t} \right)^{\alpha}, \quad (w'_t = (1- \alpha')M'a_t \left( \frac{K'_t}{a_t N'_t} \right)^{\alpha'}) \quad (1)
\]

\[
    q_t = \alpha Ma \left( \frac{K_t}{a_t N_t} \right)^{\alpha-1}, \quad (q'_t = \alpha'M' \left( \frac{K'_t}{a_t N'_t} \right)^{\alpha'-1}) \quad (2)
\]

whereby \( w_t \) (\( w'_t \)) denotes the real wage rate in South (North) and \( q_t \) (\( q'_t \)) denotes the real unit capital user costs in South (North).

Two generations of homogeneous individuals overlap in each period $t$. At the beginning of period $t$, a new generation of size $L_t$ ($L'_t$) enters the economy in South (North), whereby is it assumed $L_t = L'_t$ for all $t = 1, 2, \ldots$. It is also assumed that the growth factors of northern and southern populations are identical and equal to $G^L$. Due to empirical findings regarding (rather similar-) GDP growth rates in southern and northern euro zone countries (as shown in figure 4 above) it is assumed $G^a = G^{a^*}$, $G^a = G^{a^*}$, whereby $G^a$ ($G^{a^*}$) denotes the respective growth factors of labor productivities in South (North), and $G^a$ ($G^{a^*}$) denotes the natural growth factors in South (North) and $G^a = G^{a^*} G^L$.

Each generation lives for two periods, working during the first when young (denoted by superscript 1), and retiring in the second when old (denoted by superscript 2).
In order to isolate the impact of the common currency in 1999 and to put it into the intertemporal general equilibrium model, following Gourinchas and Jeanne (2006), and Fagan and Gaspar (2008), it is assumed the existence of a) financial autarky of both countries, South and North, before the inception of the common currency, and b) financial integration, in period after launching the euro.

3.2. Intertemporal Equilibrium under Financial Autarky

In order to make the way of building the model of pre-euro situation as financial autarky simpler, some empirical facts will be taken as assumptions: 1. large real interest rate differences between core and peripheral countries, for the benefit of core countries; 2. non large current account deficits in southern countries – that is why we will assume that both the current account and the net foreign asset position of South and North were zero; 3. small differences in debt to GDP ratio between core and peripheral countries – that is why we will assume that the government debt to GDP ratios, b, in South and North remain constant over time; 4. the personal savings ratio, σ in South was persistently lower than in euro zone core countries (North). Further, as reference with differential development of labor compensations costs across euro-zone core and periphery, respective differences in southern and northern production technologies will be assumed (Farmer: 2012, p. 12).

Steady-state intertemporal equilibrium for the capital output ratio

A steady-state intertemporal equilibrium for the capital output ratio \( v_{t+1} = v_t = v \) (\( v_{t+1} = v^* = v^* \)) is:

\[
v^2 + \frac{G^*b - \beta(1-\alpha-\gamma)}{G^n(1+\beta)}v^* + \frac{\alpha b}{G^n(1+\beta)}v^* + \frac{\alpha^* b^*}{G^n(1+\beta)} = 0
\]

The relatively high capital production share α and the low savings rate σ in South imply under financial autarky that the steady-state capital output ratio v in South is lower than in North, and it is attributed to the higher real interest i and a relatively low real wage rate w i.e.: if \( \alpha > \alpha^* \), \( \gamma > \gamma^* \) and \( \sigma < \sigma^* \), then \( v_2 < v_2^* \) implying \( i > i^* \) and \( w < w^* \). For the sake of simplicity is taken that \( b^* = b \) and \( b < b^* \). Comparing assumptions of the conclusion regarding capital production share α, savings rate σ and government expenditure share γ, with empirical findings with respect to northern and southern candidate countries for EMU in the late 1990s, it will lead us to the following: a) \( \alpha > \alpha^* \) is empirically warranted, since the southern European countries were (are) less developed (lower GDP per capita) than the northern European countries and the existence of empirical examples for the fact that the capital production share is higher in catching-up than in advanced countries (Bai and Quian: 2010); b) \( b^* = b \) is not empirically warranted (Lane 2012, p. 51), but the reality closer assumption \( b > b^* \) would enforce the claim in the last conclusion; c) \( \gamma > \gamma^* \) is not empirically warranted for less developed countries; in fact, highly developed countries exhibit larger expenditure shares than less developed countries. If we observe Italy as large-economy, which belongs to the southern bloc, the assumption \( \gamma^* = \gamma \) remains relevant; d) \( \sigma < \sigma^* \) is empirically warranted. Last conclusion is intuitively plausible. A low savings rate and a relatively high capital income share (corresponding to a relatively low labor income share associated with low per capita savings) drive the capital output ratio down to ensure asset market clearing. Moreover, due to decreasing marginal productivity of capital, the lower capital output ratio is associated with a higher interest rate and a lower real wage rate. (Farmer, 2012, p. 17)
### 3.3. International Equilibrium under Financial Integration

In order to mimic financial integration after the formation of the EMU, it is taken as assumption that both physical capital (that is mainly accumulated by housing investment, in accordance with empirical finding) and government bonds can be freely traded across both countries without incurring any transaction costs - in line with Buiter (1981) and Lin (1994). Since the interest rate are higher in South, northern younger households will use their savings to invest in southern physical capital and buy the bonds emitted by the southern government until the southern real interest rate declines as much as there is no longer an incentive to shift northern savings towards the South.

It is assumed that domestic and foreign real capital as well as domestic bonds and foreign bonds are perfect substitutes.

**The intertemporal equilibrium capital output ratio dynamics**

From the national Fisher equation and the international Fisher equation, the following relationship between northern and southern capital output ratios can be derived as follows:

\[
 V_{t+1}^{*} = \frac{\alpha^*}{\alpha} V_{t+1}.
\]

whereby the \( V_{t+1}^{*} \) denotes the northern capital output ratio at the beginning of period \((t+1)\), \( V_{t+1} \) denotes the southern capital output ratio at the beginning of period \((t+1)\), \( \alpha^* \) the northern capital production share and \( \alpha \) the southern capital production share.

The intertemporal equilibrium capital-output ratio dynamics of the one-good, two-country OLG model under financial integration:

\[
 i_v = \frac{\alpha^*}{\alpha} \mu V_{t+1}^{1/(1-\alpha^*)} + b(1-\sigma) V_{t+1} a/(1-\alpha) + b^*(1-\sigma^*) \mu V_{t+1}^{a/(1-\alpha^*)} \\
= \frac{\sigma}{G^*} [(1-\alpha - \gamma) - \frac{ab^*}{v_i}] V_{t+1} a/(1-\alpha) + \frac{\sigma^*}{G_n} [(1-\alpha^* - \gamma^*) - \frac{ab^*}{v_i}] V_{t+1} a/(1-\alpha^*) \]

Hence, the union-wide real interest rate, \(i\), southern and northern real wage rates, \(w\), and thereal exchange rate between South and North, \(e\), are attributed to the motion of the capital output ratio. The real exchange rate is defined in line with Lundquist (1988) and Lin (1994) as follows:

\[
e_{t+1} = \frac{\alpha^*}{\alpha} \mu V_{t+1}^{1/(1-\alpha^*)} \left( \frac{\alpha^*}{\alpha} \right)^{\alpha^*/(1-\alpha^*)} \left( \frac{\alpha}{\alpha} \right)^{\alpha/(1-\alpha)} \]

\[
e_{t+1} = \frac{a_{t+1} M^{1/(1-\alpha)}}{(1-\alpha) a_{t+1} M^{1/(1-\alpha)} a/(1-\alpha) \left( V_{t+1} \right)^{a/(1-\alpha)}} \]

\[
e_{t+1} = \frac{(1-\alpha) a_{t+1} M^{1/(1-\alpha)} a/(1-\alpha) \left( V_{t+1} \right)^{a/(1-\alpha)}}{(1-\alpha) a_{t+1} M^{1/(1-\alpha)} a/(1-\alpha) \left( V_{t+1} \right)^{a/(1-\alpha)}} \]

From (4) and (5), and under assumption \( \alpha > \alpha^* \), it can be easily seen that:

a) the common real interest rate, \(i\), declines with rising capital output ratio in South,
b) both the southern and the northern real wage rates, \( w \), increase with rising capital output ratio in South (North), and
c) the real exchange rate of South, \( e \), increases with rising southern capital output ratio.

### 3.4. Financial autarky vs. financial integration

Definition of a steady state intertemporal equilibrium of the capital output ratio under financial integration is:

\[
\begin{align*}
1_{t+1} &= 1_t, \\
v_{t+1} &= v_t, \\
v^*_{t+1} &= v^*_t, \\
e_{t+1} &= e_t, \\
i_{t+1} &= i_t, \\
w^*_{t+1} &= w^*_t, \\
w^*_{t+1} &= w^*_t.
\end{align*}
\]

The relationship between northern and southern capital output ratios: \( v^* = \frac{\alpha}{\alpha} v \) \((6)\)

and the intertemporal equilibrium capital-output ratio dynamics of the one-good, two-country OLG model under financial integration:

\[
\frac{\sigma^*}{G^*} \left( 1 - \alpha - \gamma - \frac{\alpha b}{v} \right) - \left[ v + b(1 - \sigma) \right] =
\]

\[- \left\{ \frac{\sigma^*}{G^*} \left( 1 - \alpha^* - \gamma^* - \frac{\alpha^* b}{v^*} \right) - \left[ \frac{\alpha^*}{\alpha} v^* + b^* \left( 1 - \sigma^* \right) \right] \right\} \mu v^*,
\]

or \( \phi = - \frac{Y^*}{Y} \phi^* = - \mu v^* \phi^* \), \((8)\)

whereby \( \phi_{t+1} = \Phi_{t+1}/Y_{t+1} \) (\( \phi_{t+1} = \Phi_{t+1}/Y^*_{t+1} \)) denote the net foreign asset position per output unit of South (North) in period \((t+1)\). The (7) and (8) claim that in a steady state the southern net foreign asset position exactly equals negative position of northern net foreign assets multiplied by the northern to southern GDP ratio.

While financial autarky implies both net foreign asset positions equal to zero and the real interest rate in South higher than in North, financial integration implies a negative southern and a positive northern net foreign asset position (Farmer, 2012, p. 23).

By the assumptions that the southern financial autarky interest rate, \( i^* \), is larger than the northern financial autarky interest rate, \( i^* \), after financial integration, the ratio of the net foreign asset position to GDP of South (North) is negative (positive), i.e. \( \phi < 0 \) (\( \phi > 0 \)).

If \( i > i^* \), then holds \( 1 + i = \alpha/v > 1 + i^* = \alpha^*/v^* \), which lead us to conclusion that decline of \( i \), (southern interest rate) is associated with rise of \( v \) (capital output ratio) in financial integration, which is explained through the decreasing marginal productivity of capital (the opposite case holds for the North).

Differentiating \( \phi(v) \) (from the definition of the southern net foreign asset position \( \phi(v) = \frac{\alpha^*}{G^*} \left( 1 - \alpha - \gamma - \frac{\alpha b}{v} \right) \) with respect to \( v \), we obtain \( \phi'(v) = \frac{\alpha^* \alpha b}{G^*} v^2 - 1 \). \( \phi'(v^*) < 0 \) occurs in the neighborhood of the southern autarky steady state with the larger capital intensity \( (K_t/A_t) \).

Hence, the southern net foreign asset position deteriorates with rising southern capital output ratio. According to equation (6) or (7), the northern net foreign asset position is positive after financial integration.

If we evaluate equations (4) for the non-trivial steady state, it can be easily seen that the common real interest rate is lower than southern autarkic real interest rate and that the southern real wage rate is higher and the northern real wage rate is lower than the autarkic values.
By the assumption $\alpha > \alpha^*$, the southern real exchange rate rises after the beginning of the process of financial integration. If we evaluate equation (5) in the steady state, and using the definition of real exchange rate of Lundquist (1988) and Lin (1994) ($e_t = w_t / w^*_t$), it is obvious the positive relationship between the real exchange rate and southern capital output ratio, by $\alpha > \alpha^*$.

4. EXTERNAL (GLOBAL) INFLUENCES ON EXTERNAL IMBALANCES AND THE ROLE OF EXPECTATIONS

Among financial integration, as a dominant determinant of the external imbalances in intra-euro zone, there are some other factors, empirically and / or intuitively found, that are counted by some authors and that cannot – so far – be put altogether in the theoretic model.

The large current account imbalances of individual intra-euro zone countries are, to a significant extent the consequence of the very asymmetric impact of trade shocks originating outside the euro area, as well as sustained cheap financing from core euro area countries to the largest net debtors. (Chen et al. 2012, p. 4). The factor of essential importance is the entering into the global market and economic rise of China, that negatively affected several southern European countries, causing losses on their international competitiveness – logically, Chinese import demand provided little benefits to the trade balance of these countries. Moreover, the sharp nominal appreciation of the euro contributed to the loss on competitiveness of deficit countries within the euro zone due to domestic prices and wages. At the same time the rise of China generated huge demand for machinery and equipment goods exported by Germany, while exports from intra-euro zone debtor countries were substituted in their foreign markets by Chinese exports. The same has happened as a consequence of the rise of oil prices: higher income in oil producing countries generated strong demand for machinery and equipment exported by Germany, as well (Chen et al. 2012, p. 4). Empirical findings show that the results for export demand elasticities for goods exported by Greece, Italy, Portugal and Spain are significantly below the euro area average, which proofs the displacement effect on the exports from intra-euro zone countries (Chen et al. 2012, p. 15).

The process of international financial integration with elimination of currency risk and the decline in credit constraints and real interest rates, together with over-optimistic expectations of convergence can also lead to increases in domestic prices and unit labor costs that are inconsistent with underlying productivity gains and with the external budget constraint (Chen et al. 2012, p. 8).

Some authors has shown that foreign-financed real estate booms may result in unsustainable growth of non-tradable sectors (Giavazzi and Spaventa, 2010, IMF, 2011).The same authors emphasize the role of relative prices and its impact on capital flows between euro-zone countries and the rest of the world. The relative price movements within the intra-euro zone area, together with trade deficits and associated capital inflows, contributed to the debtor countries’ real exchange rate appreciation (Chen et al. 2012, p. 5).

The next stimulating factor was expected growth, i.e. expectation of convergence in the intra-euro zone, that stimulated capital inflows by eliminating currency risk (Chen et al. 2012, p. 7). The “over-optimism” contributed to higher consumption / investment (especially housing) and not corresponding savings ratio. It also contributed to real exchange rate appreciation (Chen et al. 2012, p. 8).

The resulting real exchange rate appreciation contributed to crowding out production and export activities, experiencing low productivity gains and stagnant economic growth, as the competitiveness of tradable goods declined. It logically led to a very significant deterioration of current accounts. Together with rigid labor markets, it leads growing competitiveness differentials among intra-euro zone countries (Chen et al. 2012, p. 8).
5. CONCLUSIVE CONSIDERATION
External imbalances in some intra-euro zone countries in period after the formation of European Monetary Union (EMU) i.e. inception of the euro, running up to the 2008, can be, as diverse theoretic and empirical analysis has shown, attributed to financial integration, “over-optimism”, “expected growth” and explanations that introduce some global, extra-European Union, such as entering of the Republic of China on the global market, increase of oil price etc. Financial integration as a main determinant of external imbalances is “tradiional explanation”, that is broadly accepted and empirically indubitable explanation.

The presented model has shown how the decrease of southern interest rate is associated with the rise of capital output ratio after financial integration, which can be explained through the decreasing marginal productivity of capital (rising capital intensity). Moreover, the southern net foreign asset position was deteriorating with rising southern capital output ratio, so the net foreign debtor of southern countries through financial integration can be traced back to the lower savings rate and the larger capital production share in South. High southern real interest rate stimulated northern agents to invest into the southern housing and residential objects, that is why the southern countries turned into the net foreign debtor position. Since the southern real wage rate rose faster than the northern, the real exchange rate appreciate, as it was shown in the model.

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**ESTIMATING THE DETERMINANTS OF GROWTH STABILITY AND INSTABILITY IN SUB-SAHARAN AFRICAN COUNTRIES: A MARKOV SWITCHING APPROACH**

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**ABSTRACT**

The goal of the present paper is to study the asymmetries characterizing African growth path. To model switching between output collapses and growth stability, we apply a Markov-switching model with time varying transition probabilities on 37 African countries over the period 1987-2011. Two distinct growth regimes are identified: a stable growth regime, which, despite the presence of negative values of the growth rate, is stable, and a highly volatile growth regime, in which the growth behaviour range from negative to positive picks of the growth rates, and vice versa. From our analysis, we observed that the likelihood of an economy being in a stable growth regime increases with the political regime, trade and variation in the exchange rate.  

**Keywords:** Economic Growth; Markov Regime-Switching Model; Sub-Saharan Africa.

**1. INTRODUCTION**

The present paper aims to study the change of growth patterns and its determinants within African countries. To do that, we apply a Markov Switching Model with time varying transition probability, relying on the idea that the country’s growth path is the result of different growth regimes (Jerzmanowski, 2006).

In other words, we assume a latent trait underlying the time series of growth rate, which explains the transition between different growth regimes occurring without obvious changes in country-fundamentals.
The lack of a linear pattern is typical of developing and emerging countries, that are characterized by large fluctuations and swings of the growth rate (see among others Becker et al., 2006), and asymmetric interchange between phases of growth acceleration and regime collapse (e.g. Easterly et al., 1993; Jerzmanowski, 2006; Kerekes, 2012; Jones and Olken, 2008). In particular, the most volatile growth rate and the most frequent output collapse\(^1\) are recorded in Sub-Saharan Africa. This region is characterized by different growth behaviours over time, in terms of different balanced growth paths, different within-state variability and different long-run growth rates. This stylized fact implies a failure, for this region, to conform to economic growth theories, especially of convergence model, that predicts a rapid and regular growth rate for these countries. Indeed, the difficulty for African countries to sustain growth for substantial period, and asymmetric switching between stable growth and economic collapses is tested by Byrne (2010)\(^2\).

\(^1\)Output collapse is described as a dip or a decline in GDP.
She also provides empirical evidence of different behaviours of the time series of growth over phases of stable growth and output collapse.

To model the evolution of the growth rate over time accounting for the different regimes, we apply a Markov Switching approach with time varying transition probability (e.g. Filardo, 1994, Filardo and Gordon, 1998, Diebold et al., 1994 Kerekes, 2012) to 37 African countries over the period 1987–2011. This statistical approach allows us to disentangle the different growth paths within countries, and to reject the hypothesis, commonly followed by standard growth regression, that countries follow constantly and indefinitely a linear growth path (Pritchett, 2000).

Entering into details, it allows us to deal with non-linear properties of the regression function such as asymmetry, dependency weights and volatility. Furthermore, it splits the time series into a discrete number of regimes, simultaneously estimating the transition from one state to another, whether the variable leading to regime shift is unobservable. Although other models commonly used to study the growth rate variation, such as autoregressive (AR), moving average (MA) or autoregressive integrated moving average (ARIMA) can capture the dynamics in data, they are unable to capture the fact that the variable under estimation change its behaviour during time, i.e. it switches between regimes (see among others Kuan, 2002, Bilgili et al., 2012).

The time varying transition probability allows us to deal with two challenges. Firstly, we can understand long run growth pattern by determining the length of time a country remains in the same regime as dependent on country fundamentals. For this reason, we believe that the Hamilton (1989)’s seminal paper is too restrictive for explaining economic growth dynamics, and we apply the Filardo (1994) and Diebold et al. (1994) extension. Secondly, since the transition probability depends on country-specific factors, we allow for cross country differences in the growth process, avoiding to model the growth process as common across countries. In this way, we can evaluate the effect of country fundamentals on switching regimes, i.e. the impact of economic factors on the movement across growth phases.

Previous works about switching growth determinants are also present in literature with special references to papers by Hausmann et al. (2005), Byrne (2010) and Jerzmanowski (2006). The present paper closely follows the Byrne (2010)’s intuition about the need for applying Markov Switching Model with time varying transition probabilities to understand the African countries growth dynamics. On the other hand, it takes its theoretical basis from the Hausmann et al. (2005)’s work for the choice of the explanatory variables of the discrete latent process. Their empirical findings provide evidence in favour of the accelerating mechanisms of investment, trade, and real exchange rate depreciation and changes to political regimes. It is worth noting that empirical evidence shows that expansion of international trade has been noted to be a primary catalyst for starting growth phases (Becker et al., 2006).

From our analysis, two distinct growth regimes are identified: a stable growth regime, which despite the presence of negative values of the growth rate, is stable and a highly

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2Byrne (2010) applies a Markov Switching Model with time varying transition probability to a panel of Sub-Saharan African countries over the period 1960–2004. She models the transition probability matrix as
dependent on education, quality of institution, trade, and dummy variables capturing the composition of output (fuel, agriculture, manufacture).

3 Hausmann et al. (2005) identify the growth acceleration phases defining a threshold for the growth rate
volatile growth regime, in which the growth behaviour range from negative to positive picks of the growth rates, and the variance within the group is extremely high. Furthermore, the probability of switching to the highly volatile regime positively depends on exchange rate depreciation, trade and foreign direct investment. The paper is structured as follows. Section 2 describes the Markov Switching approach with time varying transition probabilities. Section 3 presents the empirical application on African countries, pointing out the results. Section 4 concludes and presents some possible extensions.

2. STATISTICAL SPECIFICATION
To formalize the different phases of growth each country faces over time, we start defining the existence of M latent states of the economy. In particular, since African countries are mainly characterized by two asymmetric regimes, unstable and stable growth (Byrne, 2010), we specify the two-state Markov switching approach. Furthermore, to allow the growth process to be not identical across countries, we model the switching process as dependent on country specific variables, through the time varying transition probability. Formally, we denote $S_t$ the discrete latent variable that takes only two values over the space $M$, such that $S_t = \{1, 2\}$, and $y_t = \{y_{it}\}$ the vector containing continuous realization of the dependent variable (i.e. the growth rate) recorded for each country $i$ ($i = 1, \ldots, n$) at time $t$ ($t = 1, \ldots, T$). We assume that the dependent variable follows an AR(1) process as:

$$y_{it} = \alpha_{S_t} + \beta_{S_t} y_{i,t-1} + \varepsilon_{S_{it}}$$  \hspace{1cm} (1)

where $\varepsilon_{S_{it}} \sim N(0, \sigma_{S_{it}}^2)$, with $\text{cov}(\varepsilon_{i,t}, \varepsilon_{j,t}) = 0$, is the error term which allows for different variability within the states, i.e. the regime varying variance represents the uncertainty measure of output occurring in each state of the economy. The evolution of the dependent variable over time depends on the history of the variable itself $y_{it-1}$. The autocorrelation effect, captured by the $\beta_{S_t}$ parameter, changes its magnitude on the basis of which latent regime occurs, and it allows for formalizing the impact of the latent variable on the growth path.

Moreover, we explicit the two different paths of the growth rate according to which state of the economy is verified as:

$$y_{it} = \alpha_1 + \beta_1 y_{i,t-1} + \varepsilon_{i,t1} \quad \text{if} \quad S_t = 1$$
$$y_{it} = \alpha_2 + \beta_2 y_{i,t-1} + \varepsilon_{i,t2} \quad \text{if} \quad S_t = 2$$  \hspace{1cm} (2)

The model described by the system of equation (2) highlights the key feature of the Markov Switching approach: the definition of the conditional distribution of the time series of the response variable as dependent on the underlying latent state.$^4$

Following Diebold et al. (1994) and Filardo (1994), we assume that the latent variable is not completely unobservable, but it partially depends on economic factors included in the set of explanatory variables $z_t$. To endogenize probabilistic changes of regime, $^4$It is worth noting that the formalized model above may also be extended by including a set of $X_t$ explanatory variables (see Kim et al., 2008 for further details.) affecting the distribution of the growth rate. This paper aims to understand what leads the transition between different growth regime. Thus, for sake of simplicity and parsimony in the computational framework, we reduce the model on the “direct” effect on growth dynamics only as dependent on the previous value of the growth rate.
since the statistical properties of the discrete latent variable are summarized by the transition matrix, we define the time varying transition probability \( \Pi(z_t) = p(S_t = j | S_{t-1} = k, z_t) = p_{jk}(z_t) \), with \( (j, k) \in M \), as dependent on economic and political factors. We denote \( p_{jk}(z_t) \) the probability of having in place regime \( j \) in period \( t \), conditional on having in place regime \( k \) in period \( t-1 \). By specifying that the switching of regimes follows a first order Markov chain, as \( p_{11} = p(S_t = 1 | S_{t-1} = 1, z_t) = p(z_t) \) and \( p_{22} = p(S_t = 2 | S_{t-1} = 2, z_t) = q(z_t) \), we infer the influence of \( z_t \) on the transition matrix \( \Pi(z_t) \), by a probit specification for \( S_t \) over \( 1, 2 \). Thus, we specify the linear regression of the latent variable on the set of covariates and latent traits as:

\[
S_t = a_{s_{t-1}} + z_t b_{s_{t-1}} + u_t
\]

where \( u_t \sim N(0, 1) \), and it is not correlated with \( \varepsilon_t \) (see Filardo and Gordon, 1998). We emphasize that the probability of switching over the state, as well as remaining in the same state, partially depends on time and on variables contained in \( z_t \). Hence, we incorporate economic variables as determinants of the probability of changing or moving from one state of the economy to another (Diebold et al., 1994). The estimation of the full parameter vectors \( \Theta = (\beta_{S_t}, \sigma_{S_t}, \Pi(z_t)) \), is obtained by applying the Maximum Likelihood Method to the complete data log-likelihood\(^6\).

We justify the use of time varying in place of time fixed transition probability by the increased and the ability of the former in capturing systematic changes before and after the turning points. Furthermore, since we include economic variables in the estimation of the switching process, it is possible to evaluate how the end of a highly unstable growth regime is affected by the country fundamentals.

3. EMPIRICAL FORMULATION

3.1 Data

The sample is composed by an unbalanced panel of 37 African countries, from 1987 to 2011. Data are retrieved from Summer and Heston database. The dependent variable is the growth rate of income per capita. Skewness and kurtosis values, as well as the Shapiro and Wilk test (\( W = 0.97290 \), with \( p = 0.0000 \)) performed on the growth rate, display departure from normality distribution.

\[ \text{Figure 1: QQ Plot distribution of the Dependent variable (own elaboration)} \]

\(^3\)The model is estimated through the Matlab Package developed by Ding (2012).

\(^6\)The second category of Political Regime includes: One-Party; military state; one party military state; monarchical state; limited multiparty

As the QQ-Plot confirms (see Figure 1), it is possible to conclude that the growth rate has not a Gaussian distribution. Indeed, the heavy tails suggests that is better to
approximate the distribution of the dependent variable through a t-student. The independent variable is the one year lagged value of the growth rate (see among others Kerekes, 2012; Byrne, 2010). The variables affecting the first order Markov chain are chosen on the basis of Hausmann et al., (2005)’s empirical findings, and they are: trade, foreign direct investment, variation in the ex-change rate and political regime. Statistical details about transition probability’s explanatory variables are provided in the following table.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>Std. Dev.</th>
<th>Min.</th>
<th>Max.</th>
</tr>
</thead>
<tbody>
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<td>-8.59</td>
<td>46.49</td>
</tr>
<tr>
<td>Trade</td>
<td>-11.098</td>
<td>20.617</td>
<td>-126.56</td>
<td>48.96</td>
</tr>
<tr>
<td>ΔExch Rate</td>
<td>17.056</td>
<td>93.856</td>
<td>-951</td>
<td>931.96</td>
</tr>
</tbody>
</table>

n. obs. 649

<table>
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<tr>
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<tbody>
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<td>Pol.Regime=1</td>
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<td>24.19</td>
<td>24.19</td>
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<td>Pol.Regime=2</td>
<td>464</td>
<td>71.49</td>
<td>95.69</td>
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<tr>
<td>Pol.Regime=3</td>
<td>28</td>
<td>4.31</td>
<td>100.00</td>
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</tbody>
</table>

n. obs. 649

It is worth emphasizing that, for sake of simplicity in the coefficient interpretation, the political regime is formalized as a categorical variable, equal to 1 in democracy, 2 in autocracy and 3 in the Transitional Regime. The latter includes: rebel regime, civil war and transitional regime; while different “levels” of autocracy are included in the second category.

3.2. THEORETICAL SPECIFICATION

In order to understand the variation in the growth path of African countries, following Jerzmanowski (2006), we assume that economic growth is the result of switching between distinct growth regimes. Variables used to model the transition between different states are based on Hausmann et al. (2005)’s empirical findings. Their results provide evidence that foreign direct investment (FDI henceforth), trade, depreciation of the real exchange rate and changes in political regimes are the main reasons behind the phases of economic acceleration. Thus, the regression function can be formalized as:

\[ E(g_{ct}) = \alpha S_t + \beta S_{t-1} \text{growthit} - 1 \] (7)

where

\[ S_t = a_{t-1} + b_1 S_{t-1} \text{trade} + b_2 S_{t-1} \text{political} + b_3 S_{t-1} \text{fdi} + b_4 S_{t-1} \text{Δexch rate} \] (8)

Equation (7) and equation (8) model the cross-country differences in growth dynamics, i.e. the non-linear country - specific growth paths, as dependent on political and economic factors.

---

7 As specified in Section 2, we assume that within each regime economic growth evolves according to an AR(1) (see among others Kerekes, 2012).

8 We emphasize that the impact of the β parameters of equation (8) should not be read in terms of impact of the economic and political variables on the growth rate, but on the transition from one regime to another.
In other words, these equations disentangle the time series of the growth rate according to which latent state occurs in the economy, that, in turn, partially depends on FDI (fdi), trade (trade), exchange rate variation (∆exch rate), and political regime (political). Entering into details, we assume that switching in growth dynamics is associated to variables that capture and affect the ability of each country to deal with internal or external shocks. For this reason, political regime is the key variable in our analysis. Indeed, it is empirically demonstrated that the presence of internal conflicts reduces the ability of a country to deal with the impact of shocks (Rodrik, 1999), leading the growth rate to switch between different phases. It is worth noting that as Durlauf et al. (2005) point out, it is common to assume that whereas output collapses are common and significant in terms of magnitude, they should be better explained by the institutional quality rather than changes in political setting. However, as Kerekes (2012) argues, the dependence assumption of the transition probability matrix on the country’s quality of institutions has some drawbacks. Firstly, the fact that it is usually estimated at the end of the sample period could generate endogeneity problems; secondly, it could change as consequence of economic growth (Glaeser et al., 2004), leading to inconsistency problem of the Markov Switching model (Kim, 2004).

Furthermore, economic instability within African countries is directly related to FDI, trade and exchange rate. Firstly, FDI are found to be one of the main reason behind economic acceleration, since they boost economic growth through different channels: employment creation, technological know-how, managerial skills, and competitiveness (see among others Kobrin, 2005 and de Mello Jr, 1997 for a survey literature). Furthermore, as Asiedu (2002) points out, the low level of FDI inflows recorded in Africa in past decades is mainly due to political and macroeconomic instability, in terms of poor infrastructure, weak investment promotion strategies and high protectionism (Dupasquier and Osakwe, 2006). Secondly, both trade and exchange rate variation capture economic external shocks, and are crucial for growth phases (Cuaresma and Worz, 2005). In particular, the sensitivity to trade volatility is higher in less developed countries rather than developed economies (Blattman et al., 2004), while the depreciation of exchange rate has a positive impact on growth if it is allowed to operate through aggregate supply channels (Thapa, 2002; Golley and Tyers, 2006 and Akinbobola and Oyetayo, 2010).

3.3. RESULTS

In our benchmark specification, we assume that there is an unobservable exogenous random process which determines the behaviour of African economic growth rate. Thus, we estimated a two state Markov Switching model with time fixed transition probability. Following Hamilton (1989), we assume that the transition probabilities are constant over time, and they do not depend on covariates.

Hence, the benchmark model reads as:

\[ E(\text{growth}_{it}) = \alpha S + \beta S \text{growth}_{it-1} \quad (9) \]

9 Akinbobola and Oyetayo (2010) concluded that the positive effect of exchange rate variation can be within the context of a broader program of adjustments and reforms.
where the state (latent) variable $S$, affecting the intercept and the autocorrelation coefficient, is completely unobservable. It is worth reminding that the use of the time varying (TVTP henceforth) in place of the time fixed transition probability (TF henceforth) is justified by the philosophical approach of the former in capturing the impact of economic fundamentals on the turning points. Furthermore, penalized likelihood criteria (AIC and BIC) confirm the choice of the TVTP approach in place of the Hamilton (1989) approach (see Table 2). For sake of completeness, a model with $M = 3$ is performed.

*Table 2: Results.*

<table>
<thead>
<tr>
<th></th>
<th>Coef</th>
<th>SE</th>
<th>Coef</th>
<th>SE</th>
</tr>
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<tr>
<td>Growth rate:</td>
<td></td>
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<td></td>
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<tr>
<td>$\text{growth}_{1t-1}$ (Regime 1)</td>
<td>0.8403***</td>
<td>0.0473</td>
<td>0.5730***</td>
<td>0.050</td>
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<tr>
<td>$\text{growth}_{1t-1}$ (Regime 2)</td>
<td>0.2565***</td>
<td>0.038</td>
<td>0.2217***</td>
<td>0.051</td>
</tr>
<tr>
<td>$\alpha_{S_{t}=1}$ (Regime 1)</td>
<td>0.8226***</td>
<td>0.2209</td>
<td>1.8751**</td>
<td>0.2242</td>
</tr>
<tr>
<td>$\alpha_{S_{t}=2}$ (Regime 2)</td>
<td>2.9752***</td>
<td>0.2557</td>
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<tr>
<td>$\sigma_{S_{t}=1}^{2}$</td>
<td>1.0000***</td>
<td>0.2235</td>
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<td>$\sigma_{S_{t}=2}^{2}$</td>
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<td>$p_{1,1}$</td>
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<tr>
<td>$p_{2,2}$</td>
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<td>Duration Regime 1</td>
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<tr>
<td>Duration Regime 2</td>
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<td>686</td>
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</tr>
<tr>
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<td></td>
</tr>
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<td>AIC</td>
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<td>-1695.67</td>
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<tr>
<td>BIC</td>
<td>3512.5</td>
<td>3507.9</td>
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</tr>
</tbody>
</table>

Significance level:  * * * : 0.1%  * * : 5%  * : 10%

Notes: $K$ number of components; $\gamma$, log-likelihood

$AIC = -2(\gamma) + d$

$BIC = -2(\gamma) + d \log(n)$

where $d$ is the number of parameters and $n$ is the sample size.

$p_{11} = p(S_{t} = 1|S_{t-1} = 1, z_{t}) = p(z_{t})$ and $p_{22} = p(S_{t} = 2|S_{t-1} = 2, z_{t}) = q(z_{t})$.

The first two columns displays results for the TF transition probabilities; the second two columns for the TVTP.
However, by looking at the BIC and AIC values, the model with two states is chosen in place of the model with three regimes. Table 2 displays results for the benchmark model (TF) and the TVTP model. In the TF specification, we find substantial differences between the two regimes, meaning that growth rate of African countries does not follow a unique path. Indeed, State 1 is characterized by a high degree of correlation between the growth rate and its value in the previous period, and by a low level of variability within the State. On the other hand, State 2 has a lower level of autocorrelation on the dependent variable and a high level of volatility within the regime. Lastly, the probability of a country in remaining in the same regime is quite high, meaning that both regimes have very high levels of persistence, whilst there is evidence about the different time length of the regimes. In particular, State 2 is found to last longer than State 1 (respectively, 16.83 time periods and 6.14 periods), and the probability of remaining in State 2 is higher than the one of remaining in State 1. Thus, Markov Switching with TF shows that African countries are most likely of following an unstable growth rate, characterized by picks both in negative and positive terms.

Table 2 displays also results for the model as it is formalized in Section 2. Similar conclusions with respect to the benchmark model could be drawn about the autocorrelation coefficients in the two states, whilst the $\beta_{St}$ is lower in the TVTP model than in the TF, particularly in the first regime. Moreover, the within state variability is observed to be almost the double with respect to the TF model. As it is formalized in Section 2, the model considered here allows the disturbance term $\epsilon_{it} \sim N(0, \sigma^2(St))$ to vary among groups. This implies the presence of a regime varying variance on the disturbance term, which accounts for the different output volatility occurring in the recession phases with respect to the one in expansion phases. As it is clear from Table 2, both regimes are characterized by high levels of variability which strongly suggests that growth rates in SSA tend to be triggered by different conditions. However, regime 2 is characterized by a higher level of variability, and by looking at the distribution of the observed growth rate in Regime 2, it is clear that countries belonging to this regime are more volatile in terms of growth experience. High output volatility could be associated with negative aspects of underdevelopment and empirical evidence points out that high volatility has negative effects on growth or is at least closely associated with lower growth. Causes of these high volatility in SSA can be broadly classified into two groups: those associated with higher exposure to exogenous shocks and augmenting factors, and those related to faulty policies and structural issues. Same conclusion could be drawn for the endogenous variables affecting the transitional probability matrix, with the exception of the exchange rate. Lastly, the probability of remaining in each regime is very high (almost 96%) meaning both regimes have very high levels of persistence. There is no evidence about the prevalence of one state to another. The posterior analysis of our data confirms that both groups are characterized by the same expected durability. A possible cause for the high persistence

---

10 The transition probability in the Hamilton (1989)’s specification are formally defined as $p_{11} = p(S_t = 1|S_{t-1} = 1) = p$ and $p_{22} = p(S_t = 2|S_{t-1} = 2) = q$.

11 Log Likelihood and the BIC value for the $M = 3$ are respectively equal to $-1711.1$ and $3695.3$, with 42 parameters to be estimated.
levels might be related to country characteristics such as education levels or political stability as well as shocks, particularly those due to terms of trade.

As a non-parametric approach, the goodness of fit is checked by graphical tools, as the empirical cumulative density function and the kernel distribution. As both Figure 2 and Figure 3 show, the Data Generating Process is well approximate by the Markov Switching Model with TVTP. It is worth noting that the higher the probability threshold used to compute the predicted value, the better the goodness of fit.

Figure 2: Fitting predicted values  
Figure 3: Empirical cumulative distribution function

3.3.1. REGIME CLASSIFICATION

As a by product of the model, two different groups of countries are found. As the empirical findings show, the two groups differ above all because of their variability. Indeed, countries belonging to State 1 are characterized by sustained growth rate, while the second group is characterized by highly volatile growth rates. This is also confirmed by the growth rate distribution. Indeed, it is noted that when country experience sudden changes in the growth rate, i.e. when there is a pick in the growth rate, the probability of belonging to State 2 is greater than 70% (e.g. by looking for example at the growth rate distribution of Lesotho, Malawi). Nevertheless, countries belonging to both states strongly depend on primary exports, political and economic instability, demographic changes (rapid population growth) and social conditions (ethnolingustic and religious diversity) which represent serious obstacle to growth. The main determinants of economic growth variability in both states are geographical factors. Indeed, climate, soil, topography and disease ecology makes African countries suffer from chronically low agricultural productivity, high disease burden and very low level of international trade.

As Table 2 displays, the duration of a highly volatile economy transiting to sustained growth is higher than the duration of an economy with sustained growth retaining its growth path (expected duration of the first state is 6.55 time period, against 8.07 in the second state). Thus, countries with highly volatile growth tend to experience longer periods of output collapse and they are likely to remain highly volatile due to higher exposure to exogenous shocks and faulty policies and structural issues. In other words,
African countries, in general, have a high degree of permanence in unstable regime. High volatility is observed to be a frequent occurrence in most economies in Africa as 26 of the 34 SSA economies had at least one switch - a ratio of 76.5%. As Byrne (2010) points out, one reason for this may be the reliance of most sub-Saharan African economies on primary commodity or extractive industries.

Table 3: Time varying Transition probability: estimates

<table>
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<tr>
<th></th>
<th>p1,t</th>
<th>p2,t</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>4.4883**</td>
<td>1.780</td>
</tr>
<tr>
<td>FDI</td>
<td>0.5326**</td>
<td>0.235</td>
</tr>
<tr>
<td>Trade</td>
<td>0.0880**</td>
<td>0.040</td>
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<tr>
<td>Pol. Regime</td>
<td>-1.5160*</td>
<td>0.811</td>
</tr>
<tr>
<td>ΔExch Rate</td>
<td>0.0098</td>
<td>0.006</td>
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Significance level: ** : 0.1%  * : 5%  : 10%
Notes: $p_{11} = p(S_t = 1|S_{t-1} = 1, z_t ) = p(z_t)$ and $p_{22} = p(S_t = 2|S_{t-1} = 2, z_t ) = q(z_t)$ where $z_t$ is the matrix containing the explanatory variables affecting the transition probability.

From Table 3 trade increases the probability of experiencing stable growth as well as FDI is found to encourage the probability of remaining in the stable regime. Political regime has a statistically significant impact on remaining in state 1, and its estimated coefficient is (as expected) negative. This implies that a change in the political regime from transitional to autocracy and from autocracy to democracy increases the probability for each country to maintain a sustainable growth rate. Indeed, as Hirschman (1958) emphasizes, with the absence of stable institutions, primary commodity and foreign owned extractive industries experience what he termed “enclave” type of development caused by the ability of primary products from mines, wells and plantations to slip out of a country without leaving much of a trace on economic growth. Also economies that transit from sustained growth to volatile growth are observed to have an increase in blackmarkets, racketeering and underground economy activities which deliberately underestimates GDP, creates shortages, leads to loss of revenue for governments and losses of legitimate industry thereby retard growth. Furthermore, by looking simultaneously at the evolution of the growth rate, the changes in the political regime and the regime change, it is clear that for countries experiencing frequent changes in the shift from one regime to another, there is a link between moving from dictatorship and political instability to democracy, and moving from State 2 to State 1. Interestingly, most economies which remain in state 1 are observed to autocratic regimes insinuating that Africa’s “home grown” democracy might not be the best political system for sustainable growth in Africa. Moreover, this is not always substantiated as countries with the longest duration of remaining in a state 1 are democratic countries. Countries belonging to State 1 have almost the same probability of experiencing autocracy as democracy. However, most of the democratic countries belong to Regime 1, i.e. 19% of the democratic countries of our sample belong to Regime 2. Additionally, countries characterized by an unstable regime, like civil war or transitional regime belong as posterior classification to State 2.
On the other hand, instability in the growth pattern could be due to appreciation of the exchange rate, disinvestment from foreign investors and a lower level of trade. Political regime has not a statistically significant impact on the transition from one State to another, thus shifting from democracy to autocracy or transitional regime and vice versa, do not affect the probability for a country to belong to move to the unstable growth rate group.

<table>
<thead>
<tr>
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<th>n. switching</th>
<th>switch to m=1</th>
<th>switch to m=2</th>
<th>n. obs in m=1</th>
<th>n. obs in m=2</th>
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<td>1</td>
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</table>

Total       | 82           | 44            | 38            | 318           | 294           |

As the Table 4 highlights, most of the African countries have experienced changes from high volatility to low volatility and vice versa. The only exception, i.e. countries that do not pass through phases of high volatility to phases of low volatility are Chad, Djibouti, Gambia, Ghana, Ivory Coast, Mauritius, Sierra Leone and South Africa.
Mauritius and South Africa have the distinction of being the only two African countries to have successfully transited to export-led growth in manufacturing and services due to their strong institutions. Economies with the longest duration (span) of remaining in state 1 include Botswana, Gambia, Ghana, Ivory Coast, Mauritius and South Africa. With the notable exception of Botswana, none of these economies spent any period of time in state 2, thus they are characterized by high persistence levels. Botswana has had the highest average economic growth rate in the world since independence, averaging 9% per year. However, its economy stagnated in early 2000 due to a fall in diamond price (its primary export), but later grew at 6-7% target in subsequent years. Interestingly, it is rated as Africa’s least corrupt nation by Transparency International. Gambia, Ivory Coast, Chad, Djibouti and Ghana have experienced sustained slow growth over time, and as a result have been able to avoid output volatility. Benin, Burundi, Congo, Guinea, Mozambique, Sudan and Tanzania which do not change their economic behaviour over time all belong to \( m = 1 \), i.e. the low volatile with the highest mean of growth rate in the group. A common feature among these countries is the existence of long term authoritarian regimes. Recent studies surprisingly show positive correlation between authoritarianism and sustainable economic growth in developing and emerging economies particularly in Asia with China, Singapore and Vietnam as prime examples. Lesotho, Senegal and Malawi experienced the highest number of transitions suggesting relatively quick recovery from shocks, while Botswana, Eq. Guinea, Mauritania and Zimbabwe experienced only high volatile growth rates within the period of observation. Economies with the longest duration in state 2 include Burundi, Chad, Ethiopia, Mauritania, Rwanda, Sudan, Burkina Faso and Niger. All aforementioned countries have been afflicted by civil wars and social unrest for the greater part of its history, and all countries are affected by their geographical location.

To conclude, the results show that though most Sub-Saharan countries have made significant breakthrough in economic growth in the past few decades, most countries find it difficult to maintain sustainable positive growth.

4. CONCLUSION

This paper applies a two state Markov Switching Model with time varying transition probability to 37 African countries over the period 1987–2011. We rely on the idea that the country’s growth path is the result of different growth regimes, that could occur without obvious changes in country-fundamentals. Thus, we study the change of growth rate and its determinants, by directly modelling the transition probability as dependent on a set of explanatory variables, such as trade, FDI, exchange rate variation and political regime. Our empirical results display the existence of two different growth regimes: a stable and an unstable growth regime. Furthermore, the probability of switching to the highly volatile regime negatively depends on exchange rate depreciation, trade and foreign direct investment, while democracy increases the probability of remaining in the stable growth regime.

Of course, a possible extension could be directly modelling the volatility of the growth rate in the estimation procedure. Indeed, even if the regime varying variance allows for accounting for different output volatility, understanding the output volatility determinants, formalizing them also as country-specific, could increase the possible policy implication.
derived from the model. Yet, other distributions, to account for the heavy tails growth rate distribution could be considered to implement the estimation procedure.

LITERATURE
4. Bilgili, F., Tuğçu N. S. H., and Dogan I. The determinants of FDI in Turkey:

ABSTRACT
This study documents the implications of financial vulnerability for export diversification in developing economies. Financial crises, by increasing the incidence of sunk costs of entry into exporting, reduce firm export dynamics. Financially-vulnerable exporters are not able to fully realize economies of scale in production and access better-sophisticated technologies. The number of products and destinations per exporter are therefore likely to decrease in times of crisis. We use a comprehensive cross-country dataset on export dynamics, with data covering 1997-2011 for 34 developing countries to investigate this issue. Building on the generalized difference-in-differences procedure proposed by Rajan & Zingales (1998) to remove any endogeneity bias, the results point to a negative and economically large effect of financial vulnerability on export diversification. Financial crises reduce export dynamics disproportionately more in financially dependent industries. This effect is less pronounced in countries with initially more open capital account, suggesting that portfolio inflows are good substitutes for underdeveloped domestic financial markets.

Keywords: Financial crises, Financial vulnerability, Export dynamics

JEL classification: F12, F14, G01, O16

1. INTRODUCTION
Diversification matters for economic development. To reduce vulnerability to external shocks, a country needs to build its capacity to reorient and redirect some of its exports towards new products and markets. The gains from trade diversification go beyond the benefits of specialization due to comparative advantage. By reducing price instability and output volatility, export diversification plays a central role in driving long-run growth and macroeconomic stability. Yet, developing countries have long been dependent on a narrow set of export products, despite some recent progress toward diversifying products and partners. Figure 1 shows that over the period 1997-2011, export concentration has been on average more than two times higher in developing countries than in advanced countries, although the gap has decreased in recent years.
Interestingly, however, this relatively low export diversification in developing countries suggests the existence of more room for upgrading the existing export basket. Also, export concentration is likely to be heterogeneous across both developing countries and geographical regions. Country-specific characteristics, circumstances, institutions and policies might have played a role in the process of structural transformation. In light of the implications of “sunk costs” for export participation discussed in the literature, one of the main drivers of this process is the vulnerability of firms to adverse financial shocks. Due to the existence of substantial sunk costs of entry into exporting (see, for instance, Roberts & Tybout, 1997; Bernard & Wagner, 2001; Melitz, 2003), only more productive firms or firms with a certain level of financial health are able to export. Furthermore, financial vulnerability has been identified as one of the major trade barriers (Manova, 2008; Berman & Héricourt, 2010; Minetti & Zhu, 2011; Chor & Manova, 2012) and the evidence suggests that the effect of credit rationing on exports is likely to be more pronounced in developing countries. The World Bank Enterprise Surveys country reports show that the percentage of firms identifying access to finance as a major constraint is typically higher in developing countries. At the macro level, compelling evidence supports the connection between financial development and export performance (Beck, 2002, 2003; Svaleryd & Vlachos, 2005; Manova, 2006, 2008; Becker & Greenberg, 2007). The idea is that countries with less developed financial sectors are likely to export goods not requiring external funding. Also, the empirical literature described how banking crises reduce export volumes but the underlying issue of the effect of crises on export diversification remains unresolved. In particular, it is still unclear whether the crisis effect of trade is the result of a reduced number of products, a reduced number of destination, or both. In addition, while there is a large literature on the implications of financial vulnerability for export-market participation, country samples have varied substantially across studies and very few papers have focused exclusively on developing countries.
Export diversification is measured here by the Herfindahl-Hirschman index. Notice that higher values of this index indicate lower diversification.

These country reports are available at http://www.enterprisesurveys.org/Reports.

This paper is, to the best of our knowledge, the first contribution to understand the extent to which financial vulnerability affects export dynamics. We focus on the developing world for three main reasons: (i) it experiences relatively highly-concentrated exports, (ii) it displays substantial heterogeneity across countries in export diversification, (iii) it is more likely to experience financial vulnerability than the advanced world. In part due to the lack of cross-country data on export diversification for developing countries, few studies have quantified the impact of financial vulnerability on export dynamics in these countries. This study also makes an important contribution to the literature by using a comprehensive cross-country database on exporter dynamics compiled at the industry level. The identification strategy follows the procedure introduced by Rajan & Zingales (1998) (henceforth RZ), which is well-known to be convenient in correcting for a potential endogeneity bias. The paper is concerned with the following specific questions: How do financial crises affect firm, product and destination dynamics? Do firms in industries with higher financial dependence suffer more? Does this effect vary across countries with different levels of capital account openness? The main result suggests that financial crises disproportionately increase export concentration in financially-vulnerable industries. Financial crises tend to reduce firm, product and destination entry rates, while increasing the corresponding exit rates. These effects are relatively more important in industries with higher financial dependence. Countries are also affected differently, with regard to the capital account openness. In the remainder of the paper, we present the identification strategy and the data used in Section 2. The results are discussed in Section 3, while Section 4 provides conclusions and implications for policymaking.

2. Empirical Strategy and Data

2.1. Baseline Estimating Equation

The central idea behind this study is that financial crises disproportionately hurt export concentration in industries that are more dependent on external financing. This is tested by estimating the following econometric specification:

\[ Export_{cpkt} = \text{FinVulk}_{k} \sum_{j=0}^{J} (\beta_1 \text{Crisis}_{c(t-j)} + \beta_2 \text{Crisis}_{c(t-j)} + \beta_3 \text{Crisis}_{c(t-j)}) + \alpha X_{ct} + d_{ct} + d_{cp} + d_{ck} + \varepsilon_{cpkt} \]

where \( Export_{cpkt} \) is the indicator of export diversification in country \( c \) for trading partner \( p \), in industry \( k \) during the year \( t \). \( \text{FinVulk}_{k} \) is the index of financial vulnerability that captures the degree of external financial dependence in industry \( k \). This index is the RZ index of external financial dependence. \( \text{Crisis}_{c(t-j)} \) is a dummy indicating whether a financial crisis happened in country \( c \) year \( t-j \). We include both the contemporaneous and lag crisis dummies to capture the average effect of a crisis on export diversification during its onset and in the following years. Three dimensions of financial crises are considered, namely banking, currency, and sovereign debt crises. Figure 2 provides the number of countries experiencing a financial crisis over time for our period of interest. \( X_{ct} \) is a set of conditioning information to control for other country-level factors influencing export diversification. This includes the Log of real GDP per capita and the Log of real exchange rate. The other potentially omitted macro factors will be captured through country-year and partner-year fixed effects (\( d_{ct} \) and \( d_{pt} \)).
We also used the Braun (2003) index of asset tangibility and the results are consistent with those that are presented.

We also include country-partner fixed effects to account for other gravity controls such as distance and common language. dck are country-industry fixed effects to control for industry-level unobserved heterogeneity across countries.

Figure 2: Number of Countries Experiencing a Financial Crisis (Starting Date)

Source: Laeven & Valencia (2013)

2.2. Identification
In estimating the baseline specification (Equation 1), the immediate concern is the endogeneity bias arising from reverse causality, omitted variables or measurement errors on the regressor variables. Although the omitted variable bias is importantly limited by the introduction of our set of fixed effects, reverse causality from exports to financial vulnerability remains a central concern. This issue is addressed by building on the generalized procedure proposed by Rajan & Zingales (1998). This approach has been largely used to estimate sectoral differential effects (see, for instance, Dell’ Ariccia et al., 2008; Manova, 2008; Chor & Manova, 2012). In practice, this method consists in using the financial dependence of U.S. firms on external financing as a proxy for the demand for external finance in developing countries. The main rationale is that any need for external finance in a steady-state equilibrium is the result of worldwide technical shocks. This amounts to saying that the demand for external financing of U.S. firms is therefore a good proxy for firms’ financial dependence in developing countries.

2.3. Data, Country sample, and sample period
The set of countries covered in this study is motivated by the consideration of focusing on countries with highly concentrated exports and less financially developed countries, which are mostly developing economies.
This is consistent with the argument of Do & Levchenko (2007), that is changes in trade patterns result in changes in demand for external financing, thus influencing developments in the financial sector. The sample consists of 34 developing countries, including 2 countries from the East Asia & the Pacific (EAP) region, 3 countries from the Europe & Central Asia region (ECA) region, 5 countries from the Middle East & North Africa (MENA) region, 2 countries from the South Asia (SA) region, and 12 countries from the Sub-Saharan Africa (SSA) region. Export diversification data, compiled at the HS 6-digit level of disaggregation, come from the Exporter Dynamics Database Cebeci et al. (2012). Export diversification is measured by three dimensions of export dynamics: (i) firm dynamics, (ii) product dynamics, and (iii) destination dynamics. For each dimension, we use both the entry/exit rates into/from export markets. Notice that when using destination entry and exit rates, one only have a country-industry-year dimension, since the destination dimension disappears.

To match these data with the financial vulnerability indicator, we aggregate them to the 3-digit ISIC industry level, using the Haveman’s concordance tables. The measure of financial vulnerability, available at the 3-digit ISIC industry level, is taken from Rajan & Zingales (1998). The other regressor variables such as the real GDP per capita and the real exchange rate come from the World Bank World Development Indicators (WDI). The regressions are run on annual data, for the period 1997-2011.

2.4. Financial vulnerability and export diversification: facts

The data suggest that export dynamics remain relatively weak in developing countries, though there is significant heterogeneity across countries. In these countries, the firm entry rate is 53%, as compared with 62% in developed countries (Table 1). At the same time, the firm exit rate is in developing countries (59%) is more than two times higher than that in advanced economies (21%). Similarly, the product entry rate is relatively higher in developed countries (31% vs. 27%) but they experience a relatively lower product exit rate (18% vs. 23%), as compared to the corresponding rates in the developing world. The same picture is observed with regard to destination dynamics, where the entry/exit rates are again relatively higher/lower in developed countries (44% vs. 25% and 23% vs. 38%) than in developing countries.

More interestingly, the standard deviation of firm, product, and destination entry and exit rates is always higher in the developing sample, suggesting a relatively higher heterogeneity. This could be due to the fact that developing countries are more represented in the sample (87% of the country sample is developing) but does not eliminate the reasons why focusing on the developing sample is interesting.
The list of countries is provided in the appendix.


Table 1: Summary statistics: Export diversification

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<td>Obs.</td>
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<td>p50</td>
<td>Std. Dev.</td>
<td>Minimum</td>
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<table>
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<td></td>
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Note: These summary statistics are based on sector-level data in the 3-digit ISIC industry classification.

Table 2: Export diversification and financial dependence

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<th>Minimum</th>
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<td>0.72</td>
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<td></td>
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<td>of the</td>
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<td>Firm exit rate</td>
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<td>Destination exit</td>
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<td>0.25</td>
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</table>

Note: These summary statistics are based on sector-level data in the 3-digit ISIC industry classification.

Furthermore, regarding the financial vulnerability issue, financial dependence tends to be a more important determinant of export dynamics in developing countries than in advanced countries mainly due to market failures. These main reasons led us to put our focus on the developing sample in the remaining empirical exercises. The correlation between external financial dependence and export dynamics can be described using the RZ index. On the one hand, industries at the top 50% of the distribution of financial...
dependence (industries more dependent on external finance) experience lower firm, product, and destination entry rates than industries at the bottom 50% of this distribution (Table 2). On the other hand, exit rates in financially dependent industries appear to be relatively more important than in other industries.

Alternatively, when we use the Braun (2003) index of asset tangibility, the data consistently show that the firm, product and destination entry rates are always relatively higher in industries with higher collateralizable assets. At the same time, industries with higher collateralizable assets observe relatively lower exit rates than industries with fewer collateralizable assets.  

*Figure 3: Financial dependence and export diversification over time*

The statistical link between the external financial dependence and export dynamics in developing countries is also evidenced for each year of our sample period (Figure 3). The average firm, product, and destination entry rates in industries at the bottom 50% of the distribution of financial dependence is always higher than that of industries at the top 50% of this distribution. As for the average firm, product, and destination exit rate, it appears however to be relatively higher in industries with higher financial dependence, with the exceptions of years 2000 and 2006.

These facts suggest a possible association between financial vulnerability and export dynamics in developing countries. In the remaining part of the paper, we further investigate the impact of financial crises on exporter dynamics.

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8To save space, these statistics are not presented here but are available upon request.
3. MAIN FINDINGS

In previous studies on the impact of financial crises on international trade, no attention has been paid to the extent to which crises affect exporter dynamics. In this section we investigate the effects of financial crises on the three following dimensions of export dynamics: (i) firm dynamics, (ii) product dynamics, and (iii) destination dynamics.

3.1. Financial crises and firm dynamics

Table 3 presents the estimates of the baseline specification, Equation 1, using firm entry and exit rates as dependent variables. The main variables of interest are the dummies of crisis in exporter and importer, their lags, and their corresponding interaction terms. Without controlling for the crisis interaction, the coefficient estimates on the contemporaneous and lagged crisis dummies in both exporter and importer have the anticipated signs and are statistically significant. The contemporaneous effect suggests that financial crises are associated with relatively higher declines in the firm entry rate in financially-dependent industries (columns 1 and 3). The magnitude of these coefficients is economically meaningful, indicating that the firm entry effects of crises in exporter and importer are -7.1 and -2.5 percentage points more pronounced for industries with higher financial dependence (column 1). These results point to a relative importance of the supply-side shock, compared to the demand-side shock. The results also confirm the presence of substantial sunk costs in export entry in times of financial crisis.\(^\text{10}\) Regarding the firm exit rate, the results on the contemporaneous crisis dummies show that experiencing a financial crisis in the partner country is associated with 10.6 percentage points relatively higher increase, for financially-dependent industries, in the rate at which firms exit the export market (column 3). The coefficient on the exporter crisis dummy is small and statistically indistinguishable from zero, reflecting a relative importance of demand shocks for the decision of firms to exit foreign markets. On the other hand, the average impact of supply-side shocks on the exit rate is relatively more important than that on the entry rate. When controlling for the interacting effect of crises, these effects remain significant with very similar magnitudes. The negative and significant coefficient on the crisis interaction in column 2 indicates that the supply-side shocks and demand-side shocks complement and reinforce each other in decreasing the firm entry rate when both countries are in crisis. But the exacerbating effect is statistically insignificant on the firm exit rate (column 4). These effects of crises on firm entry/exit into/from exporting are sizable given the cross-country variation of firm dynamics in the data (see Table 1). Regarding the lagged crisis dummies, their estimated effects have the expected signs as well. The results in column 1 show that the medium-run impact of crises on the firm entry is economically significant and disproportionately severe for financially-vulnerable industries. On average, the firm entry rate falls relatively higher in these industries by 7.8 and 11.3 percent in the 3 subsequent years after a financial crisis in the exporter and in the importer, respectively. Conversely, the firm exit rate raises relatively strongly in vulnerable industries by 9.3 and 6.8 percent in the medium-term, respectively for crisis in exporter and importer (column 3). The lagged crisis interaction also enters with the expected sign but its coefficient is only significant for the one-period lag. This is the sign that the exacerbating effect of crises on firm dynamics is not persistent over time. The results on the control variables are quite intuitive as well. Real GDP per capita for both exporting and importing countries enter positively and significantly in explaining the firm entry rate.

\(^{10}\)The sunk costs of entry into foreign markets include learning about foreign markets, administrative standards, and establishing distribution networks (e.g., Roberts & Tybout, 1997; Bernard & Wagner, 2001). These sunk costs are likely to be sensitive to firm financial conditions and are amplified during crises.
Their impact on the firm exit rate displays the right sign but is insignificant at any conventional level. An increase in the real exchange rate, which represents a real appreciation of the exporter currency vis-à-vis the importer, reduces the entry rate of exporting firms but fails to show any significant effect on their exit rate.

3.2. Financial crises and product dynamics

This section complements the previous one by focusing on the second dimension of export dynamics: the product entry/exit rates into/from export markets. Product dynamics is one of the aspects of the intensive margin of exports. Indeed, firms entry and exit do not tell us enough about the number new products exported. However, financial crises may affect product dynamics through the disruption effect and the income effect. The results from estimating Equation 1 using product entry and exit rates as dependent variables are presented in Table 4. As before, we first focus on the impact of crises on export dynamics while ignoring the crisis interaction (columns 1 and 3). As anticipated, financially vulnerable industries in crisis-hit countries tend to experience lower levels of bilaterally exported and imported products, reflecting the balance-sheet problems increased fixed costs of exporting a new product—in the wake of financial crises. The contemporaneous estimated effects of financial crises on the product entry rate are statistically and economically significant (column 1). In times of crisis, firms tend to delay exporting new products or abandon exporting some existing products owing to the limited access to working capital and reduced foreign demand. Other things being equal, financial crises are associated with 2 and 9.5 percentage points more pronounced collapses of the product entry rate in financially-vulnerable industries, respectively for crises in exporter and importer. In addition, the coefficients in column 3 indicate that the product exit rate raises disproportionately higher by 13.3 percent in financially-dependent industries during financial crises in the exporting country. The coefficient on the contemporaneous effect of crises on the product exit rate is positive but statistically insignificant, suggesting that demand shocks matter more than supply shocks for product exits. This is consistent with the results presented in Table 3 and signals that the disruption of trade credit at the height of a crisis in the exporting country introduces important sunk costs of entry of new products without necessarily causing the exit of existing products. Once again, the estimated coefficients on the lagged crisis dummies indicate the gradual nature of the product dynamics adjustment. Nearly 50 percent (0.036/0.072) and 80 percent (0.097/0.119) of the effect of a financial crisis would remain three years after the event, respectively when the crisis occurs in the exporting and importing country. Financial crises in both exporter and importer countries are associated with relatively higher declines of the product entry rate and increases of the product exit rate in vulnerable industries. On average, the number of new exported products as a percentage of all products exported falls relatively higher in vulnerable industries by 7.2 and 11.9 percent over three years following the onset of the crisis, respectively for a crisis in the exporter and importer countries. By contrast, a financial crisis in the importing country leads to 9.3 percentage points relatively higher increase of the product exit rate over the three following years in financially-dependent industries. The crisis in the exporting country positively affects the product exit rate but its effect is statistically insignificant. As regards the estimated coefficients on the crisis interaction terms, it is apparent that the impact of financial crises on product dynamics is amplified when both exporter and importer countries are in crisis. However, this exacerbating effect becomes statistically insignificant two years after the crisis. As before, controlling for this interaction does not alter our main results on the detrimental impact of crises on product dynamics in financially-vulnerable sectors. Regarding the conditioning information, higher levels of real GDP per capita of both exporter and importer raise the product entry rate and reduce its exit rate. An increase in the bilateral real exchange rate is associated with lower
levels of product entry rate but its effect on the product exit rate is statistically insignificant. 

**Table 3.** – Financial Crises and Firm Dynamics

<table>
<thead>
<tr>
<th>Dependent variable</th>
<th>(1) Firm entry rate of incumbents</th>
<th>(2) Firm exit rate of incumbents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crisis in exporter</td>
<td>-0.071*** (0.025)</td>
<td>0.010 (0.012)</td>
</tr>
<tr>
<td>Crisis in importer</td>
<td>-0.025*** (0.007)</td>
<td>0.106*** (0.046)</td>
</tr>
<tr>
<td>Crisis interaction</td>
<td>-0.283** (0.128)</td>
<td>0.452 (0.483)</td>
</tr>
<tr>
<td>Crisis in exporter (t-1)</td>
<td>-0.118*** (0.040)</td>
<td>0.039* (0.022)</td>
</tr>
<tr>
<td>Crisis in importer (t-1)</td>
<td>-0.024*** (0.008)</td>
<td>0.093*** (0.027)</td>
</tr>
<tr>
<td>Crisis interaction (t-1)</td>
<td>-0.092** (0.004)</td>
<td>0.151*** (0.019)</td>
</tr>
<tr>
<td>Crisis in exporter (t-2)</td>
<td>-0.183*** (0.060)</td>
<td>0.085** (0.036)</td>
</tr>
<tr>
<td>Crisis in importer (t-2)</td>
<td>-0.009** (0.004)</td>
<td>0.040*** (0.013)</td>
</tr>
<tr>
<td>Crisis interaction (t-2)</td>
<td>-0.016 (0.050)</td>
<td>0.191 (0.216)</td>
</tr>
<tr>
<td>Crisis in exporter (t-3)</td>
<td>-0.129*** (0.044)</td>
<td>0.082** (0.035)</td>
</tr>
<tr>
<td>Crisis in importer (t-3)</td>
<td>-0.002* (0.001)</td>
<td>0.051*** (0.015)</td>
</tr>
<tr>
<td>Crisis interaction (t-3)</td>
<td>-0.000 (0.004)</td>
<td>0.019 (0.030)</td>
</tr>
<tr>
<td>Log exporter’s real GDP PC</td>
<td>0.260*** (0.089)</td>
<td>-0.154 (0.167)</td>
</tr>
<tr>
<td>Log importer’s real GDP PC</td>
<td>0.319*** (0.106)</td>
<td>-0.189 (0.195)</td>
</tr>
<tr>
<td>Log real exchange rate</td>
<td>-0.015* (0.008)</td>
<td>0.003 (0.010)</td>
</tr>
<tr>
<td>Average supply shock</td>
<td>-0.078** (0.033)</td>
<td>0.093*** (0.027)</td>
</tr>
<tr>
<td>Average demand shock</td>
<td>-0.113** (0.049)</td>
<td>0.068*** (0.021)</td>
</tr>
<tr>
<td>Observations</td>
<td>27981</td>
<td>27981</td>
</tr>
<tr>
<td>R-squared</td>
<td>0.808</td>
<td>0.871</td>
</tr>
</tbody>
</table>

Note: The dependent variable is the rate of export entry or exit of firms by country–destination. The regressions include
### Table 4. – Crises and Product Dynamics

<table>
<thead>
<tr>
<th>Dependent variable</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product entry rate of incumbents</td>
<td>0.020** (0.010)</td>
<td>-0.020** (0.009)</td>
<td>0.184 (0.205)</td>
<td>0.182 (0.206)</td>
</tr>
<tr>
<td>Product exit rate of incumbents</td>
<td>0.095*** (0.032)</td>
<td>-0.086* (0.028)</td>
<td>0.133** (0.060)</td>
<td>0.129** (0.057)</td>
</tr>
<tr>
<td>Crisis interaction</td>
<td>-0.101* (0.059)</td>
<td>0.002** (0.000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Crisis in exporter (t-1)</td>
<td>-0.145** (0.045)</td>
<td>-0.146** (0.048)</td>
<td>0.204 (0.213)</td>
<td>0.204 (0.194)</td>
</tr>
<tr>
<td>Crisis in importer (t-1)</td>
<td>-0.171*** (0.050)</td>
<td>-0.170*** (0.051)</td>
<td>0.237*** (0.065)</td>
<td>0.228*** (0.073)</td>
</tr>
<tr>
<td>Crisis interaction (t-1)</td>
<td>-0.128** (0.058)</td>
<td>0.032* (0.018)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Crisis in exporter (t-2)</td>
<td>-0.088*** (0.029)</td>
<td>-0.083*** (0.026)</td>
<td>0.107 (0.148)</td>
<td>0.105 (0.146)</td>
</tr>
<tr>
<td>Crisis in importer (t-2)</td>
<td>-0.115* (0.066)</td>
<td>0.098* (0.056)</td>
<td>0.125*** (0.043)</td>
<td>0.125*** (0.039)</td>
</tr>
<tr>
<td>Crisis interaction (t-2)</td>
<td>-0.041 (0.052)</td>
<td>0.219 (0.287)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Crisis in exporter (t-3)</td>
<td>-0.036** (0.017)</td>
<td>-0.037** (0.017)</td>
<td>0.060 (0.075)</td>
<td>0.068 (0.078)</td>
</tr>
<tr>
<td>Crisis in importer (t-3)</td>
<td>-0.097* (0.056)</td>
<td>-0.094* (0.056)</td>
<td>0.103*** (0.035)</td>
<td>0.101*** (0.033)</td>
</tr>
<tr>
<td>Crisis interaction (t-3)</td>
<td>-0.003 (0.003)</td>
<td>0.144 (0.205)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Log exporter’s GDP PC</td>
<td>0.448*** (0.131)</td>
<td>0.439*** (0.133)</td>
<td>-0.099*** (0.033)</td>
<td>-0.092*** (0.030)</td>
</tr>
<tr>
<td>Log importer’s GDP PC</td>
<td>0.281*** (0.080)</td>
<td>0.280*** (0.087)</td>
<td>-0.108** (0.049)</td>
<td>-0.108** (0.048)</td>
</tr>
<tr>
<td>Log real exchange rate</td>
<td>-0.017 (0.038)</td>
<td>-0.023* (0.013)</td>
<td>0.062 (0.116)</td>
<td>0.063 (0.129)</td>
</tr>
<tr>
<td>Average supply shock</td>
<td>-0.072*** (0.033)</td>
<td>-0.102* (0.059)</td>
<td>0.068 (0.071)</td>
<td>0.016 (0.033)</td>
</tr>
<tr>
<td>Average demand shock</td>
<td>-0.119*** (0.049)</td>
<td>-0.044 (0.107)</td>
<td>0.093*** (0.027)</td>
<td>0.028 (0.035)</td>
</tr>
</tbody>
</table>

Observations: 21006 21006 20989 20989
R-squared: 0.740 0.752 0.717 0.719

Note: The dependent variable is the rate of export entry or exit of firms by country–destination. The regressions include...
3.3. Financial crises and destination dynamics

In this section our interest is on the impact of financial crises on the extensive margin of exports to a given destination. The destination entry and exit rates are alternatively used as the indicators of destination dynamics. One advantage of considering destination dynamics is that independently from firm and product dynamics, the disruption effect could matter for the decision to exit a destination or to export to a new destination, as suggested by Muuls (2008). Since the interest is in the number destinations, we estimate a modified version of Equation 1 in the full panel of the measures of destination dynamics for the 34 countries used in subsections 3.1 and 3.2 over the 1997-2011 period.

\[ \text{Export}_{ct} = aX_{ct} + \beta \text{FinVulkCrisis}_{t,j} + \delta_t + \delta_k + \varepsilon_{ckt} \quad (2) \]

The regression results in Table 5 show that financially-dependent industries in crisis-hit countries experience lower levels of participation to new export destinations. The estimated coefficients on the crisis dummies are all negative in the destination entry rate equation, reflecting the detrimental nature of financial crises for the entry of exporting firms in new markets (columns 1 and 2). A contemporaneous crisis leads to a relatively lower destination entry rate, by 4.9 percent in vulnerable industries, confirming that financial crises are associated with increased sunk costs of exporting. This negative impact is persistently significant four years after the crisis. Additionally, during financial crises, the destination exit is disproportionately raised by 0.5 percent in financially-vulnerable industries but this effect becomes statistically insignificant in the years following the event.

Given that we are no longer on a bilateral specification we control for relative GDP per capita. This is the deviation of the country’s real GDP per capita from the average level of its trading partner. The coefficients of 0.149 on this variable implies that, other things being equal, a country whose GDP per capita is twice the average GDP of its trading partners will have a destination entry rate that is 29.8 percentage points higher than that of the trading partners, on average (Column 1). Consistently with this result, the coefficient on the relative GDP PC in column 3 indicates that an increase in relative GDP reduces the destination exit rate of incumbents. Furthermore, a real appreciation is associated with lower destination entry rate and higher destination exit rate but the latter effect is not statistically significant.

We further investigate the variation of the magnitude of the crisis effect across countries by splitting our sample between countries with higher and lower financial account openness.
Table 5: Crises and destination dynamics

<table>
<thead>
<tr>
<th>Dependent variable</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Destination entry rate</td>
<td>Destination exit rate</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Crisis</td>
<td>-0.044***</td>
<td>-0.049***</td>
<td>0.005**</td>
<td>0.004**</td>
</tr>
<tr>
<td></td>
<td>(0.012)</td>
<td>(0.014)</td>
<td>(0.002)</td>
<td>(0.001)</td>
</tr>
<tr>
<td>Crises (t-1)</td>
<td>-0.102***</td>
<td>-0.094*</td>
<td>0.014</td>
<td>0.014</td>
</tr>
<tr>
<td></td>
<td>(0.036)</td>
<td>(0.026)</td>
<td>(0.094)</td>
<td>(0.083)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.271)</td>
<td></td>
</tr>
<tr>
<td>Crises (t-2)</td>
<td>-0.015</td>
<td>-0.014</td>
<td>0.028</td>
<td>0.034</td>
</tr>
<tr>
<td></td>
<td>(0.063)</td>
<td>(0.061)</td>
<td>(0.077)</td>
<td>(0.061)</td>
</tr>
<tr>
<td>Crises (t-3)</td>
<td>-0.080***</td>
<td>-0.083***</td>
<td>0.009</td>
<td>0.011</td>
</tr>
<tr>
<td></td>
<td>(0.023)</td>
<td>(0.025)</td>
<td>(0.037)</td>
<td>(0.022)</td>
</tr>
<tr>
<td>Crises (t-4)</td>
<td>-0.041**</td>
<td>-0.044**</td>
<td>0.085***</td>
<td>0.079***</td>
</tr>
<tr>
<td></td>
<td>(0.018)</td>
<td>(0.019)</td>
<td>(0.028)</td>
<td>(0.020)</td>
</tr>
<tr>
<td>Relative GDP PC</td>
<td>0.149*</td>
<td>0.136*</td>
<td>-0.018**</td>
<td>-0.012*</td>
</tr>
<tr>
<td></td>
<td>(0.087)</td>
<td>(0.079)</td>
<td>(0.007)</td>
<td>(0.006)</td>
</tr>
<tr>
<td>Log REER</td>
<td>-0.133**</td>
<td>-0.133**</td>
<td>0.099*</td>
<td>0.087</td>
</tr>
<tr>
<td></td>
<td>(0.060)</td>
<td>(0.061)</td>
<td>(0.056)</td>
<td>(0.089)</td>
</tr>
<tr>
<td>Average supply shock</td>
<td>-0.078**</td>
<td>-0.102*</td>
<td>0.093***</td>
<td>0.016</td>
</tr>
<tr>
<td></td>
<td>(0.033)</td>
<td>(0.059)</td>
<td>(0.027)</td>
<td>(0.033)</td>
</tr>
<tr>
<td>Average demand shock</td>
<td>-0.113**</td>
<td>-0.044</td>
<td>0.068***</td>
<td>0.028</td>
</tr>
<tr>
<td></td>
<td>(0.049)</td>
<td>(0.107)</td>
<td>(0.021)</td>
<td>(0.035)</td>
</tr>
<tr>
<td>Observations</td>
<td>17126</td>
<td>17126</td>
<td>17004</td>
<td>17004</td>
</tr>
<tr>
<td>R-squared</td>
<td>0.783</td>
<td>0.792</td>
<td>0.749</td>
<td>0.765</td>
</tr>
</tbody>
</table>

Note: The dependent variable is the entry or exit rate of products in exports by country and product category (HS-3 digit). REER stands for Real Effective Exchange Rate. The regressions include year and exporter-importer fixed effects. Heteroskedasticity-robust standard errors are reported in parentheses. ***, **, and * denote significance at the 1-percent, 5-percent, and 10-percent levels, respectively. Here the crisis interaction is defined to take 1 if the country is simultaneously in crisis with at least one of its five top trading-partners. The relative GDP PC is the deviation of the country’s real GDP per capita from its trading-partner average. All the crisis-related dummies are interacted with the sector-level financial dependence index.
The first group includes countries at the top 50% of the distribution of financial openness, averaged over the 1997-2008 period,\(^{11}\) whereas the second group includes the bottom 50% of the distribution. Financial openness is measured by the Chinn & Ito (2008) index of capital account openness.\(^{12}\) The results show that exporters are relatively more resilient to both supply-side and demand-side shocks in countries with higher financial openness (Tables 4.6 and 4.7 in the appendix).\(^{13}\) Also, the supply-side effect is always insignificant for the sample of countries with higher financial account openness (Tables 4.6). By contrast, this effect is large and statistically significant for the sample of lower financial openness, though insignificant on the destination exit rate (Tables 4.6). As regard the demand-side effect, it is significant in the case of more financially-open countries only for the entry rates. It has no significant effect on the exit rates in these countries. On average, this negative impact of crises in partner countries on the firm entry rate, for which both coefficients are significant and therefor comparable, is more than five times higher in countries with lower financial openness. Similarly, the interacting effect is always lower and statistically insignificant in countries with higher financial openness.

These regression results contribute to reconcile the two existing views in the literature. The debate on the relative importance of supply-side shocks versus demand-side shocks is now better understood through this decomposition of the impact of crises on the three dimensions of export dynamics. The results on the product and destination dynamics reveal the importance of both supply-side and demand-side shocks for export diversification.

4. CONCLUSION

Export diversification, as a core element of countries structural transformation, is now a priority on the policymakers’ agenda. This study mainly revealed that financial vulnerability is negatively related to export diversification. Financial crises reduce export firm, product, and destination entry rates and increase the corresponding exit rates disproportionately more in financially-vulnerable industries. This detrimental effect is less pronounced in countries with initially more open capital account.

These empirical results have important policy implications in developing countries in promoting export diversification. Reducing the dependence of firms to external financing may be a key for strengthening export dynamics and diversification, since this would result in increase entry rates into exporting and a reduced exit rates. Alternatively, measures to facilitate portfolio flows may be a second best option, given that increased capital inflows is found to be a good substitutes for domestic funding.

\(^{11}\)2008 is the last year for which the data on financial openness are available.
\(^{12}\) See the list of countries in the appendix.
\(^{13}\) We report only the coefficients on our variables of interest to save space.
LITERATURE
INDUSTRIAL POLICY AND REINDUSTRIALISATION IN TRANSITION ECONOMIES

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ABSTRACT

Recent economic crises have changed mainstream economics a great deal regarding its view on industrial policy. Deindustrialisation was considered to be a normal path of economic development, and industrial policy was viewed with suspicion due to its theoretical incompatibility with free markets. Today industrial policy is on every country’s agenda as a way of achieving economic growth. In line with that, serious questions are being raised about the desirability of the level of reindustrialisation modern economies are currently experiencing. This topic is even more important for transition economies in which deindustrialisation occurred at significantly lower levels of GDP. The aim of this paper is to analyse the existing literature on deindustrialisation of developed countries in order to ascertain the main determinants of that process. Based on that, we will try to give recommendations for industrial policies in transition countries.

Keywords: deindustrialisation, industrial policy, literature review, reindustrialisation, transition countries

1. INTRODUCTION

History shows that along with economic development the share of industry employment first grows while the agricultural share falls. The industry share continues to rise up to a certain point after which it stabilises and then starts to fall; at the same time the share of services in total employment increases. The first phase is called industrialisation, the second deindustrialisation. Likewise, the definition could be expressed through the sector share of GDP. Defined as the relative decrease of industry measured as the share of industrial employment in total employment, or the share of industry in GDP, deindustrialisation is in the literature considered to be a natural course of economic development. This opinion prevails because most of the studies conducted are based on data for developed countries. However, the data also provides a clear picture of deindustrialisation in transition countries.32 But, this process in transition countries begins at much lower levels of per capita income. It is believed that industry is still an important factor of economic growth, although it ceases to be an activity that employs the most workers, as new technologies replace human labour. Therefore, especially after the economic crisis in 2008, countries are considering an array of different measures geared toward encouraging industrial growth. These measures together can be seen as constituting the industrial policy of a country.

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32 In this paper we consider only the European transition economies classified according to the IMF (2000) and they are: Albania, Armenia, Azerbaijan, Belarus, Bulgaria, Croatia, Czech Republic, Estonia, Georgia, Hungary, Kazakhstan, Kyrgyz Republic, Latvia, Lithuania, Moldova, Poland, Republic of Macedonia, Romania, Russia, Slovak Republic, Slovenia and Ukraine.
However, after the collapse of the SSSR and Yugoslavia, transition countries denied any state involvement in the economy, including any form of industrial policy. This has led to a system where many industries closed and only one or two dominant industries survived. The recent economic crises again stressed the importance of industry to transition economies. Consequently they started to reconsider their industrial policies thus announcing the desirability of reindustrialisation.

The paper is structured as follows. After the introduction, a descriptive analysis of the data is carried out on value added and employment by industry for OECD (developed) and transition economies. The analysis shows that deindustrialisation in transition countries started at lower levels of GDP per capita. In addition we conduct a search for similarities between the processes of industrialisation and deindustrialisation. Based on the analysis of the causes of the deindustrialisation and on the most important results of relevant studies, we attempt to gain a more comprehensive view of this issue. The sequent chapter examines the main objectives of the “new” industrial strategy of the European Union33 and its implications for the industrial policies of transition economies.

2. MAIN FEATURES OF INDUSTRY DEVELOPMENT – GDP AND EMPLOYMENT STRUCTURE

With GDP per capita growth, the share of agriculture (in GDP and employment) decreases, while the share of industry increases (industrialisation). After a certain level of GDP per capita the share of industry in GDP and employment gradually declines (deindustrialisation) while the tertiary sector constantly grows. Most developed countries have reached this turnover point in the 1970s when the era of deindustrialisation started.

If we take the economy structure of developed countries as a role model, than the deviations from that structure experienced by transition economies may be considered unsatisfactory. Figure 1 provides information on sector shares of employment and value added in 2012 with respect to the level of GDP per capita. As can be seen, the value added and employment share of agriculture in OECD countries declines as GDP per capita grows, and the value added and employment share of services grows. However, while the value added of industry in OECD countries remains relatively stable as GDP grows, the employment share rapidly declines. Based on this we can conclude that deindustrialisation in terms of employment is more obvious than in terms of value added. Therefore most of the studies define deindustrialisation as a process which decreases the employment share of industry in total employment.

If we take into account the period when deindustrialisation started in developed and transition economies, transition economies exhibited lower levels of GDP per capita, and a higher share of agriculture in GDP than OECD countries. On Figure 1 we can also see that in the period when deindustrialisation started in developed and transition economies, transition economies exhibited lower levels of GDP per capita, and a higher share of agriculture in GDP than OECD countries. When the “normal” path of development indicates that the relative importance of industry should increase, the data shows that the industry share in value added in transition countries is about average and the employment share is lower than the average in OECD countries. As this cannot be explained by a sudden and dramatic productivity increase we can conclude that the process of deindustrialisation in transition economies was considerably stronger. The pattern is maintained when we look at the service sector, where GDP and employment shares were lower than the OECD average.

33 The EU is the subject of analysis when it comes to industrial policy, because European transition countries follow their policies.
Furthermore, we can clearly see that on GDP per capita levels transition economies achieved when deindustrialisation began, OECD countries were not deindustrialising (see Boulhol & Fontagné, 2006 or Dasgupta & Singh, 2006). From this we can conclude that the industry share in transition economies in this period should have continued growing, not falling. Therefore, transition countries were going through a premature deindustrialisation.

3. INDUSTRIALISATION AND DEINDUSTRIALISATION – ARE THERE SIMILARITIES?

Industry is considered one of the most important factors of economic growth. This status is obtained primarily because of a spill-over effect (multiplier effect) of manufacturing to other sectors. Lichtblau, et al. (2013) exploration of industry as the engine of growth illustrates the relevance of industry in various economic dimensions. But, this statement was not considered universally true. At first, industry did play a major role in growth and development – during the process of industrialisation. Later, the process of deindustrialisation took its place, and industry began to lose its high standing in the growth literature. Simultaneously neoliberal economics as a predominant economic school ruled out state intervention.

In order to assess this issue we will first take a look at the process of industrialisation and then deindustrialisation. As an opening remark, we may observe that industrialisation did not follow the same path in every country. Industrialisation in developed countries began with the development of light industry, while in the case of the former socialist countries it started with the development of heavy industry. Likewise, the industrialisation of today's developed countries began earlier and lasted longer than the industrialisation of transition countries (that were characterised by late and fast industrialisation). It is generally understood that the industrialisation took its “natural” course with England as the first industrialised country. Transition economies on the other hand experienced rapid industrialisation with the aim of achieving developed countries after 1945. That industrialisation was mainly state-controlled and focused on expansion of heavy industry whereas development of other industries was almost completely ignored. As for deindustrialisation, it was shown in the previous chapter that it was premature. Therefore, its positive effects are often rightly suspected.

So, the question arises if there are similarities between the process of industrialisation and the process of deindustrialisation regarding its starting position and speed. Another question that arises from this is even more important – can these groups of countries use the same set of industrial policies in order to reindustrialise? If the models of industrialisation, as well as deindustrialisation differ, then it would be reasonable to assume that models of reindustrialisation cannot be the same.

In this context, it is questionable whether the still popular policies of liberalisation, deregulation and privatisation encourage or hinder the growth of developing (including many transition) countries. Shafaeddin (1998) in his analysis confirms the misconception that early industrialised countries developed their industrial sectors without protection of new industries and without government intervention. In fact, all countries that have industrialised in the first three waves of industrialisation, including East Asian countries, have relied on the protection of infant industries. And exactly this is nowadays forbidden to the countries at lower levels of income. This may be one of the reasons transition countries have weak industries. In order to ascertain the truth of this issue we will take a closer look at the determinants of deindustrialisation, taking into account both theory and empirical research.
Figure 1: Employment share and value added by sectors in 2012 (World Bank data)

Notes: 1) Blue rhomb indicates OECD countries, and red square indicates European transition countries (according to IMF classification)
2) Czech Republic, Estonia, Hungary, Poland, Slovak Republic and Slovenia are taken as OECD countries and not transition
3) Due to missing data, some data are taken from earlier years (e.g. 2010 or 2011)
3.1. The main causes of deindustrialisation

The reverse-U relationship between the share of industry in total employment and per capita income was confirmed by numerous empirical studies (Rowthorn & Wells, 1987, Alderson, 1999, Rowthorn & Ramaswamy, 1999, Mickiewicz & Zalewska, 2001, Oh, 2001, Mickiewicz & Zalewska, 2002, Rowthorn & Coutts, 2004, Palma, 2007, Kang & Lee, 2011, Rowthorn & Coutts, 2013). However, most of these studies were conducted for developed countries. But, countries on a lower stage of economic development also pass through a similar process and it occurs on lower levels of their per capita income. In the earlier studies the threshold was estimated at $ 10000 per capita at current prices, while current estimates suggest that this threshold reduced significantly, to the extent of $ 3000 per capita in some countries (Dasgupta & Singh, 2006, p. 5).

In the literature, the most frequently cited causes of deindustrialisation are the following:

(1) Classification – along with the development of industry, numerous activities such as design, import, transport, distribution, cleaning, insurance, data processing etc., which used to be part of the firm’s production process, are today performed by specialised providers of certain services (the shift from factories to offices). Correspondingly, a reclassification of activities from “industry” to “services” occurred. Thus the employment share in industry decreased substantially due to changes in statistical coverage of certain activities (Rowthorn & Coutts, 2013, p. 7);

(2) Changes in consumption patterns / changes in the income elasticity (structure) of demand – these changes are classified among the most important causes of deindustrialisation. In developing countries income elasticity of demand is very high while in developed countries it is low, which explains the initial rise and consequent fall in the share of industry in GDP. The reasons behind spending a smaller proportion of income on industrial goods despite its growing demand are plentiful, but the most important is the decline of their relative prices;

(3) Differences in labour productivity – the labour productivity growth rate is by definition equal to the difference between industry and employment growth rates. Thus, if two sectors grow at the same rate, the sector with higher labour productivity will have slower employment growth. Statistics show that, on average, over the past 40 years real output in industry rose at the same rate as real output in the service sector. At the same time, labour productivity growth was much faster in the industrial sector, i.e., the share of employment in industry declined (Dasgupta & Singh, 2006, p. 5). Thus, labour productivity growth is the cause of relatively less employment in the industrial sector;

(4) International trade – affects the structure of employment in several ways but the most important channel is through productivity and specialization. By stimulating competition and thus encouraging domestic firms to produce more efficiently, international trade can increase industrial productivity. This will eliminate low value added and/or inefficient firms by substituting their products with imported ones. The result is a process in which developed countries specialize in industries with high value added, while low-income countries specialize in industries with low value added products. Since the first are capital intensive and the second labour intensive, the net result is a decrease in the share of industrial employment in developed countries (Boulhol & Fontagné, 2006, p. 10);

(5) Investments – domestic investments act contrary to previous determinants, i.e. they slow down the process of deindustrialisation. A higher rate of investment may increase the relative demand for industrial products and thus increase the relative importance of the industrial sector (via a higher share of industry in GDP and employment). However, in the case of foreign direct investment (FDI), their outflow will reduce the demand for labour in the domestic industrial sector, leading to a reduction in industrial employment. Likewise, FDI
outflow can reduce the investment rate in the domestic industrial sector, which acts as a crowding out effect and accelerates deindustrialisation.

If we classify all causes of deindustrialisation in two groups – internal and external, empirical evidence shows that proponents of the internal factors have the majority (see e.g. Iversen & Cusack, 2000).

3.2. Literature overview on the deindustrialisation process

The debut study on deindustrialisation was conducted by Clark (1957), but Blackaby (1978) made the first systematization of all the research on this subject. Rowthorn & Wells in 1987 construct a basic model of deindustrialisation. According to the authors, the long-term structural changes are induced by two (internal) factors: productivity growth at different rates across sectors (the lowest in the service sector) and differences in the income elasticity of demand. These two factors are considered to be sufficient to explain the long-term dynamic structural development which results first in the phase of industrialisation (growth both of industry and services share at the expense of the share of agriculture in total employment), and then in the phase of deindustrialisation (growth of the share of employment in services at the expense of the share of industry). Therefore the main driving force of structural change is the rate of change in productivity - its growth leads to growth in per capita income which in turn affects the structure of demand. Increased demand then leads to the development of new sectors, or more specifically, the service sector.

In their later studies Rowthorn and Ramaswamy (1997a & 1997b) even more fervently advocate the thesis that deindustrialisation is primarily a characteristic of successful economic development caused by internal factors, and that trade between developed and developing countries is not a variable of great significance when explaining deindustrialisation. Their panel data analysis shows that productivity growth is responsible for more than 60% of the decline in the share of industrial employment in industrialised countries. Their estimate is updated and expanded by Rowthorn & Coutts (2004), who conclude that the most important causes of deindustrialisation are internal, such as productivity growth and changes in consumption patterns, while trade with low-income countries also showed as a significant factor.

Along with these studies that consider internal causes as the main determinants of deindustrialisation, there are authors who advocate the opinion that deindustrialisation is primarily a result of external factors. For example, Sachs & Shatz (1994) empirically show that the increasing volume of international trade is the most important reason of deindustrialisation in the United States. Analysing the relationship between employment in industry and imports from developing countries, Wood (1995) shows that an increase in the volume of trade can cause a great drop in industry in OECD countries. He explains this by the fact that industrial products imported from developing countries are labour intensive, which leads to a displacement of low-skilled workers in developed countries. At the same time, with the growth of GDP per capita, the demand for services grows, so the employment rate in this sector increases. A similar study conducted by Saeger (1997) explores the causes of deindustrialisation in OECD countries. He finds that trade with developing countries is a statistically significant predictor of employment and real income in the industrial sector. His results also suggest that trade among OECD countries cannot be considered the main cause of deindustrialisation (Saeger, 1997, p. 580).

Lawrence (1983, p. 157) concludes that about a third of the fall in employment in industry in the US is caused by trade. He believes that despite numerous closures in the 1970s most of the lost jobs were cyclical in nature and thus have no long-term significance.
Unlike Lawrence (1983), Bluestone (1984) concluded that deindustrialisation in the United States occurred in spite of the fact that industrial employment remained constant in the 70s, and it manifests itself in substantial job losses in key base industries and regions. Eventually, models have expanded with the aim of identifying additional external effects on deindustrialisation. In particular, attempts have been made to explore the impact of globalization on deindustrialisation. The first such study was published by Alderson (1999). He studies the relationship between globalization (FDI and trade with developing countries) and deindustrialisation in developed industrial countries (18 OECD countries for period 1968-1992). The results showed that FDI 1) reduces industrial employment, 2) may increase the required marginal rate of return on domestic investment 3) shifts investment from industry to the service sector and 4) reorients investment from real investment toward purely financial investments. He also concludes that trade in industrial goods caused a reduction in the industrial employment’s share in developed countries, which suggests that imports from developing countries played a significant role in the process of deindustrialisation of developed countries and that the pattern of international trade is an important determinant of deindustrialisation (Alderson, 1999, p. 717).

Recent researches on deindustrialisation try to decompose factors of deindustrialisation. Tregenna’s (2009, 2011) results indicate that in most cases the decline in industrial employment is associated primarily with lowering labour intensity in the industry, and not with the overall decline in output of the industrial sector or in the fall of its share in GDP. Accordingly, the author considers that deindustrialisation should not be defined only in terms of the share of employment in the industry, but also in terms of the share of industry in GDP (Tregenna, 2011, p. 16). The data shows that if this is the case, some countries would not be considered as deindustrialising since the reason for the decline in industrial employment is reduced labour intensity rather than the overall decline in value added or share of industry in GDP (Tregenna, 2009, p. 461).

All of the presented papers seek to assess which factors most affect deindustrialisation, and therefore most of them assume that internal and external factors affect deindustrialisation independently. In reality there is a possibility that external factors, such as trade or FDI, directly affect the internal factors (Kang & Lee, 2011, p. 318). However, after numerous researches on the causes of deindustrialisation the general consensus is that internal factors are stronger than external factors, and therefore represent the main cause of deindustrialisation. Consequently, when modelling deindustrialisation Rowthorn’s model is in most cases used as a starting point. However, most studies are based on data for developed countries; therefore deindustrialisation at lower levels of income in formerly socialist (developing) countries is still mainly uncharted territory.

Mickiewicz and Zalewska wrote several papers trying to cover various aspects of deindustrialisation in former socialist countries. In their paper from 2001, they model the employment evolution structure in these economies. They conclude that in countries where reforms were more efficient both the decrease in GDP and the share of industry in GDP would be smaller (Mickiewicz & Zalewska, 2001, p. 18). These results also indicate that the structural evolution of the economy is affected more by the speed and quality of reforms than by GDP levels. In other words, the “quality” of reforms, rather than the initial level of GDP (at the beginning of the reform) determine the “path” of development (transition) of an economy (i.e., the path by which the structure of employment in the economy changes). Finally, they conclude that rapid deindustrialisation is not the optimal path of transition.

In a later paper Mickiewicz & Zalewska (2002) prove a negative relationship between the size of deindustrialisation and the effectiveness and consistency of market reforms. They also
show that agricultural reforms play a significant role in the placement of former socialist countries on a development path that leads to convergence to EU employment structures.

4. CRISIS AND THE RETURN TO INDUSTRIAL POLICIES

Until the global crisis of 2008 it was conventional wisdom that industrial policies are in opposition to the fundamentals of the neoliberal system. Nowadays, economists (see Rodrik, 2009) stress that industrial policies are necessary in case of market failures. Both developed and European Union countries are now returning to industrial policies with the aim of reindustrialisation. Most of the transition countries were hit hard by the global crisis. It revealed weaknesses in their economies and the fragility of the transition process. The comeback to industrial policies is therefore an opportunity not to be missed. Until recently, most European transition economies had no industrial policy and they are adopting one primarily because of EU’s request (if they are member states), or by simply following EU’s example. In our opinion, these countries should take the industrial policy seriously as a way to economic growth and prosperity.

A key part of the EU strategy of economic recovery is the idea of a joint, strong, ambitious and proactive industrial policy (The Concept Paper, 2013). The basic idea of integrated industrial policy is described in the Communication on industrial policy 2010, 2012 and the recent Communication 2014. The European Commission (2014) believes that strong industrial foundations will be crucial for the economic recovery and competitiveness of Europe. The whole strategy is written in the spirit of urging need for the reindustrialisation and modernisation of Europe's industrial base that would trigger sustainable development and increase employment.

The EU strategic documents also emphasise: 1) Development of key technologies (KET - Key Enabling Technologies) such as microelectronics, biotechnology, nanotechnology etc.; 2) Advanced manufacturing technologies such as clean production (3-D printing), also photonics, robotics etc.; 3) Bio-products markets or markets for industries that use renewable energy sources or apply bio-based production processes; 4) Clean transportation, including vehicles and boats with engines that run on alternative fuels, and smart grids or other adequate infrastructure that is necessary for the integration of renewable energy in the electricity system. In addition, special emphasis is placed on a sustainable industrial policy – cost reduction, energy efficiency and waste reduction.

However, it is a big question if transition economies should follow the same principles as developed countries. As we have shown, these countries differ by their level of development and therefore it stands to reason that their economic policies should be different too. Besides, even if they take a key guidelines form developed countries the question remains whether they are able to follow all of the key points.

5. AS A CONCLUSION - THE IMPLICATIONS OF THE ANALYSIS RESULTS TO REINDUSTRIALISATION SCHEMES IN TRANSITION COUNTRIES

A closer look on the main determinants of deindustrialisation in developed countries leads us to the conclusion that all of them have an effect on transition countries deindustrialisation processes too. The question is if the effects are of the same direction and intensity. The exact quantification is left for some future empirical work. But, the authors believe that there are differences, and descriptive analysis conducted in this paper indicates that.

The literature overview suggests that the process of deindustrialisation took its natural course in developed countries while the deindustrialisation of transition countries is/was significantly different. That is, the level of GDP per capita of the developed countries on which the deindustrialisation occurred was higher than it is in transition countries. Therefore, it can be
concluded that the de-industrialisation in the transition countries was premature and new industrial policies need to be considered.

If industry is the engine of growth and thus the trigger of overall economy development, then we can conclude that the process of de-industrialisation in transition countries is not synonymous with the process of economic development. Policymakers in transition countries should take this fact into account. On the other hand, since our approach looks at all of the countries together as a group, it is difficult to give policy recommendations without extensive analysis of data for individual countries. However we can note that due to the fact that de-industrialisation processes in transition and developed countries differ, economic policy regarding re-industrialisation should be modelled separately.

What is certain is that transition countries definitely need an industrial policy in order to re-industrialise. We believe that transition countries should learn from the experience of developed European countries and the Asian tiger economies, but that they should not directly copy the patterns. In doing so, the focus of a country’s industrial policy should be based on modern globalization trends, but also on existing facilities, technologies and on the inadequately exploited qualified labour force. They should also try to attract foreign direct investment in domestic industry.

The approach of “picking winners” was not proven effective in the former socialist countries. Industrial restructuring and export growth are necessary not only for industrial growth but also comprehensive economic growth. We recommend creating a positive business climate in which the successful companies might stand out. In addition, the policy of clustering is in our opinion to be preferred. In doing all of this, the government policy plays a key role. Finally, in order to make the process of re-industrialisation successful, industrial policies should be part of a concisely designed national economic strategy.

LITERATURE
MARKET STRUCTURE AND PERFORMANCE IN THE BANKING INDUSTRY

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ABSTRACT
This paper reviews the analysis of market structure and performance in the banking industries in selected countries with special remark on Croatia. During the last two decades, Croatian banking industry has experienced a transition period as a consequence of deregulation of financial services sector, development in information technology and globalization of the banking industry. Impacts of that changes were observable in areas such as number of banks and bank branches, used technologies, quality of human resources and the scope of banking operations in the industry as well as regulatory frame and institutional structure of the banking industry. This paper investigates correlation between banks’ market structure and banks’ performance and their impact on the performance of the banking industry. Therefore, efficiency and productivity as well as concentration are an important requirement for the development of the banking industry.

Keywords: banking industry, market structure, bank performance, Croatia

1. INTRODUCTION
There is no banking system in the world which did not pass through various changes. Emerging countries from Central Eastern Europe (CEE countries) started transformation of their financial/banking systems few decades ago as an effect of abandoning communism. Transformation of general economy is known like economic transition what include privatization, liberalization and stabilization. The basis of that changes are in the Washington Consensus from 1989. The Washington Consensus adopted for the economies in transition represents the agreement between the Governments of the debtor countries and international institutions. Core of agreement is on the implementation of neoliberal approach to administering the country, which means greater emphasis on the free functioning of markets, institutions and price without government impact, liberalization of foreign trade sector and overall reduction of government importance on the national economy. The neoliberal approach meant liberalization and deregulation of all segments of the economy. Croatian financial system, as well as financial systems in other transition economies, has in last decades been strongly influenced by the globalization process taking place under the auspices of the World Trade Organization. At the outset of WTO over 70 members took on some obligations, out of which about 60 members for the liberalization of the banking sector and 10 for the insurance industry. Liberalisation of the financial sector is achieved through external and internal liberalization over time i.e. through several stages with the possibility of retaining a certain degree of restriction. For each country this process had its individual course, but the
goals were, with no doubt, to reduce the restrictions in this sector, to abolish monopolies, to increase competition which consequently contributes to faster economic growth in the national economy and to ensure an efficient allocation of resources.

At the beginning of transformations of economy, financial systems in CEE countries were highly bank based financial systems with mostly state owned banks and undeveloped non-banking sector. Croatia had same state with all of its positive and negative characteristics. With all general efforts what include the Washington Consensus and world globalization process there is also trends which causes changes in financial/banking sectors: the deregulation of financial services at the national level and country opening to international competition, expansion of informatization, growing disintermediation and increased emphasis on shareholder value. The banking systems in CEE countries has been transformed as a result of privatization of state-owned banks that had dominated their banking systems in the early 1990’s. The period was marked by crucial structural changes which can be described by the entry of foreign capital, the growth in credit activities in particular to households, the improvement in profitability, high and satisfactory rate of capital adequacy despite credit expansion and the growth of risk assets and the improvement of supervisory framework. According to that facts, the new international banking architecture has been affected, in first way, by financial liberalization. Indeed, the various measures of the latter have increased interbank competition what strictly influence on main goal of bank business, profit.

All that reforms aimed to enhance both the productivity and efficiency and the degree of competition of banking markets as a way of improving overall operational performance of the financial services sector specialy because problems in the functioning of the banking sector can have an impact on macroeconomic (price stability and international capital markets) and microeconomic effects (functioning of the payment system and development of financial markets and brokerage functions).

Consequences of early state ownership also is affected on level of capital adequacy. Capital adequacy is at much higher levels in emerging markets than in developed economies. This has allowed banks to sustain their growth and to feel practically no or little bit pressure from regulators on capital adequacy what was clearly obvious on satisfaction of Basel III requirements. Loans in emerging markets have been growing at double-digit rates for most of the past decade, and the economic slowdown has only briefly interrupted this trend. Yet the gap to developed-market banks has also been disappearing, as these banks have boosted their capital positions significantly following the financial crisis.

The paper is organized as follows. Section 2 presents theoretical background of related literature on market structure and performance in the banking sector, discusses on main characteristics and relations. Section 3 gives overview of banking industries in selected countries with special remark on concentration and bank performance. Analysis of concentration and bank performance in Croatian banking industry is investigated in Section 4. At the end, Section 5 concludes the article.

2. REVIEW OF RELATED LITERATURE

For investigation of behaviour of the banking market we can use structural and non-structural approaches. Structural approaches are mainly based on the traditional industrial organization theory which focuses on the structure-conduct performance (SCP) paradigm and on the efficient structure paradigm. Literature based on structural approaches has investigated how the market concentration weakens the market competition by fostering collusive behaviour among firms. Conversely, non-structural approaches assume that factors other than market structure and concentration may affect competitive behaviour, such as entry/exit barriers and the general contestability of the market.
The SCP paradigm is the most used framework for the analysis of the performance of the banking industry. The structure-conduct-performance (SCP) model, which is incorporated in neoclassical theory, dominated industrial economics until the early 1980s (Chamberlin, 1933; Robinson, 1933, 1953; Bain, 1951, 1956). The basic principle behind the SCP paradigm was that perfect competition and monopoly are usefully viewed as opposite ends of a spectrum of market structures along which all markets lie (Pepall et al., 2008, p. 10). Measures of market performance try to provide an answer to whether market power is exercised in an industry. Two different measures that directly or indirectly reflect the profits or the relationship of price to costs are commonly used to gauge how close an industry’s performance is to the competitive benchmark: the rate of return and price-cost margin. A third measure Tobin’s q is less commonly used (Carlton and Perloff, 2005, p. 246). According to this model, market structure determines the way in which companies in one industry interact, which in turn determines their profitability. The proponents of this model argued that market structure was basically affected by technological factors (e.g. economies of scale and scope), and that the existence of high profit levels in one industry was evidence of the monopoly that a company in a given industry possessed. While its theoretical foundations are well established in the industrial organization literature (Stigler, 1964; Scherer, 1989), its applicability to the banking firm has not always been rigorously justified. The SCP theory predicts that profits and output prices would be higher the greater the level of concentration in a given market. This is due to the greater ease of collusion in a more concentrated market. When applied to the banking industry it predicts that profits, interest rates on each type of loan and services charges would be higher in a more concentrated market. On the other hand deposit rates offered would vary inversely with concentration (Gilbert 1984).

The analysis of market concentration in the banking sector typically branches off into two directions in the literature. One direction is a structural approach based on the so-called SCP paradigm (structure-conduct-performance), the hypothesis on market efficiency and a range of other formal approaches in the theory of industrial organization. The SCP paradigm analyses whether a higher level of market power concentration leads to tougher competition between large banks and better overall market performance for clients (primarily through lower interest rates). This paradigm highlights the theoretical relationship between the structure (concentration levels), behaviour (competition) and performance (for example, profitability of banks).

The literature on bank performance is not conclusive on all the factors that contribute to bank profitability. However the literature points to factors such as market concentration, market power, ownership, efficiency and market growth as influencing the performance of banks. The literature is also inconclusive about the nature of the influence of these variables on bank performance.

Non-structural approaches have been developed in the context of the new empirical industrial organization (NEIO) literature. This study is based on structural approaches expecting to uncover the advantage of enhancing banks operational efficiency against bank concentration. The next section presents basic arguments of structure conduct performance hypothesis (SCH) and efficient structure hypothesis (ESH), application in banking industry and their findings.

The intuition behind the MP theory contains two hypotheses: Under the structure conduct-performance hypothesis (SCP), more concentrated markets lead to increased interest rate spreads as a result of market collusion and other imperfections. Under the relative-market-power hypothesis (RMP), on the other hand, banks with strong market shares may capture market power from product differentiation, which allow them to set advantageous deposit and loan rates. While subtle, these theories differ in the fact that RMP hypothesis suggests that
only the largest banks will benefit from increased consolidation, while the SCP hypothesis suggests that all banks will benefit—regardless of market share or size (Skorep, 2011, p. 3). Most usual researches are based on bank profitability and concentration. Accord to that point of view here is literature review on selected topic and comparable variables and methodology. On the basis of the obtained results, Erins and Erina (2013) conclude that internal and external bank performance indicators may not affect the profitability of CEE countries banks directly, except such indicators as credit risk and bank size, which influence one of the bank profitability indexes – return on average equity. Boyd, De Nicolo and Al Jalal (2006) explored relationship between concentration and banks risk of failure, using z-score as an empirical risk measure. Their results revealed a positive association between market concentration and risk of failure, driven primarily by a positive association between concentration and volatility of the rate of return on assets. Andries and Asandului (2010) analyse the impact of financial liberalization on banking performances, highlighting the determination of the impact of the presence of foreign banks on the performance of the Romanian banking system. The analysis reveals the fact that the liberalization and internationalization of the banking system had as effect the increase of competition which determined domestic banks: to reduce their operational costs concomitantly with investing some important amounts into new technologies; to increase their credit portfolio in relative terms by reducing other assets and increasing the client base, which led to the increase of the credit risk and to the increase of the bank provisions; to diminish their net interest margin by decreasing the interest rate for loans, concomitantly with increasing the interest rate for deposits. Ramlall (2009) has discovered a positive correlation between bank size and profitability: the bigger is the bank, the more profitable it is in comparison with a smaller bank due to economies of scale. On the other hand, Hannan and Prager (2009) note that small banks can earn higher profit because they have lower expenses and better performance efficiency.

Bailey (2007) examined the nature of the relationship between concentration (measured by HHI) and profitability (presented with ROA and NIM) by utilizing a dynamic VAR framework. The results of the conducted analysis did not support the SCP hypothesis. Moreover, results showed that improvements in efficiency contributed to increased profitability for the dominant bank. Brissimis et al. (2008) examine the relationship between banking sector reform and bank performance – measured in terms of efficiency, total factor productivity growth and net interest margin – accounting for the effects through competition and bank risk-taking. The model is applied to bank panel data from ten newly acceded EU countries. The results indicate that both banking sector reform and competition exert a positive impact on the bank efficiency, while the effect of reform on total factor productivity growth is significant only by the end of the reform process. It is unavoidable to study some researches with impact of financial crisis. According to that, Andries et al. (2012) show large differences between pre-crisis period and crisis period and among the banking systems in terms of performance indicators. In average, banks from countries that are not members of European Union recorded an ample decrease of profitability and stability during current financial crisis. They observe that the best-performing banks during current financial crisis had significantly more core equity capital and are more focus on traditional banking activities. The SCP framework has been widely used in the literature to examine market structures. However, it does not account for other factors which influence firms’ profitability and concentrations. Further, SCP studies ignore the long-run equilibrium in the market. Therefore, the evidence from market concentration studies may be insufficient to support firm conclusions about the relationship between market behaviour and competition (Seelanatha, 2010).
3. BANKING INDUSTRY IN SELECTED COUNTRIES

The market structure and profitability of banks constitutes a strong element in the analysis of banking industry, especially in the countries in which the level of the banking industry represents the main component of the financial system what is clearly obvious in Central Eastern Europe (CEE) countries. That structure of financial system is known as bank-based financial system. Further, that part of Europe is synonym for changes in their banking industries which are effect of mutation at the level of the structure of shareholding as a result of bank privatization, then of the entry of foreign banks and of the increase of competition determined by the liberalization of the market and changes in supervision and regulation. The early stages of banking transition in South-eastern European countries consisted in the restructuring of state banks and in abandoning direct financing. Reconstruction leads to bank privatization and growth of financial markets. The period of transition of the banking industry included significant structural changes which had some basic features: 1. Entry of foreign capital; 2. Growth in domestic lending in particular for consumption primarily for consumption of foreign goods; 3. Increase in the exposure to foreign currency risk; 4. Increase in profitability and a satisfying rate of capital adequacy; 5. Implementation of international accounting standards; 6. Changes in the regulation and supervision; 7. Credit expansion and growth of risk assets.

Since the inception of the financial crisis in 2008, the euro area banking sector has been going through a rationalisation process which has resulted in a reduction in the overall number of credit institutions. This banking sector consolidation process relates to pressures to achieve cost containment, deleveraging and restructuring, in particular in the banking sector of those euro area countries that were more severely affected by the financial crisis (ECB, 2014). At the end of 2013, the total number of credit institutions, including foreign branches, in the euro area was 5,948, down from 6,100 in 2013, if calculated on a non-consolidated basis. By comparison, at the end of 2008 there were 6,690 credit institutions, including foreign branches. Mentioned changes have significant impact on market concentration. Market concentration, as measured by the share of total assets held by the five largest credit institutions or by the Herfindahl index is shown on Chart 1. HH index has increased both at euro area and EU level since 2010 and in comparison with the pre-crisis period. This primarily reflects the decline in the number of credit institutions as M&A activity remained rather subdued. For both the euro area and the EU as a whole, the indicators peaked in 2011, fell slightly in 2012 and increased again in 2013, remaining well above the pre-crisis levels (ECB, 2014). The modest increase in 2013 was mostly driven by moves in the crisis countries where larger banks acted as consolidators in resolutions of non-viable entities – especially in Cyprus, Greece and Spain.
With regard to cross-country comparison, concentration indices reflect a number of structural factors. Banking systems in larger countries, such as Germany and Italy, are more fragmented and include strong savings and cooperative banking sectors. Banking systems in smaller countries tend to be more concentrated, with the notable exception of Austria and Luxembourg. In the case of Austria, this is on account of a banking sector structure similar to that which characterises larger countries, and in the case of Luxembourg it is due to the presence of a large number of foreign credit institutions. At the end of 2013, market concentration (measured by the share of assets held by the five largest banks) ranged from close to 95% in Greece to just over 30% in Germany and Luxembourg (see Chart 2). Regarding developments in the period from 2008 to 2013, the banking sector structure tended to become more concentrated in a number of countries, in particular those undergoing deep banking sector restructuring processes such as Cyprus, Greece, Ireland or Spain (ECB, 2014).
For European banking, 2013 was a year of extensive deleveraging. Spill overs of this trend to the CEE region were once again limited, but its overall positive image does not rule out selective country strategies on the part of foreign-owned CEE banks (Raiffeisen Research, 2014). Banks from developed countries carried out substantial portfolio shifts over the last three to five years (focussing on more profitable and less risky markets).

International banks have been active in the transition countries since the early 1990s, after a significant financial market liberalisation and elimination of entry barriers. Today foreign banks already own more than 50% of the equity capital of banks in Central and Eastern Europe (CEE). In many countries foreign banks control over 80% of the banking market (see Chart 3). The interest of foreign banks has now further enlarged into Eastern Europe, towards to attractive emerging markets of Russia and Ukraine (Liuhto, Sorg and Uiboupin, 2006).

In transition countries banking sectors differ from their counterparts in many developing and emerging market countries by the high percentage of assets held in banks with majority foreign ownership. The change in foreign participation in banking in these countries from the early transition years to the later ones is significant. Next chart clearly shows that statement. Central Europe (CE) consists of five EU and OECD members: Poland, Hungary, Czech Republic, Slovakia and Slovenia. South-eastern Europe (SEE) consists of seven countries, which are characterized by stark economic and political divergence. SEE consists of the EU member states Romania, Bulgaria and Croatia, as well as four other countries: Serbia, Bosnia and Herzegovina, Albania and Kosovo.
During the past few years, state-owned banks in CE have increased their average market share by 3-4pp, but only to a still modest level of around 10-15%. This tendency was driven largely by the growing extent of state-ownership in the Polish, Hungarian and Slovenian banking sectors. In the case of the latter two markets, recent increases in state-ownership were largely crisis-driven and/or induced by tough policies. Conversely, in Poland’s case the moderate increase in the state-ownership ratio was more a reflection of the relative strength of state-run banks, as well as well-targeted policy initiatives to support overall economic growth. In SEE, the average market share of state-owned banks increased marginally in recent years, i.e. by 2-3pp, at low average levels of around 7%. This increase was driven by a broad-based but modest increase in state ownership across all larger SEE banking markets (i.e. in Romania, Serbia, Croatia and Bulgaria). According to previous explanation, next Table shows main indicators for banking industry in selected CEE countries in 2013.

<table>
<thead>
<tr>
<th></th>
<th>Number of banks</th>
<th>Market share of state-owned banks (% of total assets)</th>
<th>Market share of foreign-owned banks (% of total assets)</th>
<th>ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slovakia</td>
<td>28</td>
<td>0,8</td>
<td>99</td>
<td>7,8</td>
</tr>
<tr>
<td>Romania</td>
<td>39</td>
<td>8,5</td>
<td>90</td>
<td>1,3</td>
</tr>
<tr>
<td>Hungary</td>
<td>35</td>
<td>5,8</td>
<td>88</td>
<td>4,5</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>45</td>
<td>2,6</td>
<td>83</td>
<td>20,6</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>30</td>
<td>3,4</td>
<td>70</td>
<td>5,31</td>
</tr>
<tr>
<td>Slovenia</td>
<td>23</td>
<td>61</td>
<td>31</td>
<td>-31,6</td>
</tr>
</tbody>
</table>

As we can observe in Table 1, Slovakia has biggest market share of foreign-owned banks with 99% being followed by Romania with 90%, Hungary with 88% and Czech Republic with 83%. Countries with less than 80% are Bulgaria with 70% and Slovenia with only 31% of market share of foreign-owned banks. Table 1 also reveals that only Slovenia had negative
return on equity with -31.6% and excellent result of Czech Republic with 20.6%. Result of Slovenia is very indicative according to their bank ownership. Namely, Slovenia has big market share of state-owned banks with 61%. That fact is also visible in Table 2 which shows ROA and HHI for selected countries from 2010 to 2014. Important note for next table is that Herfindahl-Hirschman Index is counted for credit institutions. But considering that in listed countries high dominant role in group of credit institutions play banks, it is justifiably to do comparison with result of ROA for banks.

**Table 2: Return on Assets (ROA) (%) and Herfindahl-Hirschman Index (HHI) for selected countries (UniCredit Research, 2015 and ECB, 2014)**

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Bulgaria</td>
<td>0.9</td>
<td>789</td>
<td>0.8</td>
<td>766</td>
<td>0.8</td>
<td>738</td>
<td>0.6</td>
<td>730</td>
<td>0.7</td>
<td>-</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>1.5</td>
<td>1045</td>
<td>1.4</td>
<td>1014</td>
<td>1.6</td>
<td>999</td>
<td>1.4</td>
<td>999</td>
<td>1.3</td>
<td>-</td>
</tr>
<tr>
<td>Hungary</td>
<td>0.2</td>
<td>828</td>
<td>-0.4</td>
<td>848</td>
<td>-0.1</td>
<td>873</td>
<td>0.1</td>
<td>836</td>
<td>0.2</td>
<td>-</td>
</tr>
<tr>
<td>Romania</td>
<td>0.0</td>
<td>871</td>
<td>-0.1</td>
<td>878</td>
<td>-0.7</td>
<td>852</td>
<td>0.1</td>
<td>821</td>
<td>0.4</td>
<td>-</td>
</tr>
<tr>
<td>Slovakia</td>
<td>1.1</td>
<td>1239</td>
<td>1.4</td>
<td>1268</td>
<td>1.0</td>
<td>1221</td>
<td>1.1</td>
<td>1215</td>
<td>1.1</td>
<td>-</td>
</tr>
<tr>
<td>Slovenia</td>
<td>-0.1</td>
<td>1160</td>
<td>-0.9</td>
<td>1142</td>
<td>-1.4</td>
<td>1115</td>
<td>-2.1</td>
<td>1045</td>
<td>-0.9</td>
<td>-</td>
</tr>
</tbody>
</table>

Previous Table shows ROA and Herfindahl-Hirschman Index for Bulgaria, Czech Republic, Hungary, Romania, Slovakia and Slovenia. As a general rule, if the Herfindahl index is below 1,000 it indicates a low concentration, while a value higher than 1,800 indicates a high concentration. For values that range between 1,000 and 1,800, the banking industry is considered moderately concentrated. Table reveals significant concentration differences in selected countries. In Bulgaria, Hungary and Romania the concentration ratios on banking markets are relatively low (below 900). The highest concentration ratios can be found in Slovakia with 1215 points in 2013. Czech Republic and Slovenia are close around 1000 points. One trend in Table is again significant, that is motion of return on assets for Slovenia which is continuous negative in observed period. On that basis, SCP paradigm should be reviewed according to moderately concentrated market and negative return indicators.

### 4. INFLUENCE OF MARKET STRUCTURE ON PERFORMANCE IN CROATIAN BANKING INDUSTRY

The shock of the recent economic crises has scientists wondering about the future of banking industry. Given the wave of consolidation witnessed over the past five decades and the recent pressure to limit and penalize the size of banks tagged ‘too big to fail’, it has never been more important than now that we resurrect the age-old structure-conduct-performance Industrial Organization (IO) debate on the relationship between market structure and profitability in the banking industry (Skorep, 2011, p. 2). Being exposed to advantage of the requirements of these various changes, the bank was marked by extensive restructuring, including the strategy of concentration seems the best solution for better banking performance. In this context, increasing the concentration of banking in theory allows to create value, gain market power and generate economies of scale and scope in order to seek greater efficiency.

Within the existing literature on the profit-structure relationship, most studies find empirical support for the assumed positive relationship between bank profitability and a measure of market structure, such as market share or some other measure of concentration (e.g.
concentration ratios or a Herfindahl index), although this evidence is weak at times (Punt and van Rooij, 2001). There is some other benefits of high concentration and they are: 1. Banks of large size are easily diversified. This allows them to adjust in other sectors of the market when one sector takes a turn for the worse: a smaller bank that focuses on one or two sectors of the industry is highly vulnerable to fluctuations within those sectors. 2. High concentration levels will increase profits for the dominant banks within the industry: while this may lead to higher interest rates and fees it will also insulate banks from economic shocks. Also, with higher franchise values banks will have less incentive to take financial risks in pursuit of profits (Helen, Murdoch, and Stiglitz). 3. Larger banks are more easily monitored than many small banks. It is easier for a regulatory commission to look after a few large banks then many small ones. Systems within each of the large banks will be similar rather than having to learn the systems of many small banks.

The Republic of Croatia is good example for importance of banks in financial system because they play dominant role in Croatian financial system. In all of aspects of financial system like country's currency, payment system, financial markets, financial institutions and relations banks are unavoidable. They are the most active of all financial institutions in the country, both in terms of the payment system and their presence on all the three financial markets: money, foreign exchange and the capital markets. Their activities are regulated and supervised by the Croatian National Bank (CNB).

The structure of Croatian banking sector has experienced significant changes from the beginning of 1990s. Although banks in Croatia were transformed into joint stock companies (owned mainly by enterprises) already in 1989, they continued with practices divorced from profitable banking, such as lending to related parties. Moral hazard and adverse selection were fuelled by war hardships, leading to a high share of non-performing assets in banks’ balance sheets. Evident example of growth of banking industry is growth in total assets of all banks in Croatia. Total assets of banks in 1999 was EUR 12,15bn, than in 2006 it jump up to EUR 41,4bn what is decrease of EUR 29,25bn or 240%! In 3Q/2014 it was EUR 51,3bn what is decrease of EUR 9,9bn or 24% in comparison with 2006. Growth in bank assets continues also in times of financial crisis (2008, 2009, 2010, and 2011). In addition to the absence of stronger growth in credit, the decrease in bank assets for the second consecutive year (2012 and 2013) can primarily be attributed to one-off effects of regulatory and methodological changes in the last quarter of 2013 and changes at the level of two individual banks.

The mergers and acquisitions are mainly related to the entry of foreign banks resulting in significant changes in banks’ ownership. As a result of bank liquidations and mergers and acquisitions during the 1990s the number of banks declined from the highest level of 60 in 1997 and 1998 to 33 banks in 2010 and 30 in third quarter of 2014. A slight downward trend in the number of banks was continued for the fourth consecutive year. At the end of 2012, Međimurska banka d.d. merged with its parent bank Privredna banka Zagreb d.d., so that there was 31 banks in Croatian banking sector. In September 2013, bankruptcy proceedings were opened against Centar banka d.d., so the number of banks (including the savings bank) fell to 30. Figure 1 shows that statements.
Figure 3 shows Croatian banking system by ownership as % of total assets. In comparison to 1999 when the share of state owned banks in total assets of banking sector was 45.6 percent, it declined to 5.7 percent in 2000 and 5.3 percent in 3Q/2014. In the same years the share of foreign owned banks increased from 39.9 to 84.1 percent. In 3Q/2014 foreign owners controlled 90.0 percent of the total banks’ assets.

Due to the bankruptcy of one bank in domestic private ownership, the total number of banks in domestic ownership was reduced by one, to 14 (Figure 1). The remaining 16 banks were majority owned by foreign shareholders and their share in the total assets of all banks was dominant. It stood at almost 90%, a slight decrease from the end of 2012. Assets of banks in foreign ownership fell by 1.0%, while assets of banks in domestic ownership went up considerably by 3.6%. Assets of banks in domestic state ownership increased by as much as 10.3%, whereas the fall in assets of banks in domestic private ownership stood at 2.5%. This fall was due exclusively to the mentioned exit of one bank from the system. Excluding this effect, assets of this group of banks rose by 5.5%.

Among the banks in majority foreign ownership, the largest number of banks, six of them, were controlled by Austrian shareholders and the assets of these banks accounted for 60.5% of total assets of all banks. The next four banks were in Italian ownership and their total market share was 18.3%. Shareholders from France, Hungary, San Marino, Serbia, Switzerland and Turkey each had one bank in their ownership, with a total share in the assets of all banks of 10.9%.
Next figure reveals share of total assets by two and four largest banks. This index refers to the concentration of banking activities. The concentration ratio of two or four (CR2 or CR4) leading companies is calculated as the sum of the percentage of market share of the two or four largest banks in the market. An unwritten rule says that if four largest firms control more than 40% of the market, it is an oligopoly. If the value of this ratio is higher than 90% it is a pure monopoly. Market concentration as measured with the share of total assets held by the two largest banks have cyclical trend what is obvious in data for 1996 when it was 46,3 then in 1998 40,5, in 2000 47,5 and in 2007 40,9 and in 3Q/2014 43,5. Situation with CR4 is more stable and it is in last decade between 64,9 and 66,8.

The Herfindahl–Hirschman Index (HHI) is considered the most reliable indicator of market concentration. The value of this index is defined as the sum of squares of individual market shares of all the competitors who participate in the market. As a general rule, an HHI below 1,000 signals low concentration, while an index above 1,800 signals high concentration. For values between 1,000 and 1,800, an industry is considered to be moderately concentrated.
Unlike CR4 or CR8, the HHI value depends on the number of competitors in the market and the differences in their relative market powers. The HHI value decreases as the number of competitors in the market increases. Also, the value of this index increases as the differentiation in size of the market power increases, because large companies have a greater weight in the calculation due to the fact that market shares are squared.

Although the number of small banks in Croatia has been on a continuous decline, their still relatively large number maintained moderate values of the Herfindahl-Hirschman index (HHI). HHI for assets stood at 1440 at the end of 2013, which was only 0.9% higher than at the end of 2012 but it counts positive trend from 2010 when it was 1361. HHI for loans granted (net) increased somewhat more strongly, by 1.3% to 1468. Next Figure shows Herfindahl – Hirschman index for Croatian banking sector.

![Herfindahl – Hirschman index (HHI) (Croatian National Bank, 2015)](image)

Return on average assets (ROAA) and return on average equity (ROAE) have always been mentioned among the main indicators characterizing bank performance and profitability. Following their two-year slight recovery, return indicators fell in 2012 and even more sharply in 2013. They dropped to their historic lows since the crisis 1998, when losses were recorded at the banking system level. The return on average assets (ROAA) thus stood at 0.2%, and the return on average equity (ROAE) stood at 0.9% (Figure 5). The decline in profitability in 2013 was primarily the result of the growth in risk costs, followed by the decline in net interest margin from 2.7% to 2.5%. Other margins remained unchanged, maintaining bank operating profitability at a very good level. Figure 5 reveals that facts.
In 2010 and 2011, banks managed to offset the growth in expenses on loss provisions and increase return indicators by widening the interest spread, notably by reducing interest expenses, and through firm control of general operating expenses. However, in 2012 return indicators fell considerably, under the key influence of the fall in average interest income. The fall was due to the rise in the significance of less risky and less generous loans (affected also by various kinds of incentives) and movements in interest rates (including the cut in the highest permitted interest rates). Such developments continued into 2013 and the downward trend in average interest income was even more prominent.

5. CONCLUSION
Particularities of banking industry, in general sense, considering the changes in macroeconomic indicators and their relation puts banking industry for high level of importance. In terms of systemic risks they are unavoidable theme especially for bank based financial systems like Croatian. That gives market concentration and performance of banking industry more importance for research. It is necessary high stability for banking industry what implies strog supervision and regulation what have impact on bank business. According to that it is important to implement all possible requirements on estimated time guided from central bank, what Croatian National Bank manage and does very well.

Croatian banking sector is consolidated due to entry of foreign banks in 1999 and 2000 when foreign banks took over four largest state-owned banks. Today, foreign banks are dominant in all aspects of bank business and the HHI index is at the level 1,430 points. Also, there is positively relation with higher level of concentration and stability. Increase in HHI was primarily driven by market exit of numerous unsound banks what contributed to the higher stability of banking sector. Foreign ownership and on the other hand financial crisis have impact on financial result of banks therefore SCP paradigm can be applicable on Croatia, but just on period before global financial crisis.

Croatian banking sector is consolidated, healthy and sound banking industry. Decline in some aspect of bank business is consequence of mainly disproportion in Croatian economy and their stakeholders.
LITERATURE
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REFERENCE SET OF PERFORMANCE INDICATORS OF HIGHER EDUCATION INSTITUTIONS – CASE OF THE FEDERATION OF BOSNIA AND HERZEGOVINA

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ABSTRACT
Calculating of performance indicators in higher education institutions arises from the need to improve the quality of higher education institutions. In this paper, the problem of research is the identification of the reference set of performance indicators in the higher education sector. Business indicators are an indispensable instrument tests and research the efficiency of business operations. The simplicity of their design and use has led to their countless multitude as soon as the opening series of questions: choice of indicators, ranking indicators, aggregating indicators and selection basis for comparison.

In the public sector of the Federation of Bosnia and Herzegovina, and therefore in higher education institutions is not prescribed reporting on performance, we undertook an empirical research with the aim of creating a reference set of performance indicators of higher education institutions in the Federation of Bosnia and Herzegovina. The paper points out the deficiencies of financial analysis, analysis of safety and stability with a focus on the analysis of (dis)satisfaction of service users of higher education institutions. In this way the research conducted on a sample of 300 students in order to identify useful information for prospective students. Most of these information can be quantified and used for design and improvement of the set of indicators to measure the business performance of public higher education institutions in the Federation of Bosnia and Herzegovina.

Keywords: analysis of satisfaction of service users, higher education sector, financial analysis, reference set of performance indicators

1. INTRODUCTION
Higher education sector is presently facing with financial and institutional reforms because budgetary resources are reducing on the one side while on the other side there are increased demands for quality. So, there is a big problem of unbalance between available financial resources and needs of higher education institutions (further in the paper HEIs). So, there is increasing interest in many countries in assessing performance of HEIs and also departments within institutions.

For HEIs, it is important to monitor and improve the quality. For that purposes they need to develop adequate and comparable performance indicators (further in the paper PIs). Performance measurement in the higher education system include set of financial and nonfinancial indicators. While financial indicators put focus on financial structure of HEIs, nonfinancial indicators are connected with customers, internal process, learning and growth.

The accounting systems of HEIs are based on a budgetary accounting concept or on a modified accrual accounting principle. The goal of that existing system is primarily in satisfying legal terms in the form of external reporting, but not in providing quality information to the internal users for effective management.
Thus, in order to succeed, institutions of higher education, just like profit oriented organizations, have to know how to enhance and manage their performance. In that context, the need for development of financial but also nonfinancial indicators, that would improve financial management and quality and would enable implementation of university strategy in higher education’s system, seems logical and necessary but still there is no legal requirement for performance measurement not just at higher education institutions but also at whole public sector institutions in the Federation of Bosnia and Herzegovina (FB&H). The paper depicts the process of defining set of performance indicators for higher education institutions in FB&H. Once determined, set of performance indicators become a basis for improving control of use of organizational resources, quality of business results, for aligning business strategy with business technology and for comparison of institutions in same sector.

2. LITERATURE REVIEW
Countries forerunner of idea of measuring performance in higher education system that already have well developed performance measurement system in all public sector entities are Australia, United Kingdom and Canada (Vasicek, Lutilsky, Dragija, 2014, p.118). Each of the aforementioned countries has a broad spectrum of obligatory performance indicators required for official reporting.
The concept of indicators at HEIs in Australia is well established and consists from five groups of indicators (Department of Education, Science and Training, 2001):

a) student indicators (number of students enrolled in a given period; actual load of students (teaching hours and hours of exam preparation); enrollment method; share of graduate students in the total number of students; proportion of students from abroad in the total number of students);

b) staff indicators (number of employees in a given period; teaching and non-teaching staff as a share of total number of employees: the proportion of college and university degree non-teaching staff in total number of employees; share of employees by function in relation to total number of employees; teaching staff by titles as part of the total teaching staff (in percentages));

c) finance indicators (share of operating revenue in total revenues and incomes; share of operating expenses in total expenditures and expenses; salaries and costs related to salaries as a proportion of total expenditure; costs per relevant student groups (equivalent full-time student units - EFTSU); own revenues as a share of total revenues; revenues from research);

d) research indicators (share of research student groups of higher degree in all student groups; revenues from research generated by students in postgraduate studies; revenues from research per researcher (in percentages));

e) outcome indicators (rate of progression of students, graduates employed full-time, graduates who continue their regular studies, the average wages of graduates).

The UK PIs were developed out of recommendations of the Dearing Report (1997) to provide suitable indicators and associated benchmarks of the performance of the higher education sector. The principles underlying the development of the PIs were that they: use a consistent and standard format, are objective, and are simple, clear and fit-for-purpose. The first set of indicators was published in 1999 by the Higher Education Funding Council for England - HEFCE on behalf of all the funding councils across the UK, and in 2004 responsibility transferred to the Higher Education Statistics Agency - HESA (Pollard and others, 2011, p.1).

To guide the development of these important metrics, the Performance Indicators Steering Group (PISG) was set up in 1998. The PISG monitor the PIs, and have made some changes.
over time to ensure the indicators remain fit for purpose. As a result the PIs have continued to evolve since their introduction. According to HESA the indicators are calculated using both financial and nonfinancial information. HESA publishes a set of performance indicators for all publicly-funded UK HEIs in April and July each year. The indicators are based on student (the population covered can vary by mode of study (full-time, part-time), level of study (first degree, sub-degree) and age of student (young, mature)), staff and finance data returns all HEIs are required to make to HESA each year.

PIs calculated in the higher education sector in the UK (Vasichek, Budimir, Letinic, 2007, pp. 68-69) are:

a) access indicators (percentage of students who went to public school, percentage of students whose parents have lower levels of education, percentage of students coming from areas known for their small share of young people who attend higher education institutions);

b) completion indicators (are shown in two ways. The first method takes into account students enrolled in the first year and monitors whether they are also in the same institution the next academic year, transferred to another one or completely left higher education. The second method uses information about the current developments of students to anticipate what will happen in the long run, what percentage of students will graduate, what percentage of students will drop out of a faculty, but will continue to study in another higher education institution as well as what percentage of students will leave higher education without any qualification);

c) efficiency (is defined as the ratio of the time that is necessary in ideal conditions for students to complete the study and the time for which it is estimated that it will be needed to complete the study. If all students graduate within the expected time, the efficiency of the institution is 100 percent. However, some students are repeating a year for various reasons, some are dropping out, some are changing institution, leading to a drop in efficiency);

d) employment indicators (percentage of employed graduates or students who are still studying compared to those who are employed, unemployed or studying, and the percentage of employed students in the total number of employed and unemployed in the country);

e) research outputs (number of PhDs awarded in relation to the costs of the teaching staff and the amount of money collected and the number of contracts in relation to the costs of the teaching staff).

In the higher education of Canada the state imposed the following categories of PIs (Vasichek, Budimir, Letinic, 2007, pp.72-73):

a) indicators based on the program results: number of students; satisfaction of graduates; academic achievement of students moving from one institution to another; degree of execution of the program; success of graduates: employment and academic status; demand and program capacity;

b) indicators that measure financial efficiency: cost per student/program; cost per graduate student, indicators related to income; indicators in relation to expenditure; total load of teaching staff; use of space;

c) indicators based on the research activity: publications and other papers; degree of success of advisers; number of graduates; number of awarded employees; level of research works in cooperation with the local community and the industry compared to the number of employees.
HEIs in the Republic of Croatia are mainly budgetary users whose main objective is efficient and effective providing of higher education services while minimizing costs. There is no legislation that would regulate the use of PIIs either in higher education or any other part of the public sector. The calculation of financial indicators based on basic financial statements implies on a fact that in the existing reporting system of HEIs in the Republic of Croatia it is not possible to develop comprehensive performance measurement system.

Quality indicators represent the basis for making better decisions in higher education system. For the purpose of continuous monitoring of educational quality, Josip Juraj Strossmayer University in Osijek Quality assurance and improvement Office annually gathers quality indicators from all faculties of the University. Quality indicators that have been gathered at University of Osijek from 2005/06 till now include the following: registered students in relation to students that following year at study, graduated students at annual basis, the average length of studying, the average grade of studying, postgraduate study students, exam efficiency and grades and employment of graduated students.


- Socio–economic context (4 indicators)
- Coverage, progression and completion (42 indicators)
- The quality of educational achievements (12 indicators)
- Educational process (16 indicators)
- Educational resources (12 indicators).

The first category of indicators pertains to the socio-economic context of the educational system (4 indicators). This category includes indicators that point to the trend in the number of children and young people who will use the services of education in future, but also the indicator that point to the effects of education on employability income. The second category of indicators is the largest and contains 42 indicators (almost half the total number of indicators). This category includes indicators pointing to the coverage of children and young people by various levels of education, directing children outside regular (mainstream) schools within the compulsory education, inclusive compulsory education, regular progress of pupils, grade repetition, drop-out rates, completion of a certain level of education and progression to the next level of education. As for the secondary education, all these indicators are listed separately for each of the three groups of secondary education programs (four-year general education program, four-year vocational education program and three-year vocational education program). In addition to primary and secondary education, this category of indicators also includes the indicators describing the coverage, progress and completion in tertiary education, as well as an indicator which points to the adult participation (25-64 years) in lifelong education and training. The third category of indicators (12 indicators) refers to indicators relating to educational achievements of students on the final exam (after the introduction of graduation exams, the same set of indicators that exist for final exam would be included as a set of indicators), as well as student achievement in two international researches that Serbia is involved in (PISA and TIMSS international studies). These indicators show the quality of student educational achievements at different educational levels. The fourth group of indicators is related to some characteristics of the educational process (learning/teaching) at different levels of education (16 indicators). The indicators that are in this category point to some of the important aspects of educational process (e.g. time that is devoted to learning outside school, frequency of various forms of learning/teaching and motivation for school
learning), teacher participation in professional development and providing professional support for teachers, student and parent participation in school life and teaching and the quality of inter-relationships between the key stakeholders (student and parent satisfaction with the collaboration with school and teachers, frequency of different forms of violence between students and between students and adults at school). At the level of tertiary education, this category of indicators is represented by the mobility of students and teachers in Serbia and towards the universities in other countries. This category of indicators is specific in relation to other categories due to NEC: Indicators for Monitoring the State of Education (41) the reason that for them there are the least data in the existing sources of information. In other words, in future it would be necessary to develop indicators on data collection and assessment, as well as the indicators for reporting. The last, the fifth category has 12 indicators relating to the resources that are invested in education. One part of indicators pertains to financial investments in education from different resources (public-private, republican sources – local investments), as well as investment per pupil. In addition to financial resources, the indicators in this category pertain to the population of teachers who are engaged in education, as well as their salaries. There are significant problems with using adopted indicators: non-integrated universities, lack of financial resources, lack of information support etc.

3. RESEARCH METHODOLOGY
The quality of higher education is a complex very area, so countries, students, teachers, employers and other stakeholders participate in its creation, maintenance and development participate countries, students, teachers, employers and other stakeholders. Since the degree of customer satisfaction by higher education institutions one of the indicators of the quality of its services, research in this section is based precisely on the testing (via a questionnaire) (dis)satisfaction of students as of biggest users of higher education institutions. Student surveys is especially interesting topic in the entire Bologna process because they seem the greatest interest of the academic community. Certainly, they are very important, because, despite all the deficiencies they are a significant source of information for the management of higher education institutions. The traditional view that the quality is defined "from above" and that expresses an expert opinion is a thing of the past in all spheres of work and business. Quality must be in user's service or as a function of their satisfaction. Defined population for this research are students of public higher education institutions universities in Mostar, Sarajevo, Zenica and Tuzla. From this population randomly surveyed 300 students from different studies, study programs, cycles and years of study which provided representative sample. The survey was conducted in the winter semester 2013/14. (November-December 2013). Students questionnaire filled out anonymously. The questionnaire contained 10 questions (open and closed, multiple choice questions and Likert scale for issues that are related to the measurement of the level of student satisfaction with the activities carried out by the faculty management). In this way the respondent has a greater range of answers which gives the possibility of giving more clearly response. Collected data were analyzed using the Excel program and a software package for statistical analysis of quantitative and qualitative data of social research SPSS 21 (Statistical Package for the Social Sciences).
4. RESEARCH RESULTS

The first set of questions in the questionnaire referred to the structure by gender, age, degree and year of study and mode of financing studies. Of all respondents, 59% were female and 41% male. By age of 21-24 years there are 50%, 38% of those under 21 years, 10% of respondents aged 25-34 years, 2% of the respondents are 35 years old and more. First level attend 79% of the student population, and only 21% of second level of studies. The reason for the smaller number of respondents of the second level is that most students complete their education after the first level, some job seekers, some found employment, and some students despite the desire do not have opportunities to continue their studies.

At public institutions of higher education universities in Mostar, Sarajevo, Tuzla and Zenica students enroll in the status of the ordinary, extraordinary student and student DL. Fee on these universities is determined by the status of the student and is not same on all universities in the FB&H. More than half (55%) co-financed by the canton (public funds – budget funds), 44% of students are self-financed and 1% of students did not answer the question of funding the study.

Motives selection study and students' satisfaction studies are some of the basic factors of quality study. Offered reasons/motivations enrollment in the questionnaire are: the number of students enrolled in college, length of study, satisfaction of graduates, success of graduates, employment and academic status, location faculty, faculty building equipment, image and reputation of the faculty, study costs, interest for disciplines that are taught at the faculty, faculty websites, the possibility for international exchange (stay abroad), parents' wishes, advice from friends, a low evaluation criteria, a high assessment criteria, failed enter a second faculty, there was no entrance exam. Results of the analysis are shown in Figure 1 and Figure 2.

Figure 1: The secondary/primary reason enrolling the faculty

Source: author's treatment
Figure 2: Not reason enrolling the faculty

<table>
<thead>
<tr>
<th>Reason</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>No entrance exam</td>
<td>245</td>
</tr>
<tr>
<td>Failed enter another faculty</td>
<td>266</td>
</tr>
<tr>
<td>High evaluation criteria</td>
<td>235</td>
</tr>
<tr>
<td>Low evaluation criteria</td>
<td>279</td>
</tr>
<tr>
<td>Recommendation from a friend</td>
<td>207</td>
</tr>
<tr>
<td>The desire of parents</td>
<td>231</td>
</tr>
<tr>
<td>The possibility for international exchange (stays abroad)</td>
<td>192</td>
</tr>
<tr>
<td>Website of the faculty</td>
<td>228</td>
</tr>
<tr>
<td>Image and reputation of the faculty</td>
<td>141</td>
</tr>
<tr>
<td>Features faculty building for teaching</td>
<td>142</td>
</tr>
<tr>
<td>Location of faculty</td>
<td>161</td>
</tr>
<tr>
<td>Interest in disciplines that are studing at the faculty</td>
<td>59</td>
</tr>
<tr>
<td>The costs of studying</td>
<td>113</td>
</tr>
<tr>
<td>The success of graduates: employment and academic status</td>
<td>87</td>
</tr>
<tr>
<td>The satisfaction of graduates</td>
<td>123</td>
</tr>
<tr>
<td>Length of study</td>
<td>215</td>
</tr>
<tr>
<td>Number of students enrolled in faculty</td>
<td>267</td>
</tr>
</tbody>
</table>

Source: author's treatment

Expressed as a percentage of 300 students - 100% of the surveyed over 50% of them considered the following motives relevant to enter faculty: interest for disciplines that are studing at the faculty - 79.93%, the success of graduates in terms of academic status and employment status -70.41%, image and reputation of the faculty - 61.56%, satisfaction of graduates - 58.02%, 52.04% cost of studying and equipment of the building of the Faculty - 51.70%.

One of the question in the questionnaire referred to the expression of student satisfaction with the following criteria: quality of the teaching process (pedagogical work of professors and assistants), conditions for studying, support during the studying, the quality of curriculum (content of subjects), student workload (hours of instruction and preparation for exams), the work of the library (courtesy of staff, library holdings, reading), the number of graduates per generation, the work of the International Relations Office (courtesy of staff, timely information), the work of student services (courtesy of staff, working hours, valid information), the number of drop-students per generation and the tuition fee. Students are initially assessed their satisfaction scale of 1 to 5 (1 - completely dissatisfied, dissatisfied – in part 2, 3 - neither satisfied nor dissatisfied, 4 - partially satisfied, 5 - completely satisfied). Results of respondents on this issue are presented in the following table view.
Table 1: Average grade of respondents on the satisfaction of certain criteria related to attendance study

<table>
<thead>
<tr>
<th>Quality criteria</th>
<th>N</th>
<th>Average grade</th>
</tr>
</thead>
<tbody>
<tr>
<td>The quality of curriculum</td>
<td>300</td>
<td>3.5567</td>
</tr>
<tr>
<td>The work of the library</td>
<td>285</td>
<td>3.4877</td>
</tr>
<tr>
<td>The conditions for studying</td>
<td>300</td>
<td>3.4567</td>
</tr>
<tr>
<td>The support students during the teaching and learning</td>
<td>300</td>
<td>3.3467</td>
</tr>
<tr>
<td>The quality of the teaching process</td>
<td>300</td>
<td>3.3033</td>
</tr>
<tr>
<td>The number of graduates per generation</td>
<td>287</td>
<td>3.0976</td>
</tr>
<tr>
<td>The work of the International Relations Office</td>
<td>281</td>
<td>3.0747</td>
</tr>
<tr>
<td>The work of student services</td>
<td>292</td>
<td>2.8836</td>
</tr>
<tr>
<td>The student workload</td>
<td>300</td>
<td>2.8067</td>
</tr>
<tr>
<td>The number of drop-students per generation</td>
<td>284</td>
<td>2.6761</td>
</tr>
<tr>
<td>The tuition fee</td>
<td>291</td>
<td>2.6426</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
<td>272</td>
<td></td>
</tr>
</tbody>
</table>

Source: author's treatment

All 300 students surveyed identified in relation to these criteria: the quality of the teaching process, conditions for studying, support students during the studying, the quality of the teaching process, student workload valuing them an average of 3.5567, 3.4567, 3.3467, 3.3033 and 2.8067 respectively.

Based on the presented measures the average can be concluded that the students expressed the greatest satisfaction with the quality of the teaching process, the library's activities, conditions for teaching and learning, support during the teaching and learning, the quality of the curriculum, the number of graduate students and work of the International Relations Office.

As a measure correlation or agreement grades of criterias presented in table 1 calculated Pearson's coefficient of linear corelation. Correlation matrix for selected criterias and their grades is shown in Table 2.
Based on the presented correlation matrix, it can be seen that there is a statistically significant correlation between most of individual criteria by students. For decision-makers are important the following criteria: the work services’ student, student workload, the number of dropout students in the generation and the amount of tuition fees. All these criteria denoted as dissatisfaction measures and all have an average grade less than 3.
One of questions was the importance of information about the positive financial result (financial operations) faculty for students. The results are shown in Table 3.

Table 3: Attitudes toward the financial operations of the faculty

<table>
<thead>
<tr>
<th>The relevance of information about the positive financial result</th>
<th>Frequency</th>
<th>%</th>
<th>Cumulated series (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>No answers</td>
<td>9</td>
<td>3.0</td>
<td>3.0</td>
</tr>
<tr>
<td>Yes</td>
<td>158</td>
<td>52.7</td>
<td>55.7</td>
</tr>
<tr>
<td>Not</td>
<td>29</td>
<td>9.6</td>
<td>65.3</td>
</tr>
<tr>
<td>No opinion</td>
<td>104</td>
<td>34.7</td>
<td>100.0</td>
</tr>
<tr>
<td>Total</td>
<td>300</td>
<td>100.0</td>
<td></td>
</tr>
</tbody>
</table>

Source: author's treatment

For 52.7% of students, information about the positive financial results of the faculty is relevant. Only 9.6% of students are not considered relevant information about positive financial operations of the faculty, while 34.7% of respondents have no opinion on the financial operations, and 3% did not consider necessary to answer this question.

Students also gave level of (dis)satisfaction following activities carried out by the faculty management: the quality of strategic planning (innovation of the curriculum, the introduction of e-learning, etc.), quality of teaching (educational work professor/assistants, regular classes and consultation, modern infrastructure), internal procedures (up to date during the processing of student requests, monitoring of transience, improving enrollment policies, etc.), cost efficiency (finding the cheapest ways of achieving a particular goal), cooperation with state authorities, support students during the teaching and learning and student practice. Their satisfaction by the management efforts to improve the quality of the higher education institutions was graded 1 to 5 (1 - completely dissatisfied, dissatisfied – in part 2, 3 - neither satisfied nor dissatisfied, 4 - partially satisfied, 5 - in completely satisfied). The average grades of the respondents (dis)satisfaction mentioned activities are given in the Table 4.

Table 4: Average grade of students on the (dis)satisfaction with the activities carried out by the management faculty

<table>
<thead>
<tr>
<th>Activities by the management faculty</th>
<th>N</th>
<th>Average grade</th>
</tr>
</thead>
<tbody>
<tr>
<td>The quality of the teaching process</td>
<td>268</td>
<td>3.5187</td>
</tr>
<tr>
<td>The support students during the studying</td>
<td>267</td>
<td>3.2097</td>
</tr>
<tr>
<td>The internal procedures</td>
<td>268</td>
<td>3.0896</td>
</tr>
<tr>
<td>The strategic planning</td>
<td>268</td>
<td>2.9291</td>
</tr>
<tr>
<td>The cost efficiency</td>
<td>262</td>
<td>2.7863</td>
</tr>
<tr>
<td>The cooperation with state authorities</td>
<td>260</td>
<td>2.7192</td>
</tr>
<tr>
<td>The student practice</td>
<td>270</td>
<td>2.3370</td>
</tr>
<tr>
<td>Valid N (listwise)</td>
<td>259</td>
<td></td>
</tr>
</tbody>
</table>

Source: author's treatment

From the data presented in Table 4 are evident that approximately 10% of students did not answer this question in the questionnaire. Based on the answers of respondents stated it can be concluded that students evaluate management activities primarily through the quality of the teaching process, support to students during the teaching and learning process and activities relating to the internal procedures with average grades of 3.519, 3.209, 3.089 respectively.
When it comes to respondents' grades on the satisfaction/dissatisfaction with the activities conducted by the faculty of management, there is a statistically significant correlation between all combinations of assigned grades to individual activities of management at the 0.01 level, Table 5.

**Table 5: Correlations matrix of the grade of students on the (dis)satisfaction with the activities carried out by the management faculty**

<table>
<thead>
<tr>
<th></th>
<th>The strategic planning</th>
<th>The quality of the teaching process</th>
<th>The internal procedures</th>
<th>The cost efficiency</th>
<th>The cooperation with state authorities</th>
<th>The support students during the studying</th>
<th>The student practice</th>
</tr>
</thead>
<tbody>
<tr>
<td>The strategic planning</td>
<td>Pearson Correlation</td>
<td>1</td>
<td>.598**</td>
<td>.601**</td>
<td>.407**</td>
<td>.546**</td>
<td>.480**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>1.732</td>
<td>.821</td>
<td>.876</td>
<td>.542</td>
<td>.746</td>
<td>.696</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The quality of the teaching process</td>
<td>Pearson Correlation</td>
<td>.598**</td>
<td>1</td>
<td>.618**</td>
<td>.422**</td>
<td>.344**</td>
<td>.521**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>.821</td>
<td>1.088</td>
<td>.714</td>
<td>.446</td>
<td>.373</td>
<td>.599</td>
</tr>
<tr>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The internal procedures</td>
<td>Pearson Correlation</td>
<td>.601**</td>
<td>.618**</td>
<td>1</td>
<td>.484**</td>
<td>.459**</td>
<td>.518**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>.876</td>
<td>.714</td>
<td>1.229</td>
<td>.543</td>
<td>.529</td>
<td>.633</td>
</tr>
<tr>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The cost efficiency</td>
<td>Pearson Correlation</td>
<td>.407**</td>
<td>.422**</td>
<td>.484**</td>
<td>1</td>
<td>.475**</td>
<td>.460**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>.542</td>
<td>.446</td>
<td>.543</td>
<td>1.025</td>
<td>.500</td>
<td>.513</td>
</tr>
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<td></td>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The cooperation with state authorities</td>
<td>Pearson Correlation</td>
<td>.546**</td>
<td>.344**</td>
<td>.459**</td>
<td>.475**</td>
<td>1</td>
<td>.469**</td>
</tr>
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<td>Sig. (2-tailed)</td>
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<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>.746</td>
<td>.373</td>
<td>.529</td>
<td>.500</td>
<td>1.079</td>
<td>.537</td>
</tr>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The support students during the studying</td>
<td>Pearson Correlation</td>
<td>.480**</td>
<td>.521**</td>
<td>.518**</td>
<td>.460**</td>
<td>.469**</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>.696</td>
<td>.599</td>
<td>.633</td>
<td>.513</td>
<td>.537</td>
<td>1.215</td>
</tr>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The student practice</td>
<td>Pearson Correlation</td>
<td>.447**</td>
<td>.303**</td>
<td>.344**</td>
<td>.346**</td>
<td>.498**</td>
<td>.470**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>Covariance</td>
<td>.776</td>
<td>.417</td>
<td>.503</td>
<td>.463</td>
<td>.683</td>
<td>.683</td>
</tr>
</tbody>
</table>

**. Correlation is significant at the 0.01 level (2-tailed).
Source: author's treatment**
Activities like strategic planning, cost efficiency and cooperation with state authorities have received lower average grade because the students were explaining to their own incompetence to assess the activities, Figure 3.

Figure 3 - Comparative view the grade of students on the (dis)satisfaction with the activities of management

The surveyed students, 270 of them, is assessed activities of management faculty on student practice with an average score of 2.337. This relatively low average rating is a result of individual student grades dominated lowest grade 1, which gave 111 students, only 16 students for this activity management gave the highest mark 5. When you compare the grades that students are provided for student practice and the quality of teaching process, it can be concluded that students prefer pedagogical work employees, much less the acquisition of practical knowledge in the partner institutions of Faculty, Figure 4.
On the basis of this research in order to build a reference set of performance indicators of higher education institutions can be concluded that for prospective students the following information useful:

a) which disciplines are taught at the faculty,  
b) whether the curriculum is aligned with labor market needs,  
c) the image and reputation of the Faculty,  
d) the conditions for studying, equipped building of the faculty  
e) the support for students during the studying of teachers and staff support services (student services, library, the International Relations Office),  
f) student practice in partner companies of the faculty,  
g) the student workload,  
h) how many students from one generation of graduates,  
i) how soon after graduation, students are employed,  
j) the number of drop-students per generation,  
k) how many students continue their studies at the second level,  
l) what are the costs of study, and  
m) operates as a higher education institution.

5. CONCLUSION  
Higher education institution are obligated to measure and track performance. Tracking performance is important for higher education program financing and performance monitoring of selected institution’s program goals and higher education in general. The basis of performance measurement is information that institutions owns, acquires and processes. In order to be relevant, indicators need quality information basis for their measurement.
So, much of suggested useful information student can be quantified and then used to design a set of indicators for measuring the business performance of public higher education institutions in the FB&H. In this way the reference set of indicators would include:

a) the size of space per student for the implementation of the curriculum, the number of projectors, computers etc. in classrooms/faculty building, capacity and computer in the reading room, the number of books in the library - mandatory and additional literature, access to a digital library and scientific bases data, and the ability to e-filing examination,
b) the number of teachers in relation to the number of students,
c) the number of teachers employed full-time in comparison to the number of external associates
d) the number of employees in support roles faculty (student services, library, International Relations Office) in relation to the number of students,
e) the number of signed contracts with partner companies of the faculty in which students perform internships,

f) the number of students to practice under one contract,
g) the number of hours of instruction and preparation of exams,
h) the number of graduates in a generation,
i) the number of graduates who were employed in the first, second, or third year after graduation,

j) the number of students of second level in relation to the total number of students,
k) the number of dropout students in the generation,
l) the number of students who continued the study,
m) cost per student/study program,
n) positive/negative financial result.

The construction of a set of indicators of higher education institutions can compare their operations with other institutions in the same sector, their business compared to previous periods, and to identify possible problems based on changes in the value of indicator.

LITERATURE


THE IMPACT OF TAX STRUCTURES ON ECONOMIC PERFORMANCE: EVIDENCE FROM CROATIA AND TURKEY

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ABSTRACT
There is a very limited number of instruments at a government’s disposal when it tries to stimulate overall economic performance. One of these instruments is the tax structure. Moreover, at the macroeconomic level, since taxes are used to redistribute income they contribute to the economic growth of the country. Therefore, it is very important to analyse the way in which a country’s tax is structured as the shares of direct and indirect taxes in overall tax revenue and in GDP influence economic performance. The problem of establishing a tax system that will encourage economic growth is especially evident in the recent years due to the consequences of global economic crisis and especially in those countries with very low or negative economic growth rates.

The aim of this paper is to examine the tax systems of two countries: Croatia, as a new European Union Member State and Turkey as Candidate Country. In this paper, the authors analyze the revenues from direct and indirect taxes in the period from 2002 to 2013 and their impact on economic growth. The analysis will primarily be focused on revenues from corporate income tax, personal income tax and VAT.

Keywords: Croatia, economic performance, tax structure, Turkey

1. INTRODUCTION
In the last forty years, there has been an increasing need for changes in the way taxes are perceived i.e. their place and role in the social, economic and political life, the structure of tax revenues, the amount of the tax burden and the share of tax revenues in GDP. The place and role of each tax within the tax system differs from country to country and depends on the objectives of taxation. Various tax forms affect decisions regarding savings, labor supply, investment in human capital, enterprises’ production decisions, creation of new jobs, investment and innovation. However, the decision-making is not just based on the tax levels, but on the way in which these taxes are introduced in the tax system and the way they are implemented in the framework of a specific economy. Therefore, the tax structure plays an important role in the functioning every country's economy.

The effects of tax levels and the structure of taxes on the behavior of economic entities are reflected in the standard of living. Acknowledging this has led many countries, especially those more developed, to carry out structural reforms of their tax systems in the last decade. The analysis of the effects of the changes in the tax structure on economic growth is of importance to tax policy creators and decision-makers and as such, is very important in the research of how to best direct the tax structure towards encouraging economic growth. However, in practice, it is difficult to completely separate the analysis of the overall tax level and that of the tax structure. In fact, very often is not possible to determine whether the positive (or negative) effects on economic growth are related to the changes in the general level of taxes or to the changes in the tax structure. In view of the above said, the aim of this
paper is to analyze the tax structures of Croatia and Turkey, as well as their economic growth rates.
The rest of the paper is organized as follows: Section 2 gives an overview of the literature linking tax structures and economic growth, thus providing theoretical background; Section 3 gives the analysis of tax revenues and output growth in Croatia and Turkey; and finally Section 4 gives concluding remarks and recommendations for future research.

2. LITERATURE REVIEW
The empirical research in the area of the interdependence of tax structure and economic growth are, to a large degree, inspired by the theoretical notions that some taxes have negative effects on economic growth. The first empirical studies that included fiscal variables in growth regressions were those by Barro (1989, 1991). In these studies, among other variables, he analyzed the ratio between real government consumption and real GDP as a regressor, and found significant negative correlation with growth.

Plosser (1992) calculated the correlation between the GDP growth rates and a number of variables for OECD countries. The calculation showed the strongest empirical link ever between taxation and growth. It was found that the share of revenues from personal income and corporate income tax in GDP has a correlation of -0.52 with the GDP growth rate.

Leibfritz, Thornton and Bibbee (1997) included three different measures of effective tax rate (average tax rates, marginal tax rates and average tax rates of direct taxes) in the regression of average growth rates in OECD countries in the 1980–1995 period. The results showed that a 10% increase in the tax rates will be followed by a 0.5 percentage point decrease in growth rate, with direct taxes reducing growth more than indirect taxes. Additional research on similar issues were conducted by Dowrick (1993) and de la Fuente (1997). These authors were more concerned with the general question of how the structure of fiscal policy affects growth. In particular, they investigated the relationship between the growth rate and the structure and level of public sector spending. In his research, Dowrick (1993) included several OECD countries and found that in these countries, personal income tax has a negative impact on growth, while corporate income tax has no effect.

Kneller et al. (1999) divided the taxes into distortive (income tax and property tax) and non-distortive (consumption taxes) and the expenditures into productive and non-productive expenditures. They found that income and property taxes reduce growth, and that consumption taxes do not.

In more recent times, Widman (2001) investigated the impact of tax structures on growth using data for 23 OECD countries for 1965 to 1990. She applied the methodology developed by Levine and Renelt (1992), but used four basic variables (initial income, the share of investment in GDP, population growth and the average tax rate (the share of tax revenue in GDP)). She analyzed the shares of different tax instruments in revenues (corporate income tax, personal income tax, property tax, sales tax on goods and services and tax on wages). The author concluded that the share of tax revenues from personal income tax has a negative impact on economic growth as well as on the progressivity of the tax system.

Similarly, Padovano and Galli (2002) found a negative effect of the marginal tax rate and cash tax progressivity on economic growth in a panel of 25 industrialized countries for 1970 to 1998. The negative impact of progressivity on entrepreneurial activity is one of the conclusions made by Gentry and Hubbard (2000). Schwellnus and Arnold (2008) and Vartia (2008) calculations showed a negative impact of corporate income tax on the productivity of companies and industries. The calculation was based on a large set of data for companies and industries throughout OECD countries. Similarly, Lee and Gordon (2005) found a significant
negative correlation between the statutory corporate income tax rates and economic growth for 70 countries during the 1970 – 1997 period. In his paper, Arnold (2008), on a panel of 21 OECD countries over 35 years, came to the results showing that higher proportions of corporate income tax and personal income tax are associated with significantly lower economic growth in relation to those on consumption and property. Moreover, when comparing corporate income tax and personal income tax, the former is associated with lower economic growth than the latter. Furthermore, by comparing consumption tax and property tax, the author showed that property taxes are associated with higher economic growth than those on consumption. Similar research results can be found in the work of Johansson et al. (2008). On the other hand, Xing (2010) disputed such results and stated that the assumptions Arnold (2008) and Johansson et al. (2008) used in their method may not be well suited for the analyzed data set. The mentioned method, the Pooled Mean Group Estimator, assumes that long-term relations between the variables are homogeneous in the analyzed set of countries. In challenging the validity of the assumption on homogeneity, Xing (2010) repeated the estimations conducted by Johansson et al. (2008) using slightly different specifications. Based on the differently set PMG estimates, the author concluded that income tax, corporate income tax and consumption taxes have a greater negative impact on GDP per capita of than property tax. However, Xing (2010) could not find solid evidence to further identify exactly which tax, consumption tax, income tax or corporate income tax has the strongest, and which the weakest negative impact on GDP per capita.

Within these findings, they concluded that an increase in corporate income tax (financed through the increase in consumption tax and property tax) has a greater negative effect on GDP per capita than a similar increase in personal income taxation. Moreover, in case of consumption tax and property tax increase (income tax and corporate tax reduction), a higher economic growth can be expected in the long run, where the positive impact of the increase in the property tax is significantly higher than that of consumption tax. Their results indicate that a revenue - neutral shift from personal income and corporate income tax to other tax forms has an impact on the increase in GDP per capita of 0.25% - 1% in the long run. Acosta-Ormaechea and Yoo (2012) observed 69 countries consisting of high, middle and low-income countries using the Pooled Mean Group estimator during the period from 1970 to 2009. The aim of the study was to determine whether there were differences in the impact of tax structures on economic growth in countries depending on their level of development. They found similar results as previous studies for high and middle-income countries, while the results for low-income countries were not significant.

For all these reasons, it is very important that, prior to implementing tax reforms, tax policy creators foresee what impact the changes in individual types of taxes will have on overall economic performance.

3. ANALYSIS OF TAX REVENUE AND OUTPUT GROWTH IN CROATIA AND TURKEY

Croatia became a member of the European Union on July 1, 2013. This was preceded by a lengthy process of adjustment and harmonization of the tax system with EU rules and requirements. This is especially true of indirect taxes (VAT and excise duties). On the other hand, Turkey is a candidate country, and is still in the process of adapting its economy EU requirements. In the field of indirect taxation legislation, Turkey’s value added tax (VAT) is still not in line with the acquis. The structure, exemptions, special schemes and the scope of reduced rates remain to be further aligned (European Commission, 2014). However, the Turkish taxation system is similar to that of the EU Member States.
In the last 10 years, the Croatian and Turkish tax systems have been undergone various tax reforms. The primary goal of any tax reform is to increase tax revenue, but in the recent years, due to the global economic crisis, tax reforms have been implemented in order to simplify the tax system and to avoid the tax burden of economic entities and general population. These reforms should result in higher employment and higher consumption i.e. an increased economic growth rate. Moreover, an expected long-term outcome of tax reforms is an increase in revenue by broadening the tax base and improving compliance fundamentals.

The Croatian and Turkish tax structures are composed of the main taxes: value added tax (VAT), personal income tax (PIT), corporate income tax (CIT) and social security contributions (SSC).

The data used in this paper are annual data covering the period from 2002 to 2013 for Croatia and Turkey. The data on tax revenues have been taken from the official webpages of the Croatian Ministry of Finance and the Turkish Ministry of Finance in domestic currency. The Croatian Kuna was converted to Euro based on the average annual middle exchange rate of the Croatian National Bank, while the Turkish Lira was based on the average annual middle exchange rate of the European Central Bank. The data for Croatian GDP have been taken from the Eurostat official webpage, while for Turkey from the General Directorate of Revenue Policies webpage.

The structure of tax in Croatia and Turkey, i.e. the shares of tax revenues from main taxes in total tax revenue for 2013 are presented in Figure 1.

In 2013, Croatia and Turkey had a similar tax structure, i.e. they have a consumption based tax system. A major part of tax revenues was collected through the tax on consumption, whose main element is the Value Added Tax. The data are not surprising, given that Croatia and Turkey, according to the World Bank (World Bank, 2014), have similar values of GDP per capita and that most of the countries showing similar economic performance as Croatia and Turkey base their tax systems on consumption tax. In 2013, the share of VAT in total tax revenues amounted to 36.06% in Croatia and 30.88% in Turkey. As far as direct taxes go
(income tax and corporate tax), the situation is different. There is a noticeable difference in the shares of income tax in total tax revenues. Namely, the share of income tax in Turkey is significantly higher. The reason for this, lies in the Turkish progressive taxation of income (4 tax rates, i.e. four tax brackets), and the constantly present high unemployment rate in Croatia, which reduces income tax revenues.

**Figure 2:** Tax structure in Croatia (2002 - 2013) as % of GDP (Author’s calculation)

**Figure 3:** Tax structure in Turkey (2004 - 2013) as % of GDP (Author’s calculation)

The previous two graphs show the structures of tax in Croatia and Turkey for the period 2002 - 2013. The total tax burden as % of GDP is significantly higher in Croatia than in Turkey

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34 The data for Turkey are not available for the period before 2004.
for the observed period. It can be assumed that the tax burden in Turkey will increase once it becomes an EU member state due to the adjustment of its tax system to EU requirements (primarily full harmonization of VAT and excise duties). Croatia, as a member of the European Union, with a 33% average share of tax revenues in GDP in the observed period still lags behind the EU average. Moreover, as in 2013, the consumption tax has also the highest share in the tax structure during the observed period and is followed by income tax and corporate tax.

Corporate income tax

The Turkish Corporate Tax is levied on income of corporations. The corporate tax rate is 20% (it was 30% prior to 2006). The Croatian corporate tax rate is also 20%.

The following table shows the shares of revenue from corporate tax in GDP for Croatia and Turkey.

Table 1: Corporate income tax as % of GDP in Croatia and Turkey (2002 – 2013)(Author’s calculation)

<table>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Croatia</td>
<td>1.97</td>
<td>1.86</td>
<td>1.75</td>
<td>2.06</td>
<td>2.43</td>
<td>2.74</td>
<td>3.04</td>
<td>2.85</td>
<td>1.95</td>
<td>2.19</td>
<td>2.33</td>
<td>1.93</td>
</tr>
<tr>
<td>Turkey</td>
<td>n.a.</td>
<td>n.a.</td>
<td>1.56</td>
<td>1.52</td>
<td>1.46</td>
<td>1.63</td>
<td>1.79</td>
<td>1.89</td>
<td>1.87</td>
<td>2.02</td>
<td>1.84</td>
<td>1.61</td>
</tr>
</tbody>
</table>

Note: n.a. – data not available

The share of revenues from corporate tax in GDP is about 2% for both countries in the observed period. The small share of these revenues in GDP are the result of increasing globalization, increase in international mobility of companies, as well as the fact that the statutory income tax rate of 20% is high in comparison to other countries. This leads to the avoidance of paying taxes in the country i.e. moving business operations to countries with lower rates of corporate income tax. Moreover, in order to reduce distortions in the payment of taxes and bring tax avoidance to a minimum, the corporate tax rate should be either equal or approximately equal to the highest rate of personal income tax.

Personal income tax

In Turkey, the highest rate of income tax was reduced from 40% to 35% at the end of 2004. In April 2006, the structure of the PIT schedule was rearranged by reducing both the tax rates and the number of tax brackets. The PIT schedule now consists of four tax brackets instead of five brackets and the new tax rates are 15, 20, 27 and 35 per cent, respectively.

The Croatian income tax system has often been changed since its introduction in 1994. The most important change occurred in July 2010 when three tax rates (12%, 25%, 40%) were introduced instead of four (15%, 25%, 35% and 45%).

The following table shows the share of revenue from income tax in GDP in Croatia and Turkey.

Table 2: Personal income tax as % of GDP in Croatia and Turkey (2002 – 2013)(Author’s calculation)

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Croatia</td>
<td>3.84</td>
<td>3.10</td>
<td>3.10</td>
<td>2.90</td>
<td>2.99</td>
<td>3.08</td>
<td>3.10</td>
<td>3.13</td>
<td>2.81</td>
<td>2.79</td>
<td>2.99</td>
<td>3.13</td>
</tr>
<tr>
<td>Turkey</td>
<td>n.a.</td>
<td>n.a.</td>
<td>3.18</td>
<td>3.14</td>
<td>3.80</td>
<td>4.07</td>
<td>4.02</td>
<td>4.03</td>
<td>3.62</td>
<td>3.64</td>
<td>3.58</td>
<td>3.54</td>
</tr>
</tbody>
</table>

Note: n.a. – data not available
The share of revenues from personal income tax in GDP in both analysed countries in the observed is greater than the share of revenue from corporate tax, but still this share is much lower than that of VAT (see Table 3). The share of the personal income tax in GDP in the observed period was on average was 1% higher in Turkey than in Croatia. This difference decreased in the last two years. However, it is also evident that there was a reduction in the share of personal income tax in GDP in both countries after 2009 as a result of the global economic crisis and increased unemployment. Furthermore, there is the generally present issue of high level of income inequality and dependence on a relatively small number of big taxpayers in field of tax revenues from direct taxes. In addition to this, there are the problems such as a low willingness of the population to pay taxes, a larger informal sector and weaker administrative capacity.

The main problem in countries such as Turkey and Croatia is the lack of the efficiency and functioning of the tax systems. Therefore, it is necessary to conduct reforms in direct taxation (personal income tax and corporate income tax) to improve incentives for savings and investment for small and large companies.

**Value Added Tax**

In Turkey, all deliveries of goods and services, in the context of commercial, industrial, agricultural and professional activities and goods and services imported and deliveries and services arising from other activities are subject to VAT. The VAT rates are: 18% (standard rate), 8% and 1% (reduced rates). The standard VAT rate applies to all supplies of goods or services, unless a specific measure provides for a reduced rate or exemption. Some goods and services such as supplies of financial transactions, water for agriculture, the supply of unprocessed gold, foreign-exchange money, stocks and bonds, duty stamps, delivery of goods or performance of services in free-trade zones are partially exempt. Examples of fully exempt supplies of goods and services are exports of goods and services and international transport. The tax rate for newspapers, food such as bread and milk is 1% as well as for used cars, while it is 8% for other food items, medications, books and cultural events.

In Croatia, the VAT system was introduced on January 1, 1998 as a replacement for the multistage turnover tax. The basic system was also developed in line with the theoretical recommendations –a uniform tax rate of 22% was applied on a broadly defined tax base, with a small number of standard exemptions and no zero rates, except those for export. As such, it was similar to EU legislation. In mid-2009, the rate was raised to 23%, and in early 2012 to 25%, which makes Croatia one of the countries with the highest rate of VAT in the European Union. A zero rate was introduced at the end of 1999; it was then abolished at the beginning of 2013 when it was replaced by a reduced rate of 5% making the Croatian VAT system fully compliant with the Directive 2006/112 / EC. A reduced rate of 10% was introduced in early 2012, and by 2014 it amounted to 13%.

The following table shows the share of revenues from value added tax in GDP in Croatia and Turkey.

<table>
<thead>
<tr>
<th>Year</th>
<th>Croatia</th>
<th>Turkey</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>13.79</td>
<td>n.a.</td>
</tr>
<tr>
<td>2003</td>
<td>12.11</td>
<td>n.a.</td>
</tr>
<tr>
<td>2004</td>
<td>11.91</td>
<td>4.89</td>
</tr>
<tr>
<td>2005</td>
<td>11.93</td>
<td>4.66</td>
</tr>
<tr>
<td>2006</td>
<td>11.87</td>
<td>5.42</td>
</tr>
<tr>
<td>2007</td>
<td>11.71</td>
<td>5.12</td>
</tr>
<tr>
<td>2008</td>
<td>11.88</td>
<td>4.94</td>
</tr>
<tr>
<td>2009</td>
<td>11.20</td>
<td>4.93</td>
</tr>
<tr>
<td>2010</td>
<td>11.49</td>
<td>5.60</td>
</tr>
<tr>
<td>2011</td>
<td>11.35</td>
<td>5.87</td>
</tr>
<tr>
<td>2012</td>
<td>12.31</td>
<td>5.17</td>
</tr>
<tr>
<td>2013</td>
<td>12.20</td>
<td>5.60</td>
</tr>
</tbody>
</table>

Note: n.a. – data not available
In both countries, indirect taxes make up for a significant share in GDP, especially VAT. The share of VAT in GDP is significantly higher in Croatia. As previously mentioned, the Turkish VAT system is still significantly different from the one in Croatia. Turkey grants many exemptions and reduced rates. Its standard rate is substantially lower, resulting in lower revenues from VAT. Furthermore, other consumption taxes, such as excise duties, make up for a significant portion of revenues in Turkey. As a result, the share of the overall tax burden through consumption tax is over 10% of GDP. In both countries, significant reliance on consumption taxes came about as a result of the inability to collect income tax and corporate tax in significant amounts.

4. CONCLUDING REMARKS AND RECOMMENDATIONS FOR FURTHER RESEARCH – dodati recomandations for further reserch

The differences in the tax structures among countries are the result of their cultural, political and economic differences. All changes in tax structures should be analysed in relation to their overall impact on the economy. The introduction of different types of taxes and their relative importance in the tax systems differ significantly among countries. Furthermore, changes in a country’s tax structure may also influence the economy as a whole or some of its segments, such as savings or investments. Croatia, as a member of the European Union and Turkey, as a member of the OECD and an EU candidate country, show similarities in their tax structures. The tax systems of both countries rely significantly on revenues from consumption tax (VAT), and have relatively low revenues from personal and corporate income tax. Although Croatia has a higher GDP per capita than Turkey, Turkey has had a higher rate of GDP growth in the recent years. Nevertheless, both countries should adapt their tax structures in order to encourage economic growth. They should lower consumption taxes, reform personal income and corporate tax systems (lower tax rates, granting incentives and benefits) in order to attract investments in highly profitable industries, increase production and employment, and prevent the outflow of capital to other countries. In this paper authors analyzed and compared the tax structure of Croatia and Turkey, which has not been sufficiently researched in the economic literature. Because of that further research in this area is needed. Future research will include other forms of taxes, such as excise duties, property taxes and social security contributions in the target countries.

LITERATURE


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MICROCREDIT IN ITALY: SEARCHING FOR A MODEL

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ABSTRACT
The main purpose of this analysis is to identify a “best practice” benchmark for the microfinance phenomenon in Italy. Starting from a review of current legislation, I continue the analysis with particular reference to the various types of non-bank lenders in the market and the respective different operating methods used to provide their services. The analysis shows that although each of these operators is able to provide effective solutions in terms of financial inclusion, none is able to offer actual solutions in terms of financial sustainability. No model was found to be uniquely superior to others. Moreover, despite the wide institutional variety, a best practice benchmark cannot be currently identified. Drawing on this research, I identify three main objectives of the microfinance industry: (i) Provide access to capital in order to help vulnerable individuals and families at risk of sliding deeper into poverty and social and financial exclusion; (ii) Provide financial literacy, monitoring, and tutoring in order to avoid excessive debt load; (iii) Prevent and fight the phenomena of usury.

I also identify common general issues faced by microcredit: (i) The lack of new and innovative strategies of risk management that also include soft information; (ii) Developing the ability to face high costs which are mainly due to activities aimed at collecting intangible information, promoting financial literacy and guiding the beneficiary throughout the life-time of the loan; (iii) Achievement of the sustainability of the business over time. In order to address the issues highlighted in this analysis, especially achieving the financial sustainability of microfinance institutions, the intervention of the legislator is needed. Indeed, the legislator should not solely focus on the characteristics of the beneficiary but should also help design a viable “loan delivery process” in order to define the key elements of the process of microcredit (i.e., monitoring, scoring, tutoring).

Keywords: Financial exclusion, Financial inclusion, Financial literacy, Loan, Microcredit, Microfinance, Unbanked

1. INTRODUCTION
The practice of microcredit, widespread in Italy since the early years of this decade, enables people experiencing poverty and social vulnerability, those without collateral, to have access to credit. Microcredit is also often used as a means of encouraging an increase in self-employed work (frequently assisting the transition from unemployment to self-employment) and to the formation and growth of small businesses, playing an important role in the implementation at a European level of EU Strategy 2020 (a continuation of the Lisbon

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35 For an updated estimate of the incidence of relative and absolute poverty in the Italian population, see Istat, (2014), Poverty in Italy. The estimate of the incidence of relative poverty (the percentage of families and poor people) is calculated on the basis of a conventional threshold (poverty line) that identifies the value of consumption expenditures below which a family is defined as poor in relative terms. The relative poverty threshold for a family of two components is equal to the average monthly expenditure per person in the country, which in 2013 was €972.52 (-1.9% compared to the value of the threshold in 2012). A family of two people with monthly spending at or below this value is classified as poor. For different sized families the value of the line is obtained by applying an appropriate equivalence scale which takes into account the economies of scale as the component numbers increase. The incidence of absolute poverty is calculated on the basis of a poverty line corresponding to the minimum monthly expenditure necessary to acquire the basket of goods and services which, in the Italian context and for a given family, is considered essential to a minimally acceptable standard of living (see Istat, (2009), Methods and Standards; the measure of absolute poverty). Families are classified as absolutely poor if they have a monthly expenditure at or below the threshold value (which differs according to the size and age composition of the family and the geographic spread and demographic size of the municipality in which they are resident). In 2013, 12.6% of families were classified as relatively poor (a total of 3 million 230 thousand) and it was 7.9% in absolute terms (2 million 28 thousand); 16.6% of the population (10 million 48 thousand) were in relative poverty while those in absolute poverty represented 9.9% of the population (6 million 20 thousand).
Strategy concluded in 2010 for growth, jobs and the promotion of social integration\textsuperscript{36}. At a time when the financial crisis is still acute and the grip of the credit crunch is ever tighter, microcredit plays an increasingly central role in promoting the financial inclusion\textsuperscript{37} of those considered to be “un-bankable”. In recent years, microcredit has undergone a significant development in Italy\textsuperscript{38}, but its failure to become widespread is largely due to structural problems, including the difficulty faced by operators in defining business models as financially sustainable\textsuperscript{39} as well as to a fragmented legislative framework\textsuperscript{40} in which there is a delay in the adoption of secondary legislation implementing primary laws\textsuperscript{41}. The main purpose of this analysis is to identify a “best practice” benchmark for the phenomenon of microfinance in Italy. Starting from a review of current legislation, I continue the analysis with particular reference to the various types of non-bank lenders\textsuperscript{42} in the market and the respective different operating methods used to provide their services. The report Public and private policies for the provision of microfinance services, which was presented in 2011 by ABI in collaboration with the Ministry of Labour and Social Policy, is the result of a joint project aimed at analyzing the financial situation of families and aspects of vulnerability\textsuperscript{43} related to developments in finance and credit. This has allowed us to map 712 microfinance operators active in Italy: 397 consortia (55.76%), 224 banks (31.46%), 62 associations/non-profit foundations\textsuperscript{44} (8.71%), 21 public institutions (2.95%) and 8 non-banking companies (1.12%)\textsuperscript{45}.

\textsuperscript{36} Such loans offer an important means to encourage entrepreneurship through self-employment and micro-enterprises, in particular among women and minorities. This instrument favours not only competitiveness and entrepreneurship, but also social inclusion”, European Commission, (2006). COM (2006) 349, Implementing the Community Lisbon Programme: Financing SME Growth - Adding European Value, p. 7.


\textsuperscript{38} The seventh Report on Microcredit in Italy, published within Fiducia nel credito – Esperienze di microcredito per l’impresa ed il sociale, Donzelli, 2013, estimated in 2011 a growth of 42 % compared to the amount of credit granted in the previous year. The eighth Report on Microcredit in Italy, published within Microcredito e Inclusione. I presti alle famiglie e alle imprese non bancabili, Donzelli, 2014, estimated in 2012 more than 12 thousand microloans for a total amount of 115 million Euro. Also at European level surveys indicate a steady increasing trend of the scale (both in terms of number as well as total volume) of microfinance provision in 2012 and 2013, compared to 2011. See European Microfinance Network, (2014). Overview of the Microcredit Sector in European Union 2012-13, p. 19 ff..

\textsuperscript{39} Financial performance and sustainability still is a complex issue, both in Italy and in Europe. See Overview of the Microcredit Sector in European Union 2012-13, p. 11.

\textsuperscript{40} Since 2007 Europe Commission invites Member States ”to adapt as appropriate national institutional, legal and commercial frameworks necessary to promote a more favourable environment for the development of micro-credit” (see COM (2007) 708 final, p. 2). See also Stefanelli, M.A., (2012). L’inadeguatezza del regolamentazione giuridica del microcredito a livello globale e le mancate sfide del sistema creditizio, in Studi di Diritto dell’Economia e dell’Impresa in Memoria di Antonio Cicognani, p.653.


\textsuperscript{42} As for the banking industry, please refer to ABI, the Ministry of Labour and Social Policy, (2011). Public and Private Policy for the provision of microfinance services. Notebooks of Social Research no. 14, p. 22 ff.

\textsuperscript{43} The definition of vulnerability is “an indicator of greater or lesser exposure of individuals to be adversely affected as a result of a given event. Therefore, it refers to the effects of a harmful event on individuals, not necessarily identify trajectories of impoverishment and social exclusion, but rather indicates the degree of exposure to negative events that an individual has given his situation. In this context, for financial vulnerability is possible to understand the degree of exposure of individuals to external events or errors in individual choices, given their starting conditions and their economic situation, family, work, health. Recognize the subject as vulnerable means to take into account at the time of the service by the bank or broker, the particular socio-economic conditions of the customer, providing the contracts that the more adaptable to changing family / work”. See Public and private policies for the provision of microfinance services, cit., p. 12 and p. 41 where there are more references to the economic doctrine.

\textsuperscript{44} It is necessary to point out that microfinance is meant, according to the definition adopted by the United Nations as, “loans, savings, insurance, transfer services, microcredit loans and other financial products targeted at low-income clients”; the main actors operating in Italy have established a shared definition of microfinance as “the set of services of credit, savings, payment and transfer offered by banks and other intermediaries in terms of sustainability aimed at facilitating the financial inclusion of vulnerable people” (see ABI, the Ministry of Labour and Social Policy, (2009), Analysis of the financial situation of Italian families). In both cases the definition is broader than the solely micro component.

\textsuperscript{45} With regard to the European perspective, “The European microfinance sector is still characterized by a wide range and diverse set of institutions active in the market”. See Overview of the microcredit sector in the European Union, cit., p. 10 and p. 28 ff.
Figure 1: Microfinance operators active in Italy

The analysis shows that although all of these operators are able to provide effective solutions in terms of financial inclusion, none are able to offer actual solutions in terms of financial sustainability. Furthermore, some types of legal operations analyzed are not fully compliant with the regulations in force, nor are they allowed to operate over the entire range of products that microcredit would require. “It thus appears that among the models of non-bank microcredit in Italy there is still no best practice point of reference that is absolutely and indisputably able to produce the best results and to completely fulfill the mission of microfinance. While on the one hand this evidence seems to show a weakness of the microcredit sector in Italy, on the other hand it confirms the institutional richness and variety of the models, which could in the future produce very effective results if they were organized and integrated in a synergetic way, using the different local specialisations and strengths of the various models in the field.”

2. THE CURRENT MICROCREDIT LEGISLATION IN ITALY

Legislative Decree 141/2010 (pursuant to the authority granted by Community law 7 September 2009, n. 88 for the transposition of Directive 2008/48/EC, as amended and supplemented by Legislative Decree 218/2010) and Legislative Decree 169/2012 have profoundly innovated the rules of financial intermediaries contained in Title V CBA (Consolidated Banking Act), limiting the financial activities subject to regulation and redefining the objective scope of the discipline: “the exercise of loans granted to the public in

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46 Regarding the concept of financial sustainability, see Public and private policies for the provision of microfinance services, cit., p. 10. See also the executive summary of the workshop organised by the Foundation Giordano Dell’Amore, The Challenge of Sustainable Italian Microfinance Institutions, 9 May 2012.


any form is reserved for authorized financial intermediaries enrolled in the appropriate register held by the Bank of Italy.”

Originally, the regulation of financial intermediaries essentially involved functioning as a census of operators: in particular, the aim of the legislator was to obtain, in the fight against organized crime, specific evidence of entities operating in the financial market. Subsequently, in light of the growing importance of these bodies in the financial market, the legislator also decided to submit financial intermediaries to the provisions of the Banking Act, prescribing the system of prior authorization by the Bank of Italy and forms of so-called equivalent supervision, albeit graded according to the scale of these operations in accordance with the principle of proportionality. The trend line of this new regulatory framework is to restrict the scope of implementation, focusing on those bodies whose activities highlight the need to protect consumers and safeguard the stability of the financial market. It is in this broader context of “actors in the financial sector” (Title V CBA), that legislator introduced the discipline of microcredit in Italy for the first time, in the amendment to art. 111 CBA. A brief description of the main objectives of the regulation of financial services follows in the figure below.


Microcredit activities can take the form of “productive microcredit”, credit support aimed at start-ups or the consolidation of microenterprises or forms of self-employment, and “social microcredit”, financial assistance for the purchase of basic goods and services, social welfare loans that can cover the costs of health care, education and job placement, or expenses arising

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50 These forms of supervision are similar to those imposed on intermediaries (banks, asset management companies, investment firms, etc.) with regards to preventive controls (requests for enrollment in the register, and presentation of the programme of activities and organizational structure), adequacy of assets and risk containment, equity interests (shares to be held), administrative rules and accounting procedures and internal controls.
from a situation of sudden and temporary vulnerability. In the first case it is an activity of funding “to any person or partnership or limited liability company simplified in art. 2463-bis of the Italian Civil Code, or to associations or cooperatives, for starting or pursuing self-employment or microenterprise”, with specific features: funding must be i) for amounts not exceeding 25,000 Euros and without collateral; ii) aimed at the establishment or development of entrepreneurial initiatives or inclusion in the labor market; iii) accompanied by the provision of ancillary assistance and monitoring services. In the second case it is an activity of financing “for the benefit of individuals with a particularly vulnerable economic or social situation” which meets specific conditions: funding must be i) no more than 10,000 Euros ii) not secured by real assets iii) accompanied by the provision of ancillary services to the family budget, iv) granted for the purpose of social inclusion, v) provided on terms more favorable than those prevailing in the market. For the purposes of paragraph 3-bis of art. 111, “social” microcredit may be granted only by operators who are also involved in the activity of “productive” microcredit. Notwithstanding the provisions of art. 106, these two specific types of financing activities may be exercised by persons enrolled in a register maintained by an appropriate body, “legally recognised under private law and organised as an association with organizational, statutory and financial autonomy”. Inclusion on the register is subject to a number of conditions regarding the legal form (corporation, limited partnership, limited liability partnership), the paid-up capital (no less than the amount to be determined under paragraph 5 of art. 111), the integrity requirements of the controlling or relevant shareholders, the requirements of integrity and professionalism of corporate officers, the social objective, which should be limited only to those activities referred to in paragraph 1 of art. 111 as well as their ancillary and instrumental activities, the presentation of a program of activities.

As a further exemption from the provisions of art.106, the activity of microcredit may also be exercised, at “rates adjusted to merely allow the recovery of the costs incurred by the creditor”, by certain non-profit organizations, recorded in a separate section of the register referred to in paragraph 1 of art. 111. However, this is only the case for “social” microcredit and not for “productive” microcredit. The characteristics of these non-profit legal entities will be contained in the implementing rules to be issued by the Ministry of Economy and Finance, after consultation with the Bank of Italy, pursuant to paragraph 5 of art.111, still pending. However, all the legal forms of non-profit organizations can henceforth be brought within the definition of “non-profit legal entities”: associations (recognized or unrecognized),

51 Note that although the requests for microcredit stem from different needs, the responses offered in the form of productive and social microcredit are characterized by a strong relationship of interdependence which is sometimes complementary. While those who receive a productive microloan often use a small part of the credit received to stabilize their personal/family situation, those who receive a social microcredit, on the other hand, are not only able to cope with a temporary financial and emergency need, but, in satisfying the latter, can often avoid triggering a negative loop which could damage their capacity to work. Since 2012 the European Microfinance Network (EMN) has adopted the following classification: “This edition of the survey therefore proposes a definition for the first time for a differentiation of the lending part of microfinance activities into two categories: (1) microenterprise lending and (2) social inclusion lending. This distinction should be seen as a first step towards a more focused discussion on institutional blueprints and lending models for microfinance in Europe.” See Overview of the microcredit sector in the European Union, (2012), p. 14 and p. 39 ss. The European Union recognizes this distinction, for example in the report of the European Commission COM (2012) 769 final, 18 December 2012, p. 4 where it is reported that “microcredit may be only available to ‘micro-entrepreneurs’, self-employed people seeking to finance small businesses. It may also focus only on other groups such as socially excluded people trying to cope with emergencies, fund education, or even acquire basic household assets”.

52 See art. 111 co. 1 CBA.
53 See art. 111 co. 3 CBA.
54 See art. 113 CBA. “The Bank of Italy will therefore not oversee individuals but the correctness of the actions of the entity, which must report violations committed by members, for the application of the relevant sanctions” (see Goffredo, M.A., Berneri, F., cit., note 14). This body, which is entrusted with the task of ensuring the proper maintenance of the list of microcredit organisations, will be sustained by the contributions received from the members, which will be determined within the limit of 1% of the amount of the total loans granted. The structure, powers and mode of functioning of the body, as well as the requisites of its members and the criteria and procedures for their appointment and replacement, shall be governed by the Ministry of Economy and Finance, after consultation with the Bank of Italy.
55 See art. 111 co. 2 CBA.
56 See art. 111 co. 4 CBA.
foundations and committees (although the latter is only a theoretical possibility, as the committee is an associative entity that is established to reach a definite objective in a given period of time, and therefore not a long-term body as providers of microcredit must necessarily be) as well as mutual companies (i.e., companies that pursue the generation of one or more type of economic benefit for its members other than profit, that is different from the generation of a profit to be divided among the shareholders or that is available to the individual. The main social type amongst these companies is the prevalently mutual cooperative).

3. MICROCREDIT MARKET PLAYERS IN ITALY

Coming to an overview of the phenomenon of microcredit in Italy, with particular reference to the various types of market players and the respective different operating modes with which they offer their services, there are essentially two types: (i) one based on “triangulation”, which generally uses a bank for payment, a group of volunteers for tutoring and monitoring, and a guarantee fund set up by third parties, such as banking foundations or government agencies, and (ii) another based on an institution specializing in microfinance, which operates as a financial brokerage company pursuant to art. 106 CBA. In Italy the first model currently prevails. In addition to classification according to the type of institution (e.g., banking institution, consortium, association, foundation, local government body, financial intermediary, etc., as will be seen below), microcredit providers can be classified on the basis of other criteria: (i) institutions that obtain a license to conduct banking activities or simply apply for registration with a banking supervisory authority, (ii) institutions having the status of non-profit organizations, or institutions who aim instead to make a profit (iii) private institutions or public institutions, (iv) institutions whose main activity is microcredit or institutions for whom microcredit is only part of their portfolio of assets. The market operators can also be differentiated according to the type of borrowers they address, according to the products and services they offer or are authorized by law to provide, on the basis of whether they are subject or not to prudential supervision rules and, finally, according to the procedures and technical tools used for funding. The banking sector is a major player in the market for microcredit through savings banks, cooperative banks and commercial banks. However, in Italy, as is the case in most Member States of the European Union, non-bank institutions are the main providers of microcredit.

3.1. Consortia

The credit trusts and warranty cooperatives (better known as consortia), belong to the family of intermediaries approved by the CBA. Disseminated in capillary form in the Italian business network since the fifties, they now form an integral part of the economic and financial system of the country. The consortia, through their guarantee funds, offer themselves as guarantors of the loans granted by banks affiliated to member companies, giving them access to credit on better terms than those that could be obtained on the market or that they would not get at all. The average size of the loans varies widely depending on the sector they belong to, and can range from small amounts of €7,000-10,000 to millions of euros. On average the offers amount to 50% of the required amount borrowed. The revenue of the consortia mainly derives from a percentage of the guaranteed loan, levied in advance, which varies depending on the amount of the loan and the repayment period, and the source of the membership fee for joining the consortium. Although the consortia do not deal exclusively with the most vulnerable businesses, nor restrict their services to smaller amounts of credit, there is not as

yet a clear link in the literature between them and microcredit, a part of their business which is effectively and concretely linked to allowing financially excluded businesses access to credit. The sustainability of this model is certainly achievable through increased revenues from guarantees granted to the strongest companies to cover the costs of investigation, assessment and support (monitoring costs) for the most vulnerable entrepreneur. The main weakness of the model is that it reduces the legal/institutional congruence which, despite their being recognized by the Banking Act for the activity of granting loan guarantees, is expressed in the severe limitations of the target subjects (excluding individuals) and the fact that their social objective is not exclusively microcredit.

3.2. Non-profit organizations
The operating model in the provision of microcredit which is used by associations and foundations is that of non-profit organizations specifically set up for the purpose of providing microcredit services or which include microcredit, although not exclusively, among their institutional activities. The model includes three main actors: 1) the institution or foundation, which intercepts and assesses the needs and demands for microcredit, presents the potential beneficiary to the bank or financial intermediary that will provide the credit and follows the beneficiary before and after activity through tutoring, 2) the bank or broker with which the body has entered into an agreement with for the provision of credit, 3) a collateral loan fund, consisting of private and/or public donors. The main strength of this model lies in its considerable ability to detect and assess the needs and demands of microcredit thanks to the often long history of the institution in the region in support of individuals and families in economic and social difficulty. The most evident limitation concerns its financial sustainability. Despite a high ability to raise the necessary funds, thanks to the organization’s intrinsic non-profit character which allows it to easily convey the right microcredit message, the fact that the body mainly carries out its activities for free and that the model is fully subsidized by funds of a public and/or private nature, typically a one-off with no guarantee of continuity, considerably limits long term planning. With regard to the legal/institutional congruence of the operations of this model, its business, although carried out free of charge, can be likened to a kind of credit mediation that still hasn’t found a precise location in the CBA.

3.3. Local Authorities
In recent years even local authorities have fielded financial resources to promote operational models, usually a mixture of public and private, motivated by the political will to implement a microcredit program. The model includes three main actors: 1) a regional network of professional or voluntary organizations that intercept and assess the needs and demands for microcredit, present the potential beneficiary to the bank or financial intermediary that will provide the credit and follow the beneficiary before and after delivery via tutoring, 2) the bank or the intermediary with which the local authority has signed an agreement for the provision of credit, and 3) a fund set aside as collateral for loans made by the local organization. The management of the program is usually entrusted to the regional financier (as is the case in Tuscany) or sometimes to external professionals (such as in Lazio and

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59 According to Public and Private Policy for the provision of microfinance services, of the 62 microcredit projects promoted by non-profit organizations, 56 are designed to provide an emergency response to social needs through the provision of “social” microcredit, while the remaining 6 offer “productive” microcredit programs. Of the total of 62 programs surveyed, 59 completed the microcredit activities with accompanying services and advice but not one of them is financially sustainable.

60 According to Public and Private Policy for the provision of microfinance services, of the 21 microcredit projects sponsored by public entities, 8 are designed to provide emergency response to social needs through the provision of “social” microcredit, while the remaining 13 provide microcredit programs with a “productive” purpose. Of the total of 21 programs surveyed, only 8 complete the microcredit activities with accompanying services and advice, and none of them are financially sustainable.
Marche), with the specific expertise and authorization necessary for the implementation of the service in compliance with the legislation in force, which is almost always a regional regulation. The most evident limitation of this model is, once again, a lack of sustainability, that is, a guarantee of the existence of the institution over time and its independence from external influences. While they are generally entirely subsidized by public funds, this does not guarantee the continuation of programs in the event of limited or reduced resources available to the local authority, a not uncommon hypothesis nowadays. In addition, the operation of “social” microcredit sometimes seems compromised by the fact that the fund manager is often similar to a consortium and carries out the service exclusively in favour of the business. This model has been shown to have good results in starting microcredit projects if they are initiated in cooperation with other financial bodies or civil society organizations, otherwise the effectiveness of its direct intervention as a provider of funds is more doubtful.

3.4. Financial Intermediaries

Compared to other models, the model that provides for the establishment of a company, whether limited, limited partnerships, limited liability companies or cooperatives, recognized and authorized by the Bank of Italy to operate as a financial intermediary, has the distinction of being a direct provider of credit in the form of interest rates and costs of investigation (ie APR, annual percentage rate), without excluding institutional co-operation with local authorities, the voluntary sector and banks.

The main strength of this model is clearly the full legal and institutional congruence of its operations. However, despite the intention of covering operating costs through revenues from the provision of credits, financial sustainability is still the biggest challenge which institutions seek to address by pursuing in the shortest possible time significant volumes of loans and by efficiency in the development of the internal scoring models and procedures to support the valuation of credits. It remains an open question whether the major Italian operators, Microcredit Solidarity s.p.a and PerMicro, can meet this challenge in light of the high cost per customer due to the fact that the number of active clients is not yet high enough to cover operating costs. The high rates of write-offs instead highlights the need for better training for operators but above-all for a more studied and detailed definition of tutoring, perhaps even at the regulatory level.

3.5. Social Enterprises

To complete the panorama of microcredit bodies, at least those with a potential role, we report on social enterprises. Although, in fact, national legislation does not recognize lending among the possible types of activities exercised by social businesses, the dominant definition of social economy formulated at a European level by the European Research Network (EMES) is not incompatible with the exercise of microcredit. The activity of a social enterprise is situated halfway between the cooperative world and that of non-profit organizations: with regards to the former, greater emphasis is given to the general interest rather than the mutualistic interest of the members, and the stakeholders can more easily include a wide

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61 Microcredit in the Marche Region, for example, is aimed only at start-ups launched by unemployed and laid off workers or women.
64 According to Public and Private Policy for the provision of microfinance services, all 8 projects promoted by non-bank microcredit programs offer only "productive" microcredit. Of the total of 8 programs surveyed, 5 complete the microcredit activities with accompanying services and counselling and only 3 are financially sustainable.
65 See www.socialeconomy.eu.org
variety of private and public actors. The latter operates in the market by taking on economic and financial risk and making relatively less use of subsidies.

4. CONCLUSION

In current market conditions, no model has been found to be uniquely superior to others. Moreover, despite the wide institutional variety, no best practice benchmark can be currently identified. Thus, although the model of financial intermediaries is certainly the most appropriate from the point of view of legal and institutional congruence with current legislation, the goal of financial sustainability has not yet been achieved. Conversely, although the consortia model has proved over the years to be more efficient in terms of costs and sustainability regarding the number of guarantees, it has not been fully legally and institutionally coherent and the system has an inherent inability to provide security to individuals and therefore a limited functional capacity with regards to the overall objective of microcredit. It should also be noted that the national legislature has enacted regulations which have not been particularly innovative, using traditional legal instruments, with considerable reference to the secondary legislation still pending[^7], and avoiding the exploration of solutions which are more appropriate regarding innovativeness and the economic and social importance of the phenomenon. At the European level the situation is also highly heterogeneous due to the differences between the legal and institutional frameworks of the Member States as well as the variety of entities operating in the microcredit field. The joint initiative of the European Commission, the European Central Bank and the European Investment Fund called JASMINE (Joint Action to Support Microfinance Institutions in Europe)[^67], in particular through the adoption of the European Code of Good Conduct for microcredit provision[^68], attempted to establish principles of governance and prudent management consistent with best practices in the industry, with the aim of establishing a set of rules approved in the European Union and recognized as essential to the operations and financial reporting of entities operating in microcredit. It proves once again that “the focus should be ... on a (ideally harmonized) regulation of the entities (MFIs). Hard and soft regulation should both be in place and converge and should be directed at instituting appropriate management and internal control systems for MFIs, at establishing an adequate public supervision, at fostering networking (also through the establishment of ‘second level’ MFI federal organizations providing regional and/or national coordination and technical assistance and support to their members) and at developing best practices for lending[^69]**. A careful look at the dynamics of supply and demand reveals that since financial, employment and social protection systems are interconnected, microcredit operations in this sector must be included in a legal framework and have broader support. Hence there is a need to ensure an overall vision and coordination by a central body with financial and social expertise and the capacity and powers to monitor and coordinate action in support of microcredit.

[^66]: See note 7.

[^67]: As microfinance lending practices vary considerably, the design of a widely accepted European Code of Good Conduct for Microcredit Provision was identified by the European Commission as an important element to promote best practices in the sector. See European Commission, COM (2007) 708 final / 2, European initiative for the development of microcredit in support of growth and employment, p. 11. The latest version of the Code of Good Conduct of June 2013 is available at the link [http://ec.europa.eu/regional_policy/eusfunds/instruments/doc/jasmine_code_de_bonne_conduite.pdf](http://ec.europa.eu/regional_policy/eusfunds/instruments/doc/jasmine_code_de_bonne_conduite.pdf). The Code is divided into five indexed sections - customer and investor relations, governance, reporting standards, management information systems and risk management - comprising 166 clauses and 20 priority clauses. A pilot phase to test the Code of Good Conduct took place from November 2011 till December 2012 with a number of volunteer organisations. Its aim was to identify potential shortcomings and clarify clauses where deemed necessary. See also EMN. (2013). Implementation of the European Code of Good Conduct for Microcredit Provision.

Drawing on this research, I identify three main objectives of the microfinance industry in Italy: (i) provide access to capital in order to help vulnerable individuals and families at risk of sliding deeper into poverty and social/financial exclusion; (ii) Provide financial literacy\textsuperscript{70}, monitoring, and tutoring in order to avoid excessive debt load; (iii) Prevent and fight the phenomena of usury. I also identify common general issues faced by microcredit: (i) the lack of new and innovative strategies of risk management that also include soft information; (ii) the need to develop the ability to absorb high management costs due mainly to activities aimed at collecting intangible information, promoting financial literacy and guiding the beneficiary throughout the life-time of the loan; (iii) achievement of the sustainability of the business over time, both in "market" models and those of "public benefit". Regarding sustainability, this will only be achieved when the loan portfolio is composed of a large number of homogeneous borrowers able to generate a volume of loans which can ensure, at the systemic level, sustainable interest rates for the particular target customers\textsuperscript{71}. In order to address the issues highlighted in this analysis, especially the achievement of the financial sustainability of microfinance institutions, two interventions are needed. The first one regards the legislator. Legislator should also help design, perhaps learning by the self-regulation experience (i.e. Code of Good Conduct), a viable “loan delivery process” in order to define the key elements of the process of microcredit (i.e., monitoring, scoring, tutoring). Based on this consideration, “it would make sense to draw up an evaluation system for the specific credit risk of microcredit, which could be of decisive support in improving the portfolio of loans and building a model segmented by customer type which would be useful for profiling specific microcredit products”\textsuperscript{72} 73. The second one regards European Institutions. Despite support from the European Commission in recent years to the Microfinance sector through several programmes (CIP, EPPA, JEREMIE, JASMINE, EPMF, etc.) “there is still a clear need to invest in the capacity building and refinancing of microfinance institutions in Europe over a sustained period of time, allowing them to improve their institutional capacities and providing them with access to sustainable funding sources”\textsuperscript{74}. And this seems to be the way that European Commission wants to carry on\textsuperscript{75}.

LITERATURE


\textsuperscript{70} According to Benjamin Franklin "An investment in knowledge pays the best interest ’, i.e. the return on investment in knowledge is higher than that of any other investment, is the root of human and social progress, the condition for economic development (see Franklin, B., (1750). Poor Richard’s Almanack). On the topic of tutoring, the executive summary of the workshop organized by the foundation Giordano dell’Amore on the 19 March 2011 was regarding the service of tutoring Italian microfinance clients, and can be found at the following link. http://www.fgda.org/dati/ContentManager/files/Workshop/servizio-di-tutoring-nella-microfinanza-italiana.pdf

\textsuperscript{71} A model to be taken as an example is certainly the case of Spanish MicroBank - Banco Social La Caixa, which from 2007 to the end of 2012 granted 169,282 microcredits for a value of 1,045,000,000 euro (only in 2012, 11,185 microloans productive type for a value of € 116.5 million and 29,599 social microloans for a value of 119 million euro). See http://www.microbanklacaxa.com/informacioncorporativa/datosbasicos_es.html

\textsuperscript{72} See Public and private policies for the provision of microfinance services, cit., p. 10.

\textsuperscript{73} Very helpful could be move from the practice of traditional credit scoring to the revolutionary practice of behavioral scoring. See note 29.

\textsuperscript{74} See EMN, (2013). The role of Microfinance and Entrepreneurship during the next EU budgetary period 2014-2020, p. 3.

\textsuperscript{75} Initiated in 2010 by the European Commission, the European Progress Microfinance will continue to offer its product to microcredit providers to allow for accessibility and availability of microfinance in the European Union until April 2016 at the latest. Progress Microfinance’s goal is disburse 500 million Euro through 46,000 microloans to final recipients. See European Commission, (2014). Report from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions. COM (2014) 639 final.
KEY ISSUES AND POLICY IMPLICATIONS FOR SWEETPOTATO PROCESSING IN PAPUA NEW GUINEA

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ABSTRACT
The development of a food processing and preservation industry was identified by the Papua New Guinea (PNG) government as one of the priority programs in the National Agricultural Development Plan 2007-2016. Food processing using local materials was envisaged to have the potential to generate employment and income opportunities for smallholder farmers, and hence contributing to poverty reduction and food security. The PNG food manufacturing sector is small, and is dominated by foreign companies using primarily imported ingredients. The objective of this study was to assess the challenges and opportunities for developing a locally-owned food processing sector in PNG, using sweetpotato as a test case. Sweetpotato was chosen because it is the main staple crop in PNG and is grown by smallholder farmers across the country all year round. Consequently, the socio-economic impact could be significant if an efficient sweetpotato processing sector could be established. The impact could be even greater if the associated technology spilled over to other food crops (cassava, yam and taro) and South Pacific countries. Research methods used included: technical trials to improve sweetpotato flour processing efficiency and flour quality; sweetpotato product development; and a review of sweetpotato processing R&D in PNG. Results showed that, although there is a niche market for sweetpotato products, sweetpotato flour, as a raw material for commercial food processing, is not versatile functionally or cost competitive, compared with wheat and corn (for flour production), potato (for fries/chips), and cassava (for starch). Limited R&D resources can be better spent on improving the value chain of fresh sweetpotato roots. However, if the PNG government is determined to develop a food processing industry, sweetpotato processing can be used as a pilot both to build research and development capacity in food processing, and to develop an enabling environment necessary for small to medium size agroenterprise development.

Key words: agroenterprise development, enabling environment, Papua New Guinea, sweetpotato

1. INTRODUCTION
The PNG food manufacturing sector is small, and is dominated by foreign companies using primarily imported ingredients. “The development of a food processing and preservation industry” (Program Area 2) was listed in the Priority Program Areas for Food and Horticulture Crops Development in the National Agricultural Development Plan 2007-2016, aimed at generating employment and income opportunities for smallholder farmers, and improving poverty reduction and food security (Ministry of Agriculture and Livestock, 2006). In the 2014 Budget Strategy Paper, “Improving the enabling business environment for the agriculture sector and facilitating the development of the small and medium enterprises” was listed as one of six key policy priorities (Government of PNG, 2013). These two documents
suggest that the policy environment seem favourable to small to medium size agroenterprise development. The objectives of this study were to assess the challenges and opportunities and derive policy implications for developing a locally-owned food processing sector in PNG, using sweetpotato as a test case.

Although the two documents did not direct specifically at sweetpotato processing, or any other crops, there is a case for developing a sweetpotato processing sector. Sweetpotato is the main staple crop in PNG, accounts for 43% of total food energy intake (Bourke and Vlassak, 2004). It is grown by smallholder farmers across the country, and supply is available all year around. Consequently, the socio-economic impact on rural communities could be significant if an efficient sweetpotato processing sector were established. The impact could be even greater if the associated technology spills over to other root and tuber crops (such as cassava, yam, taro), and potentially to other South Pacific countries. Developing the sweetpotato sector is an important pro-poor strategy to economic development (Fuglie, 2007).

2. METHODOLOGY
We conducted an extensive literature review of sweetpotato processing research in PNG, as well as in China and Africa where such research has been the most extensive and where the findings are most relevant to PNG. Technical trials were conducted on-station to assess the processing efficiency and quality of sweetpotato flour, based on the process suggested in Van Hal (2000). Sweetpotato products were developed on-farm in collaboration with community groups, following the territorial approach to rural agroenterprise development popularised by the CIAT (Ferris et al., 2006). We also conducted social mapping of collaborating communities to track the dissemination of sweetpotato processing technology and to monitor and evaluate the community impact of the project. In this paper, we summarise the results from on-station technical trials and on-farm product and market development. More detailed information can be found in Chang and Mais (2014).

3. SWEETPOTATO AS A FOOD CROP
As a food crop, sweetpotato offers several advantages. It requires fewer purchased inputs and less labour than other staple crops such as wheat, rice, maize or cassava. It is adaptable to a wide range of agro-climatic conditions, including high altitudes, marginal areas, dry periods and poor soil. In addition, sweetpotato has the capacity to establish ground cover very quickly enables early weed suppression, controls soil erosion and helps maintain soil fertility (GTZ, 1998). It provides more edible energy per hectare than wheat, rice, maize or cassava. It has a reputation as a food security crop – that is, the one that a family relies on when the maize or rice fails.

Sweetpotato may not be the most nutritious staple crop compared with cereal crops, but it has the highest nutritional value as a vegetable. Sweetpotato roots are high in carbohydrates and dietary fibre. They are also rich in vitamin B and C and minerals like potassium, magnesium, phosphorus and zinc (WHfoods, n.d.). In addition, the orange-fleshed varieties contain high levels of β-carotene, a pre-cursor for vitamin A, and are heavily promoted to combat vitamin A deficiency in sub-Saharan Africa (SSA). Being low Glycemic Index (GI), sweetpotato is a beneficial food for diabetics; it can help stabilise blood sugar levels and reduce insulin resistance. Sweetpotato vines/tops, often under-valued and unreported in government statistics, are also high in protein, vitamins and minerals (Islam, 2006) and are widely consumed as a leafy vegetable.

According to FAO, 115 countries produced close to 107 million tonnes (Mt) of sweetpotato in 2010. Production was concentrated is Asia (82.3% of global production) and in Africa (14%). China is the world’s largest sweetpotato producer, with 76.2% (81 Mt) of global production in
2010. This was followed by Uganda (2.84 Mt), Nigeria (2.84 Mt), Tanzania (1.4 Mt) Indonesia (2.05 Mt) and Vietnam (1.32 Mt). Together, Uganda, Nigeria and Tanzania represent half of total African production. In contrast to the declining production trends observed in Asia due to economic development in recent decades (Huang et al., 2004), sweetpotato production has increased in the United States and some African countries. Expanding production in Africa has been explained largely by strong population growth and subsequent increases in demand (UNCTAD, 2012). Although a small producer (about 1 Mt), sweetpotato production is increasing in the US due to increased awareness of its health benefits, particularly its low GI, high fibre and low fat content. The US is the leading global exporter of sweetpotato, mainly to Europe (UNCTAD, 2012).

Sweetpotato has several potential uses, including as a fresh food, a stockfeed, and as a raw material for food processing. The main sweetpotato food processing options are: starch, dried chips/flour, and new food products (Fuglie et al., 2006). Changes in sweetpotato use in developing countries from the early 1960s to 2009 are presented in Table 1. The data show that sweetpotato use in fresh form declined from 77.6% of total production in the early 1960s, to 52.4% in the late 1980s. This trend was largely counter-balanced by an increase in the use of sweetpotato as stockfeed, from 11.7% of total production in the early 1960s to 36.1% in the late 1980s. By comparison, there was little change in sweetpotato used for processing into new food products, with a minor increase of 4.5% to 5.4% recorded over the same period.

Table 1. SP utilisation in developing countries (Scott, 1991)

<table>
<thead>
<tr>
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<th>1961-63</th>
<th>1973-75</th>
<th>1986-88</th>
<th>2009*</th>
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<tr>
<td>1000 Mt</td>
<td>%</td>
<td></td>
<td></td>
<td></td>
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<td>Fresh food</td>
<td>77.6</td>
<td>70.2</td>
<td>52.4</td>
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<td>Stockfeed</td>
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<td>19.0</td>
<td>36.1</td>
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<td>4.8</td>
<td>5.4</td>
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<td>0.2</td>
<td>0.2</td>
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</tr>
<tr>
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<td>5.8</td>
<td>5.8</td>
<td>6,637</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>102,143</td>
</tr>
</tbody>
</table>

* Calculated by authors using FAOSTAT database.

Two decades later in 2009, the proportions of sweetpotato used for food, feed, processing were 54.2%, 39.0% and 0.04%, respectively (Table 1, last two columns). The most significant change by 2009 was the reduction in the proportion used in processing. This was mainly a result of sweetpotato losing its competitiveness as a raw material for starch production, especially in China (Fuglie et al., 2006).

4. SWEETPOTATO PROCESSING RESEARCH IN PNG

Unlike in Western countries, there is little awareness among the general public of PNG of using sweetpotato as a vegetable (as opposed to a starchy staple food). Likewise there is little awareness of the potential to use sweetpotato as a raw material for processing into bakery products, noodles or snack foods, as is common in Asia and Africa.

Sweetpotato processing research and development was institutionalised in PNG when the Food Processing and Preservation Unit (FPPU) was established in 1984, with the goal of developing a food processing sector in PNG (Cegumalua, 2007). Work at FPPU focused on developing products for downstream processing, and on training and assisting entrepreneurs in progressing further into commercial scale agroenterprises. FPPU was reviewed, and was subsequently shut down, in 2007. The review found that the program had failed to achieve its original objective (Cegumalua, 2007). First, there was little uptake of the processing technology by entrepreneurs and trainees. Of those few individuals who were interested in
adopting the technology, most did not succeed because of insufficient technical knowledge. Those who managed to go into processing business failed to develop into fully-fledged commercial enterprises either because of lack of necessary capital or business management skills to scale up. Most continued to operate at the cottage industry level, selling their produce in informal markets. Second, the building and processing equipment of FPPU had deteriorated over the years, and eventually became un-operational, due to poor management and lack of financial support from the government.

After the closure of FPPU, most processing research was conducted at the National Agricultural Research Institute (NARI). NARI research focused on evaluating sweetpotato varieties and their suitability for producing sweetpotato flour. Research also focused on using composite sweetpotato/wheat flour to produce derivatives such as cakes, donuts, pancakes, biscuits, and noodles. Similar research was also conducted with other food crops such as cassava, yam and taro. The main objective was to substitute imported wheat flour with locally produced flours as much as possible while maintaining the integrity of products that were derived from the composite flours. Those experiments were not as successful as expected.

Sweetpotato flour is functionally very different from all-purpose flour, for example, it is gluten-free, sweet and has a strong flavour (Peters and Wheatley, 1997). This restricts the use of sweetpotato flour as a substitute for wheat or other flour. Even partial substitution (at a level of 10–15%) of wheat flour with sweetpotato flour can change the taste, smell, and texture of products, such as bread, enough to have them marketed as different products. The potential for sweetpotato flour in making bread is limited, but flat unleavened products such as pancakes, puddings, and chapattis can be made with higher proportions of sweetpotato flour. This is also true for a much wider range of products, mostly with a sweet taste, including donuts, biscuits, muffins, cookies, brownies, noodles, pies, and baby foods (Woolfe, 1992; Peters and Wheatley, 1997).

These results suggested that rather than imitating wheat-based products, more attention should be given to developing recipes that suit the unique characteristics of sweetpotato, and use locally available materials.

### 4.1. On-station sweetpotato flour processing

#### 4.1.1 Factors influencing processing efficiency and flour quality

The most important quality characteristics of sweetpotato flour are moisture content, protein, starch and β-carotene content, as well as microbiological quality, colour, taste, and odour. The quality of sweetpotato flour is defined in the African Standard CD-ARS 827:2012(E) (ARSO, 2012), as shown in Table 2.

<table>
<thead>
<tr>
<th>Parameter</th>
<th>Requirement (In % on dry matter basis)</th>
<th>Method of test</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total ash</td>
<td>&lt; 3.0</td>
<td>ISO 2171</td>
</tr>
<tr>
<td>Moisture</td>
<td>&lt; 12.0</td>
<td>ISO 712</td>
</tr>
<tr>
<td>Crude fibre</td>
<td>&lt; 5.0</td>
<td>ISO 5498</td>
</tr>
<tr>
<td>Acid insoluble ash</td>
<td>&lt; 0.15</td>
<td></td>
</tr>
<tr>
<td>Total sugar (as sucrose)</td>
<td>&gt; 6.0</td>
<td>ISO 2173</td>
</tr>
<tr>
<td>Starch</td>
<td>&gt; 60.0</td>
<td>ISO 15914</td>
</tr>
<tr>
<td>pH of aqueous extract</td>
<td>4.5-7.0</td>
<td>ISO 1842</td>
</tr>
<tr>
<td>Cold water solubles</td>
<td>&lt; 12.0</td>
<td>ISO 941</td>
</tr>
</tbody>
</table>
Survey of literature showed that sweetpotato flour of a desirable quality can be made at the household/village level using simple technology (Wheatley et al., 1995; Van Hal, 2000). Sweetpotato flour processing involves the following steps: selection of fresh roots, weighing, trimming, washing, peeling, slicing/shredding, soaking (bleaching/blanching), pressing, spreading, drying, grinding, sifting, weighing and packaging (Van Hall, 2000). Although not a complex process, each of these steps has some bearing on the final quality and processing cost of the flour, especially the selection of fresh roots.

Dry matter content and flour yield are the most important factors influencing processing cost. Both are affected significantly by the choice of variety. Sweetpotato roots are classified into two general types in terms of dry matter content and colour: dry-fleshed cultivars with mealy, light yellow or white flesh, and moist-fleshed cultivars with soft, gelatinous, bright orange flesh. Yields reported in the literature range from 17 to 38%, as moisture content can vary from 65-80%, depending on variety, but they are most likely to be in the range of 25-29% (Van Hall, 2000). Therefore, careful consideration must be given to the selection of the raw sweetpotato roots.

For any given variety, sweetpotato roots must be sorted based on their size and shape, while removing roots with rots, insect damage, excessive mechanical damage, and excessive soil or other foreign materials. Peeling takes more time when the roots are too big, too small, or irregularly shaped. Excessive culling and trimming to remove undesirable parts of roots will increase wastage, reduce yield, and increase labour costs (Gakonyo, 1993).

4.1.2 Results from flour processing trials

Altogether, six batches of sweetpotato flour in different volumes, and using three different varieties, were produced. Data collected included: (1) the time taken to carry out each of the various processing steps; (2) variable costs of raw material, labour, water and electricity; (3) extraction rate/flour yield; and (4) proximate contents of flour.

Key results were:
- On average, it took 28 hours to process 100kg of fresh roots, including 20 hours of drying time in the oven.
- Extraction rate/flour yield varied between 17-20%, depending on varieties, quality of fresh roots, and drying time.
- Results from proximate analysis from 4 samples tested (Table 3) showed average readings for protein, at 3.26%; moisture, at 6.34%; fat, at 1.67%; ash, at 1.93%; and fibre, at 1.82%.
- Average variable cost of flour was K7.80/kg. This is high compared to the retail price of wheat flour at K3.8-4.5/kg and of rice at K3.45-4.0/kg at the local supermarkets. Similar results were found in other studies (e.g. Peters and Wheatley, 1997) that sweetpotato flour has to be 50%–90% cheaper in order to compete with wheat flour and replace it in any significant volume. However, if sweetpotato roots could be sourced locally or from the farm, the average variable cost would be reduced to around K5.0/kg.

Table 3. Proximate analysis results from 4 samples (in %)

<table>
<thead>
<tr>
<th>Variety</th>
<th>Milled</th>
<th>Tested</th>
<th>Protein</th>
<th>Moisture</th>
<th>Fat</th>
<th>Ash</th>
<th>Fibre</th>
</tr>
</thead>
<tbody>
<tr>
<td>One-moon</td>
<td>04.10.12</td>
<td>23.10.12</td>
<td>2.58</td>
<td>8.25</td>
<td>3.75</td>
<td>1.00</td>
<td>2.00</td>
</tr>
<tr>
<td>Wahgi Besta</td>
<td>29.11.12</td>
<td>9.12.12</td>
<td>3.24</td>
<td>7.50</td>
<td>0.75</td>
<td>2.50</td>
<td>1.50</td>
</tr>
<tr>
<td>Wahgi Besta</td>
<td>11.12.12</td>
<td>18.12.12</td>
<td>4.22</td>
<td>2.85</td>
<td>0.67</td>
<td>2.48</td>
<td>3.26</td>
</tr>
<tr>
<td>Kerot</td>
<td>22.04.13</td>
<td>29.04.13</td>
<td>3.00</td>
<td>6.75</td>
<td>1.5</td>
<td>1.75</td>
<td>0.50</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td><strong>3.26</strong></td>
<td><strong>6.34</strong></td>
<td><strong>1.67</strong></td>
<td><strong>1.93</strong></td>
<td><strong>1.82</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


These results suggested that only by sourcing inexpensive raw materials and through very efficient processing can sweetpotato flour be cost competitive with wheat flour. To reduce raw material costs, consideration must be given to improving yields to lower the cost of production, selecting/breeding varieties with high dry matter, identifying processing sites that are near the source of supply, and improving postharvest management to reduce product losses during transit and storage. To reduce processing cost, more research is also required to determine the desirable moisture content, the optimal combination of temperature and drying time, and the effect of leaving the sweetpotato unpeeled on the quality of flour and its derivatives.

4.2. On-farm sweetpotato product development

The territorial approach to rural agroenterprise development popularised by the CIAT (Ferris et al., 2006) involves the following activities:

- develop partnerships, territorial diagnosis and joint planning;
- identify market opportunities for small rural producers;
- analyse market chains;
- design and implement rural agroenterprise business model;
- strengthen business development services; and
- advocate for improved marketing and trade policies.

In this paper, due to time and other resource constraints we presented results from partnerships development, territorial diagnosis, the spread of processing technology, and impact assessment.

4.2.1. Developing partnerships

Two rural communities were invited to participate in this research: the first group was members of a farmer co-operative (co-op) based in Sibi village, and the second group was from Gebansis village. Our main contact persons were the project coordinator of the co-op and a community leader for the latter group. Sibi village is located in a mountainous area 600 meters above sea level, and is an hour drive away from the Lae City – the second largest city in PNG. Gebansis is more conveniently located near the main road and is 30 minutes drive to the Lae City. The different locations and makeups of the two groups allowed us to compare results and develop locally appropriate intervention strategies.

4.2.2. Territorial analysis

A social mapping method was used to assess the resources available at the communities. Two maps were produced for the first group: one for Sibi village and one for the Middle Erap community of which Sibi village is a part. The focus of the village map was to identify the main roads, mountains, rivers, and any other relevant geographic features in relation to the resource centre of the co-op located in Sibi village. The community map focused on identifying the locations and names of villages in the community, and the location of community resources such as schools, health clinics, churches, resource centre, drum oven, fish ponds, rice fields, and pineapple fields. Chinese taro (Xanthosoma sagittifolium) was identified as the major food crop. Coffee and cocoa were the major cash crops, and were widespread in the community. Like most rural PNG, there was no electricity service in the community, but few households had generators and solar power. Both the main road and feeder roads were in poor conditions and were impassable after heavy rains. There was one wood-fired drum oven in the community.

Similar mapping exercise was undertaken in Gebansis village. The village had good roads and easy access to the Lae urban centre, and electricity connection was available for those who
could afford it. Banana was the staple food crop while cocoa was the main cash crop. Gebansis village had a cocoa co-op. Several households were out-growers for a poultry company (Tablebirds). Three wood-fired drum ovens were identified.

4.2.3. Product and market development
Basic training on flour processing and baking was provided to both groups, and sweetpotato flour was distributed to Sibi and Gebansis participants along with recipes. Participants were encouraged to work together and to experiment with making sweetpotato products and develop their own recipes. Several weeks after the training, a number of sweetpotato products had been developed. The Gebansis group had made sweetpotato strips, cassava/sweetpotato cake, fried sweetpotato balls, sago/sweetpotato fries, donuts, cookies (with pumpkin and banana), and boiled sweetpotato flour balls. For the Sibi group, more interesting new products were developed using ingredients that were available in the village. These included: donuts, pastry (pumpkin, potato), scones, fried flour, sweetpotato cookies, banana cakes, peanut cookies, ukoi (with pumpkin and pawpaw), strawberry flavoured cookies, steamed banana cakes, bread, cassava donuts with locally made desiccated coconut, pizza bases, and buns with various flavours.

Fifteen households in Sibi and seven households in Gebansis were involved in developing these products. In most cases, half a dozen experiments were required to arrive at a product of acceptable quality. Some products were sold in the villages and were well-received. Demand was high and profits were significant. Training in marketing, costing, hygiene and packaging was provided to participants who were active in product development. Marketing trials to sell a few selected products to schools and government agencies in the Lae City are to be conducted later to get consumer feedback before commercial roll out.

4.2.4. Tracking the spread of sweetpotato processing technology
Six months after the project started, social mapping again was used to track the spread of the sweetpotato processing technology, focusing on the social networks through which sweetpotato knowledge was disseminated, agents of change, individuals who received the knowledge second-hand, and their relationship to the change agent. We found that in Gebansis, social networks were mainly kinship-based, and were largely limited to people who were related to the community committee chairman. In contrast, in Middle Erap community, social networks extended beyond Sibi village to include neighbouring villages who were also members of the co-op. The project coordinator of the co-op, being employed from outside the district, appeared to be more objective and inclusive in her decision making. Given that rural communities are diverse and their social and political structure is complex, the participatory methodology employed in this project helped us gain significant insights into the workings and power relationships of these rural communities, which has bearing on knowledge dissemination aimed at improving livelihood. More details on social mapping can be found in Sar et al. (2013).

4.2.5. Monitoring and evaluation
The research team visited Sibi village nine months after the project started to assess the impact of the training activities on the community, their experience with sweetpotato processing, and to find out more about the constraints and opportunities for village-level processing. Several issues were identified:

- Product development – development costs were high because it took time and several experiments before satisfactory results could be achieved. Using local ingredients had reduced costs and encouraged creativity.
• Equipment – availability of equipment and tools was a serious issue for the community because there was only one drum oven in Sibi village. However, members of the community were looking into alternative ways to baking, such as using dish ovens, steaming, and frying. More research is needed to identify food processing equipment that is practical for rural communities where there is no electricity access.

• Costs of ingredients – the availability and costs of ingredients, such as oil, sugar, eggs, and wheat flour, was also an issue.

• Labour intensity – it was tedious and time-consuming to make sweetpotato flour. Participants were interested in finding alternative methods for sun drying and solar drying of sweetpotato.

• Access to sweetpotato processing training and flour – some interviewees complained about not having had access to training or flour because they were not part of the community or network that was involved in the project.

Some of these results are similar to what was found by Chang and Irving (2013). They found that although there was interest in food processing in rural communities, the uptake of technology after training was often poor. Major constraints to adoption were: labour intensity, and lack of access to equipment (such as milling machinery, baking ovens, and kitchen utensils), ingredients (such as milk, sugar, butter, and eggs), and basic services (transport, clean water, electricity, credit, and technical support).

Further research is required to address the socio-economic constraints to technology dissemination and adoption, and to identify locally appropriate technology (equipment and tools) for rural households with limited resources and budget. Given that leadership is the most significant enabling factor in the spread of technology and initiation of change in rural communities, it is crucial to identify individuals who have the social capital and commitment to broaden the existing kinship networks to include the wider community, as well as being proactive in problem-solving, rather than relying on outside help.

Overall, the project has produced significant results with respect to flour processing and product development. As well as raising community awareness of sweetpotato processing. Sweetpotato products have been sold in both Gebansis and Sibi villages with good outcomes – demand was high; profits were significant; and a quick income source. These results showed that marketing opportunities exist for good quality, low cost sweetpotato products that are made from locally available materials using family labour.

5. KEY ISSUES AND POLICY IMPLICATIONS

Lack of access to basic services (transport, water and electricity) and basic equipment in rural communities were recognised in this paper, and by Chang and Irving (2013). Problems with capacity, business support services and business linkages were clearly identified in the review of FPPU by Cegumalua (2007). In addition, GTZ (2003) outlined ten preconditions that are necessary for successful intervention in rural development through agro-enterprise development:

• an enabling environment that provides for an attractive investment climate and fosters dynamic entrepreneurship;

• adequate mechanisms and structures that address local needs;

• active private sector institutions and linkages;

• functioning and effective infrastructure (hard and soft);

• access to integrated and open markets;

• access to effective and efficient support services and resources;
• adaptive management capacity and entrepreneurial competence within business and enterprises;
• local organisations, groups and associations (representing the poor) as building blocks;
• active participation in and ownership of development processes by well-linked stakeholders; and
• ongoing learning from success and failure by all stakeholders.

Most of these are lacking in the current business environment in PNG. The main policy implication was that the PNG government should play a central role in supporting agroenterprise development by considering the following policy interventions (Ferris et al., 2006):
• encouraging diversification and adding value locally in rural areas;
• promoting participatory methods that directly involve local chain actors in decision-making and develop local capacity;
• stimulating collective action and involvement of rural economic organisations with a solid business and market orientation;
• strengthening the market for business support services and its coordination;
• generating and promoting technologies related to small-scale agricultural production;
• improving service infrastructure such as water and electricity supply; and
• Investing in research and development to reduce raw material costs.

6. CONCLUSION
Food processing has the potential to create employment and diversify and increase income for smallholder farmers and rural communities by adding value to local produce. In the longer term, a well-functioning food processing sector is crucial for the sustainability of the farming sector, as the demand for value-added and processed products can be expected to increase as the economy develops. This means there is a good case for investing in rural agroenterprise development.

However, promoting small to medium-scale processing agroenterprises in PNG will be challenging, due to the current operating environment and resource and capacity constraints. For starters, limited resources should be spent on improving the value chain of fresh sweetpotato roots to reduce the raw material cost. However, if the PNG government is determined to develop a food processing industry, sweetpotato processing can be used as a pilot both to build research and development capacity in food processing, and to develop an enabling environment necessary for small to medium size agroenterprise development.

LITERATURE


Considering the attention has been paid, recently, to the adoption of community governance-based approaches to help addressing developing and post-conflict countries’ need of achieving a minimum level development due to the lack of institutional authority or scarce Government’s capacity to adopt effective solutions to issues of economic and social development and protection of fundamental human rights of the community. Universities have assumed an expanded role in local economic and social development especially in institutionally fragile countries and have helped to initiate a slow, but effective process of development within communities and territories, as the evidence collected in two Balkan post-conflict countries, Croatia and Kosovo, will demonstrate. By leveraging insights from the literature on Community Governance, Community Resilience, social capital, capacity/capability building, and sustainable development, this paper emphasises a socially embedded and community-centric approach to development of territories as a strategy to transform post-conflict situations into contexts of community empowerment. On these premises, the working hypothesis this paper will be based upon is that Universities are actors, amongst the others, which most likely drive territories and their communities towards resilience though steering processes of learning and adaptation, though the shaping of a knowledge based economy and through promoting sustainable development by facilitating the increase of social capital stocks. The paper’s research question is conducted through a methodology based on a qualitative investigation that has been carried out in two countries of the Balkan region both affected by the Balkan’s War which ended in 1995. Central to the transformations developed in the aftermath of the end of the war is the emergence of new approaches for the country’s resilience. The establishment of network-based relationships amongst actors helped triggering processes pursuant strategies of development supported by the role played by Universities that have helped creating the building up of social capital within the communities.

The paper, moreover, will seek to demonstrate that social capital leveraged by Universities plays a significant role in compensating for the weaknesses of formal structures responsible for public education, community empowerment being a crucial variable affecting policy change processes resulting from the modernization agenda. Therefore, the argument that Universities could be strengthened or weakened by informal networks connecting formal institutions with the wider society and for that reason they should be studied.

Keywords: community governance, social capital, sustainable development, community’s empowerment, resilience
1. INTRODUCTION
This research is an innovative contribution to the debate on the role of higher education institutions by leveraging the notions of engaged learning, capacity building, collaborative leadership-based knowledge for achieving development within the enlarged neighbourhood countries of the European Union. It intends to demonstrate that the development of a territory does not necessarily depends on the level of institutional capability and performance but also on how social capital is developed through the action set in motion by educational institutions whose role has been pivotal in increasing social capital stocks which could not otherwise be underpinned by actions undertaken by local governments and the traditional civil society’s actors.

This study will start, in the third paragraph, with an historical presentation of both contexts, Croatia and Kosovo, after the war by emphasising on the changes purported by the war itself which have urged for a transformation of policy making attitudes. This chapter will attempt to give insights on the scientific background supporting the study of this research and which will be presented in the fourth paragraph.

The latter will provide a literature review on the stakeholder theory, capacity building, social capital and its relationship with the paradigm of community governance focusing on network-based approaches that will enable the understating of how a territory can reinvent its governance system through the acting of different players.

The fifth paragraph will contain the findings and results coming out of the qualitative investigation conducted on the field. The paragraph will attempt to demonstrate the reliability of University in producing social capital stocks and for their being as engaged learning promoters of civic engagement.

The answer to the research question will be found in the sixth paragraph that will analyse the independent variables selected in order to understand if there are some elements that would determine the extent of the University’s capacity to contribute to community resilience, hence, to the production of social capital. The aim of this paragraph is, also, to establish the general theoretical framework of this research giving high priority to the issue of engaging communities in learning processes to give policy directions for the territory and community in the attempt to arrest a potential decline in social capital production.

The seventh paragraph will subsume the results and draw to the main conclusions of this study and open up new inputs for future research agenda.

2. TWO HISTORIES IN A NUTSHELL
2.1. Croatia
The Croatian model inspires what could be called as “a constructive change” in post-conflict societies where Universities and higher education could be defined as empowering actors for the youth using a process-structure platform that has produced immediate solutions to conflict as well as long-term vision for sustainable social change. The Croatian community after the Croatian War of Independence became proven and resilient, providing survival and coping mechanisms for insecurity and fragility.

Yet, the Croatian case study teaches that even in areas of sheer desolation, social life and organisational systems can readily re-emerge within community networks. In fact, the Croatian society undertook a period of significant change that also evolved community’s understanding of the concept of democracy while engaging in the attempt to reconstruct the strained and shattered society. As a post conflict country, at first, and as a pioneer of an accessing EU country later, Croatia made an effort in setting up conditions for peace and

social stability in order to be able to transform and the resolve the conflict itself pointing at education as an agent for change and empowerment. This had been possible thanks to the work set in motion, in the late 1998, by a conference which took place in Graz (Austria), on European Educational Co-operation for Peace, Stability and Democracy, which had a huge impact on educational reconstruction in the Western Balkans.

The Graz Process was followed by the Stability Pact for South-East Europe which reaffirmed an action plan designed to include education as a priority area on which States had to invest. Thus, the Graz Process evolved into the Enhanced Graz Process (EGP), encompassing a number of governmental, non-governmental and international organizations and, in the following years, became the main supporter of the region’s educational reconstruction, linking up with education trends in other European countries and promoting regional cooperation and networking as instruments for wider participation in international initiatives. To overcome the post-conflict impasse situation, an educated, committed citizenry deeply involved in creating and sustaining diverse democratic societies was an essential step to take in order to ensure progress, development and advancement of the quality of people’s life. At the aftermath of the war, in the interethnic Croatian community, the two pioneer Universities of Zagreb and Rijeka, made a great effort in contributing to conflict transformation while educating students and improving democracy through social reconstruction interventions which mainly focused on social education, knowledge awareness and community development. According to the literature on development, it would be possible to read development as a movement away from the growth paradigm (which is measured by aggregate wealth creation) and toward the development paradigm, a complex, multi-dimensional concept that has profoundly impacted our understanding of people’s values, quality of life and the private and associational behaviours that contribute to it, and what public policies are necessary to ensure and maintain it.

Thus, since the end of the Croatian War of Independence, there has been a significant shift by the EU and the major international development organizations in their approach to the reduction of poverty, moving toward more comprehensive strategies that incorporate recognition of the importance of communities, institutions, and social relations and focus on human resources development policies. Simultaneously and germane to this shift, social capital has emerged in social science literature as a powerful concept in its three dimensions: diffused social trust (expresses the widespread and mutual confidence in others, on the part of people not related by family ties); solidarity norms of reciprocity (when solidarity norms prevail, they underpin an inclusive and common vision of societal improvement benefiting all); and engaged associational behaviour (facilitates the formulation and adoption of policies in pursuit of a common vision of development).

2.2. Kosovo

After the Kosovo War and the 1999 NATO bombing of Yugoslavia, the territory came under the interim administration of the United Nations Mission in Kosovo (UNMIK), most of whose roles were assumed by the European Union Rule of Law Mission in Kosovo (EULEX) in December 2008. In February 2008, the Assembly of Kosovo declared Kosovo’s independence although Serbia does not recognise the secession of Kosovo and considers it a United Nations-governed entity within its sovereign territory. This makes

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Kosovo, still today, being considered a disputed territory, partially-recognised as a Republic and a self-declared independent state which has de facto control over the territory. Nevertheless, the post-war reconstruction of the higher education system in Kosovo, being the predominant national priority, became possible thanks to the support from abroad and the outburst of passion from inside the country.

The international aid arriving particularly from the US-Aid and other UN-related agencies, after the post-war reconstruction, favoured a piecemeal establishment of a modernized education system free from pressure and disaster. The International community did some very good starting activities, based on intensive communication and exchange, however less on institution building and structural reform, least in fields that are politically sensitive and controversial. Normally, education plays a small role in peace negotiations, peacekeeping and peace building but as for Kosovo, there was an immediate recognition that it would have played a key-role in rebuilding the soft sectors of a new society. It was at this stage that universities, as the foremost amongst education institutions, had been immediately used as cornerstones for civil reconstruction in a devastated post-conflict Kosovo. In fact, Tom Koenigs, former chief of civil administration for UNMIK in Kosovo, had argued that, in a conflict situation, "exit from the military options should normally follow government’s efforts towards education and notably, higher education, as the core instance for modernization and human rights."81

The changing political conditions following the cease-fire for Kosovo reached in June 1999 has provided, in addition to other important changes in the civil and administrative structure in Kosovo, the chance to create a modern, cross-ethnic school and university-system for this country. A proper reconstruction in Kosovo could not be made without a substantial support from the international community and international donors who played a decisive role in dictating provisions for the future of Kosovo. And in this respect, education became a priority after the support of basic needs such as food and shelter to the local population.

And this is the time of the rise and proliferation of private American universities, the result of interveners’ substantiated presence after the NATO bombardment that has allowed the creation of alternative forms of education for the Kosovars to be used for the development of community’s capacities, hence, for the restructuring of the country as a whole.

3. SCIENTIFIC BACKGROUND TO THE STUDY

This research study has conducted a selective literature review in order to produce a convergence of perspectives from different fields, to provide the foundations for the stakeholder model applied to the public field and to understand the implications of the systemic approach to decision-making. The stakeholder theory offers the potential to explore the implications of these broader users and political concerns, representing a shift from traditional methods used in the public sector which has historically relied on the dissemination of information to achieve its aims. This study will also show how stakeholder theory is inextricably connected to open methods of communication which, if effectively carried out, can be successful in the public sector: “...[by] engaging with stakeholders ... the end result will be trust, ongoing involvement and sustained, mutually respectful relationships: in other words the building of genuine community.”82

81 Tom Koenigs, SRSG OF UNAMA, cf. his interview in The FAS, 5 November 2006, p.12: [...] rebellion comes, where development is only slowly trickling [...]. Reforms of the government haven’t yet had impact. In parts, they are not even wanted. In the countryside, people speak of family, religion and harvest, and the government has not had any delivery in these fields [...]. Development is also supply with security, law courts and administration. We realize now that this has been missed [...].

and cultivating trustful as well as sustainable relationships with stakeholders inside and outside the organization in order to achieve mutually shared objectives based on a vision of business as a force of good for the many, and not just the few (shareholders, managers). In fact, it is arguable that decision-makers need to build and rely on social capital which allow citizens to facilitate responsible action.

The main key to responsible decision-makers is, thus, the ability to enable sustainable and mutual beneficial relationships with stakeholders, to create stakeholder goodwill and trust while creating a multi-stakeholder benefit. Reviews on stakeholder theory’s literature leads to the understanding of the notion of social capital that is inextricably connected with the paradigm of governance. The concept is far from the idea of government, which is necessary to build a strong and efficient local government and to overcome the shortcomings of a pluralistic democracy. Hitt and Ireland have argued that managing social capital is the “essence of strategic leadership” while Ballet tried to link social capital to the stakeholder concept. In research on social networks, more explicitly, Andriof and Waddock have contended that “in an era of networked stakeholder relationships, understanding social capital is essential to learning how to construct and maintain corporation-stakeholder connections.” As it has been reported earlier, an increase in the number of stakeholders into public decision-making leads to the understanding of the latter as an open system, whose entities can engage in a co-operative behaviour, even though the degree and scope of their co-operation may vary substantially. As a result, groups of stakeholders base their participation in a mutually beneficial scheme of co-operation.

3.1. The stakeholder theory

The stakeholder concept emerged in the 1960s amongst academics at the Stanford Research Institute, who proposed that, instead of focusing exclusively on shareholders, a firm also should be responsible to a variety of stakeholders without whose support the organisation would collapse. Freeman was instrumental in relating the successes of an organisation to its stakeholders. His definition of stakeholders forms a strong basis for the practice of the theory. He described stakeholders as “...any individual or group who can affect or is affected by the actions, decisions, policies, practices or goals of the organisation”. Freeman sought to account for the correlation between the organization of a firm and its external environment. His focus was upon commercial organizations and he examined the possibility that non-shareholders might impact upon managerial decision making. He suggested that each company had its own set of discrete stakeholder groups: some groups would be primary, in that their interests were directly linked to those of the company, and other would be secondary, in that their influence was indirect or that they were less directly affected by the activities of the company.

The interesting questions which Freeman’s work gives rise to is the closeness of the relationship, the nature of the influence of the company upon the stakeholder and the stakeholder upon the company. This expansion of the original concept resulted in widening the view of the firm from a strictly economic view to a political one to the extent that some

have theorised an extra dimension to its practice, describing it as “a theory of organisational management and ethics”. By this perspective, it would be important to assume that stakeholder management needs to be considered as a central part of the corporate strategies, operations and communication of contemporary organisations. In fact, different groups of stakeholders could include employees, trade unions, investors, customers, the local community, Government and media. Instead of an organisation’s primary emphasis that is on profits to shareholders, a stakeholder approach to business emphasises on the idea of being accountable to “other groups outside shareholders who are important for the continuity of the organisation and the welfare of society.” Given the importance of the stakeholder theory, it is important to map stakeholders, assessing their capacities and the power they have. This has been illustrated by Johnson in a power/interest matrix which underlines the importance of two issues: “how interested each stakeholder group is to impress its expectations on the organisation’s purposes and choice of specific strategies; whether stakeholders have the power to do so.” In other words, stakeholder mapping is important in identifying stakeholder expectations and in contributing to the understanding of political priorities. The power/interest matrix categorises stakeholders on the basis of the power they possess and the extent to which they are likely to have or show an interest in an organisation’s activities.

According to Cornelissen, the idea of the power-interest matrix is to allow public relations practitioners to formulate appropriate communications strategies on the basis of identifying and categorising stakeholders which importantly means that an organisation will know how intensely it needs to communicate with particular groups. Therefore, the practice of stakeholder theory relies on ongoing communication between an organisation and its stakeholders in order to build a stable, long term relationship that manages conflict that may occur in the relationship. What emerges from this description is that stakeholding always implies some notion of co-operation that drives individuals to, yet, pursuing their own goals but in a fairly harmonious way, within the rules, as part of a cooperative social system.

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3.2. Social capital: its development for building Governance

Social capital was conceptualized by Bourdieu (1986) who at first used to define the often informal contacts which linking members of urban communities together. He also defined social capital as the complex of resources and assets which are embedded within more or less institutionalized networks and social obligations, and which can provide members of such relational structures with different kinds of benefits. The importance of the concept of social capital, then, lies in the realm of civil society’s resources which are used to upgrade government’s capability of public services.

The term refers, also, to those specific features enabling people to act collectively, such as networks, relationships, norms, trust and, thus, the goodwill inherent in social relations. The other seminal social capital theorist, Coleman sees the concept of social capital as a way to escape the rigid assumptions of sociologists (social structure as the determinant of behaviour) on one hand, and neoclassical economists (self-interest as the determinant of behaviour) on the other hand, in the study of social actions. According to him, social capital is a set of assets which are embodied in the relations among actors. It consists of obligations and expectations, information channels and social norms, and has a positive effect on the creation of human capital (meant as knowledge and skills owned by an individual).

The two conceptual elaborations, which have been outlined above, have in common the nature of the concept and its instrumental value. However, they are inscribed in very different conceptual frameworks of society. Bourdieu has an intentional, voluntary vision of social capital, which is instrumental to his study of power structures inherent to capitalist societies and is, therefore, more concerned with the role of social assets as power and domination tools. Consistently with such a vision, the focus of its work, which is mainly conceptual and theoretical, is on individuals and struggling interest groups. On the other hand, Coleman’s vision and approach can be defined as normative and optimistic. Social capital assets exist independently of intentionality and are defined in an apolitical sense, as providers of benefits for their users. The focus of this analysis is mainly on individuals and households, meant as parts of a community. Therefore, the concept serves as an analytical tool for studying positive dynamics of human capital enrichment.

Coleman’s vision has proved to be the most influential among the two, probably in part because of the empirical and quantitative approach of the proponent, and in part because it is the main influence on the most popular conceptualization of social capital so far, the one elaborated by Robert Putnam. The author considers networking as a form of social capital, this way departing from the seminal definitions according to which it is rather embedded within networks.

The most relevant thing here, however, is the definition of trust as the key dimension. Albeit dealing, such as Bourdieu, with socio-political issues and adopting a proactive view, Putnam sees social capital as the basis of a pluralist society and the source of mainly positive dynamics, focusing on inclusion rather than struggle and power inequalities. Entitling social capital as a “bowling alone" phenomenon, his focus was on the phenomenon of voluntary associations and social engagement as an underlying factor behind the strength of political institutions. Critics have seen this approach as downplaying political and power issues, ignoring the vertical dimension of social relations.

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98 Bourdieu P., “The Forms of Capital”, in Richardson J. (ed.), Handbook of Theory and Research for the Sociology of Education, Wetsport, CT, Greenwood Press, 1986, (p.249). He defined social capital as “the aggregate of actual or potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance or recognition”
Whatever its limitations, Putnam’s work has, anyway, proven extremely influential both in regional economics and planning. As for the latter, the conceptual similarities with the institutional, collaborative tradition of planning theory and practice are evident. With regard to the former, his analytical approach to social capital theory is compatible with economic geographers’ conceptualizations and useful for the definition of a consistent theory of learning, to be based on a quantitative approach. He considered that social networks are constructed through investment strategies in group relations of mutual advantage. Here, the notion of social capital is considered in straightforward terms as an investment in social relations with expected returns in the marketplace. Linked with social network theory and based on the insight that economic action is embedded in social structure, social capital has become an “umbrella concept”, as Adler and Kwon argue, spanning from individual level analysis to community-level analysis.

The popular conceptualization put forward by Cohen and Prusak argues that “social capital consists of the stock of active connections among people: the trust, mutual understanding, and shared values and behaviours that bind the members of human networks and communities and make co-operative action possible”. In contrast, Nahapiet and Ghoshal adopted a resource-based view that also includes potential resources and define social capital “as the sum of the actual and potential resources embedded within, available through, and derived from the network of relationships possessed by an individual or social unit”. Adler and Kwon, stressing on the social dimension of social capital, have emphasized on the quality of these resources as beneficial assets since social capital is the goodwill available to individuals or groups. Therefore, its source lies in the structure and content of the actor’s social relations and its effects flow from the information, influence, and solidarity it makes available to the actor. What most authors seem to agree on is that there is potential value in the content of social network ties. Nevertheless, it would be more appropriate to consider Putnam’s definition of social capital and its indicators of trust and social participation to study its connection with the efficacy of stakeholders involvement during the phase of planning of a given territory since it is able to improve quality of democratic politics and the vitality of economic life of society. Development of social capital is to create social equilibrium with high levels of cooperation, trust, reciprocity, civic engagement, and collective well-being.

3.3. Social capital within the paradigm of Community Governance

Considering the emphasis that it gives to the territorial and geographical dimension and to social capital as a construct inside a given territory rather than something given by the history, the paradigm of Community Governance is very much connected to concepts of trust, generosity, reciprocity and collective action put in place to solve societal problems. The acute social and communitarian elements found within the CG perspective makes possible to understand and pursue development as a process which is not necessarily led by the Government that eventually contributed, in the past, to produce conflicts and increase gaps.

101 Ibarra, H., M. Kilduff and W. Tsai, “Zooming In and Out: Connecting Individuals and Collectivities at the Frontiers of Organizational Network Research”, Organization Science 16(4), 2005
but by a number of community’s actors that cooperate to achieve a common vision for the territory and its community.

By this perspective, the model of CG is based on the idea that there is an implicit monitoring process of the behaviour of each single actor engaged in the macro and micro decision-making process is made accountable/responsible of his/her own actions. To increase the community’s capacity to produce social capital, policies should be oriented towards investment that are more likely to improve the community environment’s conditions as well as increasing the number of places and occasions for personal exchange is increased. In a modern context where the territory and the community are nurtured by the spirit of communitarianism, the objective to achieve is, yet, leading the community to action but also to enable it to increase efficient actions of Community Governance based upon the capacity of the main actors to produce social capital at the territory’s level.

A reasonable synthesis of the multitude of approaches, and perspective of social capital, is the one considered by R. Putnam\textsuperscript{107} who, leveraging on trust, shared values, inclusive norms, willingness to aggregate in order to achieve common goals, identified three different forms of relationships. This perspective is the most coherent with the discourse made on the integration of community planning processes with those embedded with Community Governance. Robert Putnam introduced a method enabling to measure the level of social capital on the basis of its inner ability to express itself through different types of relationships which were produced according to the typology of social organizations. The latter, at turn, had been considered as an evolved form of relationships given by the evolutionary process occurring at the level of the community and territory level.

The first form of social capital is identifiable with forms of “linkages and bonds” which generate themselves at the micro-community level and therefore, on the basis of family bonding, they create strong and binding cultural values as well as physical proximity. The degree of trust and capacity to share values amongst the members of a community is usually higher than the one which is experienced inside a wider territorial community. The so called “bonding” social capital enables members of the community to take action to fulfil the primary needs of a community in a faster manner, hence, to grant support to those weaker individuals living the micro-community.

The second level of relationship, the “linking” type of social capital, is considered to be the evolved and advanced form of the former type of social capital that enables to create trust and to share values in wider territorial contexts so as they are prepared to share and cope, in an efficient manner, all the general social, economic and cultural issues as well as the challenges of a modern society.

The third type of social capital is called “action-based social capital” as it drives the territory’s stakeholders to move easily from situations where debate is heated to others where a common vision is shared amongst participants. This form of action-based social capital also leads actors to implement strategies after they are formulated by encouraging engagement of all individuals inside a community who are, directly or indirectly, interested to take part in the process of community building that as Hutchinson argue, “is the soul work of governance\textsuperscript{108}” as it creates support and connection within insecure and fragmented environments.

Due to the tension which characterises this type of social capital towards the goal of creating structured and durable relationships amongst actors, it is also defined as “linking” social capital. More specifically, the extent of impact that social capital is able to produce is better analysed in the approach suggested by R. Leonardi and R. Nanetti\textsuperscript{109}, who both distinguish

\textsuperscript{107} Putnam R., Bowling alone: the collapse and revival of American community, Simon and Schuster, 2000

\textsuperscript{108} Hutchinson V., “It is the Local that Learns - some thoughts on community governance”, Community Governance Forum, Christchurch Convention Centre, 2-3 June, 1999

\textsuperscript{109} Leonardi R., Nanetti R., La sfida di Napoli. Capitale sociale, sviluppo e sicurezza, Guerini e Associati, 2008
between two methods. The one used to achieve results, in other words, the *outputs* which are the results achieved by each single policy or single action, and the other one used to fulfil the *outcome*, that is the level of impact that a set of actions and policies produce at the level of territory's development and so, how they impact on both wealth and quality of life within a community.

<table>
<thead>
<tr>
<th>Types</th>
<th>Method</th>
<th>Output</th>
<th>Outcome</th>
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</thead>
<tbody>
<tr>
<td>“Bonding”</td>
<td>Self-help</td>
<td>Service delivered to micro-community</td>
<td>Increase of the group’s wealth</td>
</tr>
<tr>
<td>“Linking”</td>
<td>Formal associative networks</td>
<td>Programmes/sector actions</td>
<td>Territorial development</td>
</tr>
<tr>
<td>“Action”</td>
<td>Coordinated agenda of policies</td>
<td>Integrated policies to development</td>
<td>Sustainable development of communities and territories</td>
</tr>
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Communities, then, in light of their capacity to collaborate and working together amidst the context in which they live, are considered to operate as true government structures so that Community Governance becomes, then, a leading paradigm which defines and set up in motion a new mode of governing. Community governance, hence, is explained in terms of the recognition that the complex issues facing communities cannot be solved by any one person or sector alone but requires collaboration that is to better facilitate the concretization of Community Governance strategies, positioned within the realm of relationship-based strategies. The success of these strategies depend on the capacity of each subject or actor involved in the process to implement an internal change within its own category in order to facilitate the ability to communicate, to exchange information and establish a dialogue by engaging further sets of different stakeholders. Here comes, then, the paradigm of Community Governance which entails a method of governing the territory that is supported by coherent processes of community planning and allows the production of “linking and “action-based” types of social capital. Therefore, this is a method which enables the definition of programmes, actions and integrated policies that, in turn, contribute to generate an authentic and long term sustainable development of communities and territories.

This view is supported by the existence of social capital as a construct, which represents the community resource *par excellence* and favours the creation of skills and abilities from which new relational opportunities can derive and which drive actors to embark on further actions that would start off processes of capacity building.

### 3.4. Capacity building approaches to sustainable development
Capacity building stands as an rather unusual subject in development that also lacks an that in private sector, instead, it is usually called business management. The lack of conceptual clarity on capacity development, however, which is often used synonymously with institutional development and state building, does not mean that the term meaningless and powerless. Traditionally, the notion of capacity came from the engineering world, and was understood to involve using particular processes to transfer knowledge, especially technical

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and scientific skills. Little attention was paid to the realm of policy formulation, social and economic research, systems analysis. The acknowledgement that knowledge cannot be transferred and has to be acquired, learned and reinvented has drove practitioners to allude that the application of capacity building and development becomes meaningful when it refers to the encompassing of both the deep pool of local understanding that is the very foundation of learning and the outside information that can be reconceived to meet local needs.

However, it is possible to account several attempts, throughout the history, towards capacity development that made the term evolve as a vocabulary and that today teach clear lessons for the future. In the early 60s and 70s, capacity development was merely used to deliver the meaning of a way to design development aid policies summed up in the concept of “technical assistance”. These words connoted the idea that rich countries have a monopoly on knowledge. Then, in the 1980s and 1990s, capacity-building came on the stage as a key concept of development aid which was widely recognized as its main goal. At the same time, the United Nations Development Programme introduced full-fledged changes in the way of measuring the impact of aid by launching two instruments: the human development index and the annual Human Development Report which both gave an important role to human resources development and institutional development. Therefore, more than the words, what has been constantly evolving is the “technology” of development cooperation.

Considering capacity building as an endogenous course of action strengthening the existing capacities and assets, it could be found across three overlapping layers: individual, institutional and societal.

For its very nature, its application became very much used to refer to processes of development that influence not only the organizational competencies and skills of people and the community as a whole, but also the development of institutions and their capacities to bring about change in the area of “stateness”. Each dimension involves learning and transfer of knowledge to meet the needs arising from each dimension itself.

Capacity development is an approach that is mostly used and adopted by those countries where the communities have often proven to be resilient in their conflict-affected and fragile contexts providing survival and coping mechanisms for insecurity and fragility. The discussion on capacity development can be seen as limited to communities and people to be empowered and to developed countries to be “helped out”.

In other words, capacity development is pursuable to the extent external agencies, or better, third countries are involved in the process of their fragile context transformation together with the work done by a resilient community. By this perspective capacity building and development in a given geographical territory is something to which international aiders/donors can contribute. The implication of this would be that interveners will need to consider the extent to which they are able to bring about change taking into account that capacity development is a necessary but insufficient component of state building; that more often than not it is institutions that are the real challenge for capacity development, and that it is particularly difficult for outsiders (especially foreign donors) to bring about development in those institutions. And Kosovo presents a real contextual lessons that has been learned about capacity development as it has been described in paragraph 3.2.

The experience in Kosovo clearly demonstrates that even in areas of sheer desolation, social life and organisational systems can readily re-emerge within community networks on the basis a manifest attitude towards resilience by the local community.

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112 Morgan Peter, “Technical assistance”, UNDP background paper, 2001
113 This critique was spoken in plenary by Peter Morgan, a freelance CD researcher and writer, at the Capacity Development Day at this years WBI 50th Birthday celebration. Washington, 8th June 2005
Having accounted that, however, today practitioners in this subject field recognise that capacity development has a threefold dimension as the World Bank’s pronouncement declares: capacity is “about skills, performance and governance”. This would assume that outside aid would not produce any effective implications nor would stand as a useful practice if it merely meant developing capacity as a pre-occupation with training and providing technical assistance. Dealing with capacity development, then, goes beyond that and it means “dealing with the capacity of individuals, organisations and the broader institutional framework within which they operate to deliver specific tasks and mandates”. In other words, developing capacity requires more than a well structured organization and system where skilled people are able to implement policy priorities by means of a good management. It also requires a supportive institutional framework made of formal (including legal system, property rights, etc, etc) and informal (norms and values that influence individual and collective behaviour) institutions. Only when these three sets of elements are aligned, the drive for harmonization and convergence around the three dimensions can lead to a developed capacity on a sustained basis.

Apart from emphasising on the operational implication that the process of capacity’s strengthening may produce so that, by virtue of the fact that strengthening cannot be overall, everywhere and all at once and, hence, it would need to be built in certain key areas, the incremental approach, at this stake, seems to be given a prominent importance as it takes into the area of good governance. To conclude, this paragraph introduces an provocative notion of capacity building/development that would rather convey the meaning of an approach, or merely, as an endogenous course of action that builds on existing capacities and assets, and the ability of people, institutions and societies to perform functions, solve problems, establish and attain objectives.

The attempt of building and developing sustainable capacities that, at turn, would ensure a sustainable development, is a long endeavour as it involves education, training establishment of viable organizations until provoking societal changes. Successful development responses account for this reality, and tend to be found where national agents, local communities, academia, the private sector and external partners come together and devise tailored responses, taking into account the uniqueness of each situation, identifying current capacities and determine those that need bolstering.

4. METHODOLOGY
The overall scope of this study, based on a hypothesis-generating research, is to attempt to provide an answer to the following research question: universities are sites of social capital construction towards conflict transformation and sustainable development? The collected data and information as well as the social phenomena emerged from data and findings, have referred to the multidimensionality of the network that Universities have been able to establish in Croatia and Kosovo which enabled them to achieve levels of sustainable development through their utmost capacity in empowering communities by leveraging on social capital stocks. The activities purported by Universities have, moreover, induced the establishment of appropriate and adequate mechanisms leading actors to take sustainable decisions.

In order to respond to the research question and understand the extent of University actors’ capacity to contribute to sustainable development within their localities, an empirical scrutiny has been conducted at the Universities’ level, in Croatia and Kosovo, that have been

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117 Hickson D.J., Managerial decision making, Dartmouth, 1995, p.78
translated into researchable entities. These have enabled to analyse the extent of their capacity to transform the conflict and deliver, at the same time, some level of development within the territory they are located.

Moreover, as a context analysis research based on a qualitative investigation, a great range of targets and phenomena have been analyzed and the collected evidence has intended to map the variety of what is being done within universities in Croatia and in Kosovo to promote civic responsibilities, democratic values and collaborative network based approaches, and therefore to produce social capital stocks. Therefore, the documentary information has been useful to assess the actual activities purported by universities and the capacities they have developed in enhancing civic responsibility and community empowerment as well as how they did contribute to these outcomes whether they are entities of private entities (as it is the case in this paper referring to the situation in Kosovo) and or public ones (as it is the case for the Croatian Universities selected for this paper).

The accumulated documentary evidence includes the gathering of official documents, records, publications, official statements and policies from relevant officials, collection of survey data statements and selected informants’ experience and knowledge. Interviews have been conducted on the level of individuals from targeted groups in the university and community and they are designed as source of information for third part (summary) and a pre-test for the development of a more focused context analysis. Group interviews have involved about 80 participants overall, divided in two categories:
- **60 respondents** falling into the Croatian lot (30 respondents coming from Zagreb and 30 respondents from Rijeka)
- **20 respondents** coming from Kosovo, more specifically, from the city of Pristine.

Respondents, as regards to both countries, have been recruited amongst managing body representatives, university teaching and teaching staff, administrators working within University offices and dealing with international funded projects, institutions and their representatives, business actors and civil society activists and local media.

The overall data have been translated in a summary, evaluative narrative of what the university is doing in education with the aim to produce social capital stocks enabling the transformation of a conflict affected community and the pursuit sustainable development within its locality. The research has developed according two main steps:
- the categorization of targets in students, faculty, and administration and their relationship to local government, schools, business, media, and civic groups;
- the delivery of questionnaire to those target groups and the conduction of surveys;
- analysis, formulation of recommendations, and distribution of materials that can be used by institutions of higher education to discuss and decide their responsibilities for civic education and democracy.

I. Universities

The selected Universities in Croatia (University of Zagreb and University of Rijeka) and in Kosovo (Iliria College in Pristine) have been identified according to their different component groups who will also be the participants of this study: students; faculty and administrators. Students have been recognized by the degree programs in which they are enrolled, especially by first and second degrees but also by courses of study. Today, they are also grouped into regular students and “non-traditional”, students who are not in degree programs, studying in specialized courses of student, or taking courses on an irregular basis. Faculty are either standing, regular members with and without permanent appointments, categorized also by rank and school or “adjunct”, often part-time. Administrators are generally divided into academic and non-academic, with the former holding decanal titles and
the later having various kinds of organizational positions, some of which are specific to universities, registrar being among the most common.

In selecting individuals from these categories, the purpose of the interviews is information about the institution and its relationship to its localities. The selection is made on the basis of the best informed rather than representativeness. Thus, the questions provided are directed to what students, completion of their studies and acquisition of qualification, do in the community.

The information sought from the informants fall into the research questions connected, accordingly, to their relative independent variable (or dimensions) set up at the beginning of the qualitative and are listed the follows:

- “what is the extent of the University’s external linkages and how is it interconnected with local partners?” - this variable seeks to evaluate the external dimension of University and its interconnectedness with the outside world;
- “what programmes do Universities have which are relevant to produce positive implications on the territory’s growth?” - this variable seeks to analyse the internal dimension of University as well as its internal structural capability;
- “how the state/government proposes to do with universities for the purpose of achieving some forms of development?” - this variable seeks to investigates the national dimension in which University operates.

a. Students

The selection of students has been made on:

- regular students (to whom it will be asked which of them they know are the most active or best informed about what is going on at the university);
- part-time students (those attending non-degree educational programs, something which is accelerating with distance learning on the internet, expanded today in programs for “life-long” learning);
- non-traditional students (those attending special programs for training people active in their professions and the work force and they are expected to be drawn primarily from the locality or region).

As this research is directed to universities as sites for democracy, attention will be given to students residing in the locality were the university is positioned, whether or not they are enrolled in degree programs. A number of 2-3 students have been selected for personal interview and 20 for group interview.

b. Faculty

The faculty selected should be from two groups:

- Teaching staff
- Research staff

Both are directly involved in teaching and programs about democracy and citizenship. A number of 2-3 faculty members are selected for personal interview.

c. Managing body

From the official faculty representatives, few component of the managing body, from the faculty senate have been selected. Since different faculties or schools within the Universities are involved with the community in different ways, faculty selection has reflected the main ones. Medical departments have health programs involving local community; public administration/social sciences departments may have close links with the local governments; business schools may use local businesses for apprenticeship experiences, etc, etc.
II. Local government officials
The starting point of these interviews has been the mayor’s office. In some places it has been relatively easy to interview the mayor; in others, the deputy mayor or the senior administrator officer in the mayor’s office have been the respondents. There has also been a request of an official policy statement from the President, Member of the National or the Local Parliament regarding the university’s official posture regarding the university’s role in civic education, civic responsibility and democracy, and their position and reaction to the conflict they underwent.

III. Local media
The link provided by the media between the university and its locality is critical to how the local and university are related. The editor or producer in charge of the local news (metropolitan page) or reporters with specific assignment to cover the university has been interviewed. This due to the fact that an increasing practice of universities is to take part in regular electronic media communications.

IV. Civic Groups
For purposes of this research, representatives of the major civic groups connected to the topic of sustainable development and alike have been selected. As informants, these representatives have been asked about the university’s contribution to civic life in the community. A number of 4-6 personal interviews has been sufficient to assess contacts with local community and the university.

V. Business groups
Business enterprises have one or more local associations, including world wide “Chambers of Commerce” or one or more “clubs”. One representative of such groups or head of important business company have been interviewed and asked about the university contribution to business life in the community.

5. RESULTS
Based on the results of the qualitative research conducted in the two geographical scope’s areas in the Balkans, Croatia and Kosovo and their sample localities, Zagreb, Rijeka and Pristina respectively, and taking into account the analysis of collected data and information defined per each target group and locality, some trends have come out of this investigation. The general academic contributions provided by this qualitative investigation that substantiate in a set of similarities between the two countries analysed include:

- a subscription to the constructability theory of social capital, a measurable increase in the social capital stock of the target groups;
- an increased capacity of youth organizations’ leadership on to prompt local and regional policy makers to focus on sustainable development;
- the analysis for understanding the relationships among higher education, institutions, civil society, business actors and the community as a whole;
- an empirical basis for developing theories of democratic development in the global era through the engagement of high education Institutions together with economic stakeholders in planning decisions for the community and the territory;
- the creation of horizontal alliances of target group organizations and leaders, hence an increased participants’ awareness of the mutually supportive relationship between social capital and peace: social capital induces development; open borders and peace nurtures it;
a participatory process that have led to value-system changes as well as broad-based associational engagement via group and inter-group based participation activities (positive-sum-game paradigm).

Together with the academic contributions achieved, the qualitative research has also produced the following eminently expected results:

- The maximum frequency of engagement with industrial/firm partners is found at Iliria College of Pristina in Kosovo and, for the Croatia part, at University of Rijeka, mainly in the Department of Technology and Civil Engineering due to the extensive harbour and shipbuilding related activities in the City of Rijeka, while in the case of the University of Zagreb, interaction has occurred with community partners as well as welfare partners. All three universities in this study, show that the frequency of interaction with the government partners is also optimal. Civil society partners are also maximally engaged with the University of Zagreb as well as with research department of the University of Rijeka and with the Iliria College of Pristina. This reflects not just the significant level of community engagement of the universities in general but also is an index of the type of research that research institutes in the post conflict Croatia and Kosovo have focused on. As far as Croatia is concerned, it is not out of context the needs that a post conflict country as Croatia, has for both basic and applied research in order to catch up with the rest of the EU member countries. By the same token, the fact that the Technology and Department of Engineering of the University of Rijeka have engaged frequently with industrial/firm/business partners is also an index of the metropolitan fairness of the industries as well as the ability of the University of Rijeka, with its new built campus, to provide a meaningful research product to the industries/companies. The engagement with other external partners is mainly informal and academic.

- At the University of Zagreb, located in the capital city of Croatia, whose major focus is international academic recognition, local needs and demands have been embedded within the broader objectives of the universities. By this standpoint, a super imposed institutionalization of the University itself which has been allowed to evolve as much as organically from its own grassroots in accordance with its own perceived need for international recognition.

- At the University of Rijeka, with its focus on city development and urban reconstruction, the interaction with external social partners has not changed much given that the community engagement has always been accepted as pivotal to University academic culture in that locality mainly due to its geographical position closer to the Italian and Slovenia. It is also reflected by high frequency of engagement with academic partners in local government and social as compared to universities in the study.

- Both Croatian Universities and the Iliria College of Pristina in Kosovo show that they have courses and programs which are directly related to democratic citizen education, either with strictly related courses/programs on public policy, public administration, or government, either with programs or courses may be focused on the locality itself, dealing with specific problems (such as housing, urban development, transportation, or simply a seminar or course on the city as a place. Of particular interest is the result which considers joint locality-university activities, the extent to which the locality presents itself as having the opportunities of a university, and, especially, the university’s involvement in various civic projects and programs that enabling the production of social capital and, hence, ensure a degree of development within the locality.

- The focus on the academic interaction has been translated, as far as the two Universities are concerned, into an active engagement with other social partners like civil societies and
other communities. The external interaction that all three universities, amongst which two are public and one is private, have established with firms and government partners is also outstanding as it shows the will to engage with local innovators at the grassroots level (informal level). The University of Rijeka has a broader paradigm of engagement with external social partners compared to all other universities. This is reflected in the high scores it obtains in the engagement with government, community, civil society partners. However, the niche where it is located makes it inevitable that it will engage with external social partners and could be a fine example of grassroots evolution of university–community engagement.

Out of the secondary data and the narrative of the surveys’ participants there is information that Universities, as far as Croatia is concerned, both in Zagreb and Rijeka have contributed to:

- train more than 1,500 students as youth leaders at 17 different locations along the borders of the war;
- engage more than 35,000 young people in youth activities in more than 50 youth centres and clubs operated in cooperation with the local municipalities of Zagreb and Rijeka and neighbouring municipalities;
- sign more than 80 contracts with local municipalities, local universities, regional and national governments;
- ensure continuous coordination with other international organisations through the Stability Pact Working group on Youth, OSCE, UNDP, UNICEF, Council of Europe, European Union and others;
- design and initiate an inclusive and participatory youth policy reform process.

The two main objectives that the Croatian Universities have concretely achieved relate to the special programmes set up in motion as a part of education activities, when participants committed themselves in practicing the development of small-scale projects on their own or through the local organisations which manage similar kinds of projects. Amongst the projects it is important to remember:

- the Learning Exchange Program intended to strengthen the relationships between university courses and its governmental counterparts, and to enhance the integration of program’s youth work into local governmental structures;
- the Youth Policy Program was developed specifically for the area of Zagreb: interventions focused largely on assisting the national and local governments to progress on creating action plans for recovering policy after the conflict. The core logic of the model is based on tight links between education, youth work and societal legitimization/youth policy.

The differences that have emerged from this study, instead, refer to the diverse nature/legal status of the universities engaged in the capacity development of the territory, since the drive for change in Croatia has been given by public education institutions, while in Kosovo, prominent has been the role of the private Iliria College University in Pristina.

In fact, the latter, as one of the most successful private entity institution in Kosovo, against the apathy of the public Universities in the country, represents an outstanding case of successful actions oriented towards a sustainable capacity development within the community that has, by the same level and extent, been conducted in Croatia by the two Croatian Universities above analysed, which are of public nature. In other words, although the substantial difference between the Croatian and the Kosovar Universities in terms of their
legal status, the actions that all three have purported and carried out seem to have driven to the same direction, that is towards capacity building and community development.

Differently from Croatia, given the diverse political and social situation, Kosovo had undergone a period of threefold reconstruction, physical (new equipping of schools and the university), legal (creation of new, normative basis for school and university structures) and academic (curricula-development, school and university management, transfer of know-how etc.), without which the private universities (those funded and supported by the international players unlike the public ones) could not be able to deliver what has been in the latest ten years provided.

Far from considering the role played by the private Universities as Iliria College, one could objectively see a gap between the claim of public university in Kosovo to be the only legitimate official authority delivering education on the one hand and the lack of manpower and organizational structures for the implementation of steps necessary to move and transform the education system on the other. In a country with weak capacity at the end of the conflict, the international players such as USAid, the Friedrich Herbert Stiftung Foundation and other international donors have enabled, through the support and encouragement given to any private initiatives to set up education institution like universities (Iliria College is the case, here), the integration of the external expertise directly into the institutional framework through gap-filling. The latter has served to ensure that the community could develop its capacity from the inside, which is a preferable action than setting up parallel institutions.

As the case of Iliria College of Pristina in Kosovo, international third agencies have helped the University itself from its start to develop the organic capacities of the organization by putting in place monitoring activities as valuable mechanisms for learning, adjusting to circumstances, for evaluation and codification of knowledge. The case suggested by Iliria College demonstrates that the presence of international players has been a realistic way of integrating external inputs into national and local priorities, processes and systems and also providing assessment of the results and successes from collective undertakings. This would not be possible for public universities that have not made themselves subject to the international community’s help.

The main result as far as Kosovo is concerned is related to the fact that the presence of international third parties in Kosovo for conflict transformation purposes has been fundamental in making a contribution to state building and determine the extent to which an effective, developmental country could emerge. Along these lines, UN different agencies and the USAid have been able to work less with critical state organisations but more with private initiative’s organization and impose overly technical or managerial solutions although evidence suggests that organisational capacity can be, in some ways, built.

The research conducted at the Kosovo’s level, and ore specifically on the Iliria College of Pristine, shows that the capacity has been built thanks to modest and incremental reforms that have been pursued in a politically supportive environments. The success demonstrated by Iliria College University, as a private institution, has depended on the wider institutional reforms that it has contributed to conduct and y assisting the government in achieving real increases in capacity within the opportunities and financial support given by the international community.

Overall, the programmes and actions conducted by all three Universities had the aim to support and facilitate processes of reconstruction after the war and improve the prospect for a lasting peace as a value by means of augmenting the social-capital stock of as the sine qua non condition for reversing the trend of underdevelopment and marginalization. The content of these programmes and courses are consistent with the aim of universities in defining activities by which target groups and their leadership incrementally share mutual trust and
acquire solidarity and peace values. In turn, this facilitates their capacity to act together on such values as they commit to a vision of change for peace and to the formulation of development projects by engaging with local institutions.

Spawned by the conduction activities, the ‘virtuous loop’ of social-capital building through iterative interactions – civil society >>> institutions >>> increased social trust, peace values and engagement >>> new development opportunities >>> increased institutional capacity >>> civil society’s increased commitment to peace and sustaining its aftermath, and so on – is set in place. In particular, the leadership of youth groups were called to task by the conducted activities, because this target group represents the pivotal force of change for the future of the peace process. The action’s strategy of social-capital building to promote a lasting peace centres on the key element of partnership. To be effective as a means of transformative development as well as self-sustaining in time, the University programmes define partnership amongst the community and requires it as a relationship among equals. Although diverse peace programmes have been conducted and imposed just after the end of the conflict in both Croatia and Kosovo, even though at different times, by the international community in order to transcend and transverse the critical war lines with the objective of bridging deep social cleavages, these have not been inclusive in nature.

Rather, what Universities have done, has been to incorporate various strata of economically able participants as being multi-sectorial in scope by embracing the multi-dimensional concept of sustainable development rather than a simple growth. While the cities of Zagreb and Rijeka, through their Universities, have been the promoters of conflict transformation, the whole of the Croatian country seems to have benefited from these actions. The same find empirical evidence also in Kosovo where private Universities, Iliria College at the forefront, have been able to acknowledge, thanks to the encouragement given by international players, the critical importance of academic freedom and institutional autonomy for the social reconstruction and development of the country. While the global network of Western universities and other institutions of higher education have always been the pioneers in producing a solid foundation for the sustainable development of their communities, in the post conflict countries analysed this was not given for granted at all. Yet, the work done by the international community together with the local communities in developing organic capacities and find correspondence between societal, political, cultural and ethical basic consensus demonstrate that development strategies are not sustainable and potentially successful enough if they are simply imported from the outside and do not find a developed local social capital. Capacity development is not a “one-size-fits-all” economic development model, applicable to all situations and all national realities because societies have their own means to determine their destiny as it has occurred in the experience of Kosovo, differently from what occurred in Croatia. Capacity development, in other words, is the ability of people, institutions and societies to perform functions, solve problems, establish and achieve objectives as it embodies the fundamental starting point for improving people’s lives.

6. CONCLUSION

One of the most important element that has been used for understanding the transition and reconstruction during the last two decades in the Balkans has been investing on human capital through knowledge that is an irreplaceable factor of social and human growth as it fosters citizenship, empowers citizens with the necessary competencies for working together, and with an awareness of shared values and belonging to a common social and cultural space. Without social capital constructed by Universities, both the post conflict societies at large would have collapsed and, this is only the case for Croatia, it would have not been able to join
the circle of the European Union which advocates principles of democracy, sustainable and inclusive societies.

The role of universities or public research institutes have played in Croatia demonstrate the extent they have been able to offer the community and their territory ways of capacity building that have facilitated the growth of social capital and, at the same time, they have stimulated turning science and innovation into a key instrument of community development as well as regional development in terms of socio-economic returns. The Croatian experience stands as a teaching lesson for those conflict affected and fragile countries that should be able to adopt the methodology of synergy base collaboration and cooperation amongst actors where local authorities together with Universities work in partnership and take measures to create a “stairway to excellence” for learning entities, including people and all social and economic actors who operate within their locality and within their areas of responsibility.

This qualitative based research has explored the actual activities carried on by higher education institutions in supporting and promoting not only democratic values and practices, but also in impacting on the civic development of their students and in strengthening the engagement of young people with campus mates, local communities, civil societies and the wider society. The role played by Universities has been fundamental in launching a process of change that began to create lasting relationships and committed networks of social, economic and institutional target groups. By doing this, the Croatian communities, as for the Kosovo’s community, have been able to establish the foundations for their acting on development projects as well as for the process to be expanded to others. Yet, no significant plans would have ever been undertaken at the national, regional and local levels without any systematic and consistent program for cooperation and/or integration developed by Universities.

In this way, Universities in the two post-conflict countries have demonstrated to have assumed the responsibility to ensure that higher education advances knowledge on sustainable democracy, civic engagement, human rights, and diversity and provides its society with transferable competences needed to build and maintain a sustainable society in which future generations will be able to live. Moreover, in their attempt to create a comprehensive structure able to channel young people’s contribution to guarantee sustainable and peaceful development, it has been crucial for them to create the conditions for cooperation among all actors and levels of education to improve the opportunity for all to benefit from higher education. In fact, it is universally acknowledged as paramount that education and educational cooperation is pivotal in the development and strengthening of stable, peaceful and democratic societies, the more so in view of conflict situations where Universities can act, in as much as they did in the western civilized countries, as illuminist and liberator from tutelage of the others.

The results of this research clear set up three main arguments:

- Universities are treated as machines for economic development
- Universities are treated as sources of civic engagement which contribute to the social progress of the communities in which they exist. This is especially demonstrated in Croatia, but it could be also the case of all developing countries and Kosovo today, which have their own social systems that have evolved in their domestic contexts.
- Universities are treated as sources for human development though their focus on the inclusiveness of technology for the human development. As it has been possible to understand, University activities involve generating, transmitting, applying and preserving knowledge for the direct benefit of external social partners (industrial partners, academic partners, community partners, welfare partners, government partners and civil society partners) in ways that are consistent with Universities’ missions.
The threefold nature of the activities conducted by educational institutions empowered with intellectual leadership, knowledge acquisition, diagnoses, and strategic intervention to conflict transformation enables the pursuit of conflict transformation through diffused mutual trust and peace-oriented value system. In doing so, Universities have set in motion a system of economic and social interactions vis-à-vis the communities around them and have readdressed the issue of inequalities through a systematic integration of community engagement in relation to the three-fold mission of teaching, research and service. This leads to consider Universities as learning organisations with intellectual leadership that, with their continuous in-service training, have also worked in function of perpetuating the model’s mission, values and structure through community-oriented projects. However, it is important to note that Universities have not acted in isolation, but in cooperation with political and managerial leaderships. The coming together of socio-economic groups and institutional representatives to learn about why and how to pursue a common vision of development for the region is a prerequisite for strengthening the communities’ capacity as a partner in the peace process and thereby giving that process greater equity. This effort has substantiated the theory advocating social innovation as something that entails a behavioural change occurring at the individual and at the societal level which also requires significant flexibility, re-distribution of power amongst organizations in order to call for a collective leadership as a necessary practice for achieving successful governance and sustainable development within communities and territories.

As both geographic experiences have been able to demonstrate, Universities have depicted themselves as being more than mere educating structures which go beyond their first and basic function, as they offer a tools to trains young persons in skills and abilities that enable them to engage in community-based activities. The success of the Croatian and Kosovar models, although differently originated, stands in its role of empowering the community coming out from the conflict providing communities with the organisational tools and resources to carry out such changes and improvements. Empowerment was promoted through the provision of information, inclusive participation and decision-making, capacity building and the means to implement decisions. In the pursuit of sustainability and in the attempt to guarantee certain level of sustainable development to communities and territories, the strategic role of Universities in both countries, at the aftermath of the war, have represented as an index of that intellectual apotheosis in their effort to contribute to the advancement of their own communities and territories through their dynamic force in producing social capital and creating non-violent alternative forms of community organisation.

They have contributed to the development of a collective vision, an envisioned cooperation to achieve shared goals, and the creation of safe spaces for dialogue that has demonstrated to have the potential to lessen tensions, to (re)build interpersonal and collective trust and to foster a sense of interdependence amongst communities and across territories.

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Section 2
Enterprise in Turbulent Environment
THE NECESSITY AND INFLUENCE OF HUMAN RESOURCES TRAINING FOR OBTAINING AND INCREASING THE PERFORMANCE OF MULTINATIONAL ORGANIZATIONS

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ABSTRACT
Increasingly more multinational organizations are concerned about identifying new resources and mechanisms to ensure a continuous and significant performance. The challenges posed by this reality, constantly changing, led to theory and practice, in general, those in the field of multinational organizations, in particular, to seek solutions to manage the obtaining and performance improvement by each of them.
In this context, it became necessary the reconsideration and revaluation of the available resources potential, human resource being by far the most important. Thus, a certainty is that human resource redefine their place and importance in multinational organizations and their management.
On this current reality and, of course, present also in the future, in the amplitude context of produced changes in the economic scale and not only, knowing and applying the best strategies specific for human resources training, capable of contributing to the acquisition of new knowledge, skills and abilities necessary for effectively perform the duties of a particular job, constitutes as essential aspects to be taken into account by human resources management within any multinational organization.
Thus, theoretical approaches and practical work in this field, directed towards enlarging the area and deepen the specific aspects of human resources training influence on delivering performance of multinational organizations, are increasingly becoming the most appropriate support of multinational organizations in a position to provide acquisition and increased performance.
The content of our work, we addressed certain aspects of human resources training field, from a perspective of theoretical and applied research, which is subject of an comprehensive study that targeted the relationship between human resource development and growth of multinational organizations performance.
We consider the issues raised in this paper as actual and as a starting point in solving problems faced by multinational organizations in human resources field as certain possibility to obtain performance.
Keywords: human resources management, human resources training, multinational organizations, performance
1. INTRODUCTION
The training area of human resources has experienced and will know constant and dynamic changes, caused both by the specific beginning of the twenty-first century, of the development of knowledge-based organization, and the need to find the best solutions to transform the management system of the organization, in overall, of multinational organization, especially, in an authentic and powerful stimulator of their performance. Thus, based on the idea that no matter how trained and experienced would be a potential employee, when he enters into a new multinational organization, still needs a training period to learn the specific procedures that will enable him to perform his tasks with success, and thus to contribute to the obtaining and increasing the performance of the organization. In this sense, multinational organizations set and project as well as possible the training requirements, to assess the short- and long-term effects, and act to know and apply the best methods and techniques specific for training the human resources to obtain organization’s performance. The intelligence, knowledge and particular experiences that any multinational organization has, need to be managed and amplified towards increasing their quality in order to ensure continuity of professionalized human resource training. This requires the implementation by the management of the organization and human resource management of a specialized and systematic transmission system of knowledge and gained experience, as well as the skills needed for further development of human potential, this becoming fundamental pillars of modern multinational organization. Thus, the theoretical approaches and practical work in the field of human resource management has directed their effort to significantly widen and deepen the specific aspects of human resources training as need of its effective management and as objective and realistic support of obtaining and increase performance of multinational organizations. Given these realities, our study aims to present some theoretical considerations and conclusions of a research which focused on the relationship between human resource management and performance of multinational organizations.

2. THE PLACE AND ROLE HUMAN RESOURCES TRAINING IN MULTINATIONAL ORGANIZATIONS TO ACHIEVE THEIR PERFORMANCE
Training human resources represents a systematic process of acquiring new knowledge, skills and attitudes necessary to perform more effectively tasks of a particular post, present or future. This activity with educational character is carried out in order to improve employee performance and concerning the change at knowledge, skills, abilities and character level. Organizations nowadays are looking forward to have a competitive advantage against the present threats in globalization. Due to the high competency requirements, most organization aim to generate the kind of performance that can bring more profit. In order to do that, the employees are required to perform well and improve (Al-Qudah et.al., 2014). A study realised by Apospori, Nikandrou, Brewster & Papalexandris, (2008) suggested that there is a significant impact of training and development on organizational performance (Apospori et. al., 2008). According to another author, training and development is a main important element of human resource management (HRM) (Vlachos, 2009). Thus, we can say that the training of human resources in a systematic conception, generally involves a logical sequence of activities, from establishing a policy of principle and resources needed to support them, followed by an assessment of training needs which ensures appropriate program and ending with some form of assessment and feedback. This specific sequence of phases is contained in a training cycle. The training cycle shows in a logical sequence of activities stages with specific impact on the proper conduct of the training process (Deaconu, 2012,
p.29). Of course, to have positive consequences, human resources management from a certain organization, will determine in an actual and objective way the registration of their own activities in this managerial cycle of training. On the other hand, it will not break the formation process from the training process, which are fundamental components of completion and professional perfection of employees. In the conditions of modernization market economy and the requirements which ensures obtaining performance of multinational organizations, the need of staff training is amplified substantially. In this context, particular attention should be towards managers and specialists training, whose knowledge, skills and behaviors requires a radical renewal. Multinational organizations that ignore or underestimate this requirement are condemned not only to lower their economic performance, but even bankruptcy. Of course, is not very important only the correct understanding of the content and the need for human resources training, but also the adoption and use of the most effective ways and specific means in this sense. For this, human resource management, as specialized subsystem of multinational organization management, will consider certain factors that influence the training activity of human resources, of which we retain (Lefter, Deaconu, 2008, p.140): extent of changes in the external environment (technological changes, new legislative provisions, etc.); internal changes (new work processes, new markets, etc.); existence of appropriate skills and qualifications in the available workforce; adaptability of the workforce; extent to which the organization supports the idea of internal career development; degree of management commitment to the idea that training is an essential element for economic success; extent to which management considers training as a motivator at work; knowledge and skills of those responsible for management training. The knowledge and skills of workers through training have become important as it faces the increasingly rapid changes in technology, products, and systems. Most multinational organizations invest in training because they believe that will result higher performance (Kozlowski et al., 2000). Therefore, human capital plays a primary source of sustained competitive advantages to a firm because human capital has not only the four criteria but also can not duplicate or bought in the market by competitors. Applying the resource-based view to training suggests that training can provide knowledge and skills for employees and in turn, its might lead to high multinational organizations performance (Thang, Buyens, 2009, p.8).

From this perspective, training is effective to the extent that it directly contributes to the strategy, objectives, or central outcomes to organizational effectiveness (Jackson, Schuler, 1987).

Chapman (1993) has pointed that a major development in the theory of training came with the distinction between relevant training to a wide variety of tasks and training which is more specific to the job and organizations - general training and specific training.

Conditioning of training and human resource performance reveals a complex system of relationships that meet various fields of expression where the social and economic ones occupies a distinct place.

Considering the opinions of the specialists in this area, but also our own choices regarding this topical issue, we conducted a terrain investigation to identify the views of human resources managers on human resource training influence on the performance of multinational organizations, some of which conclusions are as follows.

3. THE RESEARCH METHODOLOGY

Organizing, conduct and completion of terrain research were based on theoretical acquisitions regarding human resources professionalization influence on the multinational organizations performance and on the requirements of scientific research methodology in social and humanity sciences. This study, correlated with the nowadays issue of multinational
organizations, we consider it as having special significance in terms of obtaining relevant information to the work theme.

3.1 Purpose, objectives and hypotheses

The study purpose is represented by the necessity determination and the influence which human resource training has on achieving multinational organizations performance.

Specific objectives

a. Determining whether the training of human resources contributes to the performance of multinational organizations;

b. The identification of specific human resources training activities that were carried out in multinational organizations to increase their performance;

c. Analysis of the effects of training human resources on organization performance.

The hypothesis from what we start in the investigation is suggested by the theoretical part of the paper where is outlined the fact that the performance of multinational organizations is dependent on several factors, of which human resource training has a fundamental role.

Thus the general hypothesis is: Training human resources contributes significantly to achieving multinational organizations performance.

This hypothesis can be operationalized, resulting the following statements:

a. The performance or failure of multinational organizations are determined, primarily by the training and the degree of human resources professionalization.

b. The more training activity resources is better known and promoted, the more the decisions made and actions taken to multinational organizations level will ensure obtaining their performance.

c. If accomplishes the proper employee training, then increases the diversification and factors quality which ensures multinational organizations performance.

3.2 Materials and methods

We chose the survey as a research method and the opinion questionnaire as a tool for investigation. Of course, in the sample selection and questionnaire application we have considered compliance with the requirements of scientific research methodology, and adoption of an ethical behavior. The research was conducted on a representative sample, consisting in 116 multinational organizations, of which 11 from Sibiu and 105 from Bucharest. The respondents were human resource managers in these multinational organizations.

3.3 Results and discussions

As a result of applying the questionnaire with specific questions were obtained a series of responses, and some of which are presented below:

The first question in the survey was:

1. To what extent do the following activities of human resource management contributes in achieving your organization's performance? (give marks from 1 to 5, where 1 means a very small extent, and 5 a very large extent)

<table>
<thead>
<tr>
<th>Variables</th>
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<tbody>
<tr>
<td>a. Human Resources planning</td>
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<tr>
<td>b. Human Resources recruitment and selection</td>
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<tr>
<td>c. Human Resources training and improvement</td>
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<tr>
<td>d. Human Resources performance evaluation</td>
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<tr>
<td>e. Human Resources motivation</td>
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<td>f. Human Resources promotion</td>
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After data results interpretation at this question were made three figures presented below:
From the figure above is noted that human resources motivation (the version is with individual score of 4.29) is considered by Sibiu respondents as the most important activity of human resource management, which may contribute to the multinational organization's performance. This proves that motivation, through its specific, must be done in the most efficient and complex way, both pecuniary and non-pecuniary. Also, as shown in the specialized literature (Drucker, 1950, 1976, 1990, Burciu, 2008, p. 145), the connection between motivation theory and managerial practice is vital for the management success, business success, coordinating a team of management and directing it towards performance. On the 2nd place, as a human resources management activity which contributes to the multinational organization's performance is considered to be variant (b) – Human resources recruitment and selection.

On the other hand, figure no. 2 shows that respondents from Bucharest placed first, as human resource smanagement activity that contributes to achieving multinational organization performance, variant (c) – Human Resources training and perfecting, with an individual score of 4.13. Thus, this confirms, once again, the importance of this human resources management activity, which decisively influences the performance achieving in multinational organizations, just as Kozłowski (2000) suggests that one of the approaches to organization improvement and development are based on enhancing the knowledge, skills, and attitudes or abilities of the workforce. This may be accomplished through training activities.
At the global level of multinational organizations from Sibiu and Bucharest (figure no. 3) is observed that variant(s) - Human Resources motivation with an individual score of 4.15 remains in first place as human resource management activity that contributes to achieving multinational organization performance.

Although every multinational organization has a collection of talents, knowledge and experiences, it is important that they be properly managed, to maintain or develop heritage as their own intellectual, through training and improving human resources by applying by the human resource management a system for the transmission of a systematic knowledge and experience, as well as the skills needed to increase its performance.

The existence of these opinion differences among Sibiu and Bucharest respondents reveals the existence of different policies and strategies of justification and supporting human resource management activities. Therefore, every multinational organization, only through effective fructification of the scientific research results and modern practices can optimally correlate human quality with product quality achieved through a realistic policy and open for increasing permanent standards recognition by them.

In this regard, the next question content becomes relevant, not only for our research but also for the theory and practice of human resources management directed by multinational organizations performance. Thus, this question was formulated as follows:

2. How much influences human resources training activity the obtaining of multinational organizations performance?

The results of this question are presented in the below figure:
The data shown in the figure above indicates that respondents both from Sibiu and Bucharest believe in a large number, that training of human resources influences the performance of multinational organizations. More than half of respondents believe that the performance of multinational organizations is much and very much influenced by human resources training. Awareness of this leads to a focus on human resources subsystem with a significant role in multinational organizations.

Another question in the survey, with a distinct relevance is the next one:

3. Arrange, according to their importance, the following managerial policy priorities to ensure your organization’s performance (note from 1 to 5 in order of their importance, grade 1 being the most important).

a. Making products / services of superior quality
b. Employees motivation
c. Linking the supply of products / services with customer requirements
d. Employees training and perfecting
e. Organizational culture promoting

From figure no. 5 results that multinational organizations respondents placed first, at this question, variant (d) Employees formation and training. 30.17% of them chose this response option, as managerial policy priority to ensure the performance of their organization. On second place is the variable (b) - Employees motivation, which supports the views expressed above.

Next, a question closely linked to all the other questions in the questionnaire, has the following content:

4. What activities of employees training and perfecting were carried out by your organization over the last 3 years?

Training and perfecting employees activities, analyzed for the past 3 years within multinational organizations, by weight of 55.50%, proving that they were materialized mainly by: initiation, training and specialization courses in the fields of IT; management; legislative analysis personnel transportation; public procurement; risk management, internal control and corporate governance; internal auditor; waste management etc.

An important percentage, namely 23.10% of the organizations surveyed, indicated that since 2012 and until now have not conducted any training and development activities of their employees.
Although the calculated percentage is not high, given the real possibilities of organizing and conducting these courses, we refer to specialized human resources, so that the weight is reasonable and even realistic.

For organizational management is required a policy able to permanent the employee training and improving, and for human resources management a clear evidence to pursue career development of each employee and organization development strategies in order to harmonize them.

The next question to which we will present the answers is the following:

5. To what extent do you agree with the statement: human resources should be considered the first strategic resources of an organization, regarded as investments, not as costs.

This question brings to the fore the fact that more than half of respondents believe that human resources should be considered strategic resources of an organization, given their importance in achieving its performance. Also, they are considered to be an investment for organizație, not a cost.

A special importance in achieving multinational organizations’ performance has the choosing of the most suitable training program. A question related to this aspect is the following:

6. What is the type of training program that applies most frequently in your organization? (Please, choose one answer option)
   a). Traditionally, that involves physical presence at the course throughout its entire duration;
   b). At distance, which implies, in particular individual work and some meetings with trainers;
   c). online (by Internet), which does not requires such meetings face-to-face between trainees and trainers;
   d). Combination between traditional and distance one;
   e). Combination between traditional and online one (by Internet);
   f). Another form. Which One? ________________________

![Figure no. 6: Interpreting the data of the question no. 5 from the questionnaire at a global level (Sibiu and Bucharest)](image)
After interpretation of data at this question it is noted that in Sibiu County multinational organizations organized and conducted 36% traditional training programs, which require physical presence at the course. 31% of respondents have placed 2nd, as type of training program, that applies most frequently in the organization where they work, the variant of answer e – a combination between traditional and online course (via Internet). Such a correlation is observed between traditional and modern methods of training.

Regarding respondents of multinational organizations from Bucharest, they placed first the alternative e – a mix of traditional and online course (via Internet) and on 2nd place variant a - a traditional training program, which involves physical presence at the course on its entire duration.

Although the order of respondents’ answers is distinguished on the two localities, placing the same type of programs on the first and second place shows that they gave the highest yield.

A last question, at which we present the results of our research is the following:

7. Which do you think that are the effects of human resource training on the organizations?
   a). increasing organizational performance
   b). increasing labor productivity level in relation to the existing one
   c). provides and develop cultural transfer of specialized knowledge and business practices within the organization
   d). increasing understanding that have the employees regarding organization function
   e). ensuring a good integration of human resources in the organization

The answers given by the respondents to this question leads us, clearly, to the last hypotheses validation, namely: if accomplishes the appropriate employee training, than is ensuring the performance of multinational organizations, whereas more than 50% of respondents (53% - respondents from Sibiu, 57% - respondents from Bucharest) chose the first alternative of response a - Increased the performance of the organization.

The issues arising from the analysis of the answers to these questions reveals that human resources training is considered as a very important activity of human resources management in multinational organizations with a major influence on obtaining and increasing their performance.

4. CONCLUSION

Today, in multinational organizations is putting increasingly more the accent on performance achievement, especially in terms of optimum use of available resources. In this direction, a decisive role has human resources, especially highly qualified human resources. Therefore,
increasing quality of human resources through a continuous training of them, and hence the performance of multinational organizations of which they are part of, is a very important activity.

From the presentation of the theoretical aspects, but also from the practical study conducted, it appeared that putting into relationship the influence of human resources training with multinational organization's performance has become a key concern of both theoreticians and practitioners in the field of management generally and also of the human resources management in particularly.

Also, it can be observed that in multinational organizations where the terrain investigation was conducted, appreciates the employee training as management policy priority to ensure their performance, along with other human resources management activity that is employees motivation.

Thus, it becomes necessary the knowledge and application of best practices, techniques and strategies in the field of training human resources able contribute to the achievement of organizations’ performance.

LITERATURE


THE EFFECTS OF COMMUNICATION TO CHANGE ON ORGANIZATIONAL COMMITMENT

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ABSTRACT
The aim of this research is to analyze the effects of communication to change on organizational commitment. The research population is employees’ working in different managerial levels and branches at the Bank X which is one of the leading banks in Sultanate of Oman. 74 percent is the response rate to the distributed questionnaire. The findings conclude that there is a positive effect of employees’ communication to change on employees’ organizational commitment. The research discusses some of the study implications and provides suggestion for future research.

Keywords: Communication to change, Organizational commitment, Three-component model of commitment.

1. INTRODUCTION
At the time of organizational change management must understand that is very important to develop a formal, coordinated, and organization-wide internal communication system to facilitate the implementation and practice of the new change (Kitchen and Daly, 2002). In addition, during a change process, it is also necessary to increase the internal communication frequency, since employees have a higher demand for information and continuous feedback. Similarly, Joffe and Glynn (2002) adds that communication to change includes spreading a vision, minimizing uncertainty, gaining employee commitment, involving employees by seeking their input into the content and process of the change, overcoming barriers to change, and challenging the status quo.

A number of scholars have found that commitment to the organization is critical when an organization engages in change initiatives, as committed employees will provide many benefits to the organization undergoing change (Meyer and Allen, 1997; Lok and Crawford, 1999; Herscovitch and Meyer, 2002; Vakola and Nikolaou, 2005; Cunningham, 2006; Chen and Wang, 2007; Herold, et al., 2007; Parish, et al., 2008; Mélanie, 2009; Visagie, 2010)

2. LITERATURE REVIEW
2.1. Organizational Commitment
Different concepts can be found in the organizational commitment literature review. According to Porter, et al. (1974) commitment could be classified into three factors as a strong belief and acceptance of the organization’s goals and values, a willingness to exert considerable effort on behalf of the organization, and a definite desire to keep organizational membership. Further research on these components has shown that any one of the three components is sufficient to produce the desired behavior (Meyer and Allen, 1997). In line of these definitions London and Howat (1979) defined employees’ commitment in terms of the identification with organizational goals, involvement with one’s work role, and a feeling of loyalty to and affection for the organization. Another commitment definition was given by Gallie and White (1993) who pointed out that employees’ commitment includes sense of loyalty and acceptance of organizational values and willingness to stay. Similarly Nijhof, et al. (1998) conceives commitment as a sense of loyalty to and identification with the organization, the work and the group to which one belongs.
Another set of organizational commitments concepts was given in the 2000s as the concept given by Ugboro and Obeng (2001) who states that organizational commitment describes the employee’s relationship with the organization and has an implication on the decision to continue or stop the employee’s membership in the organization. Walsh and Taylor (2002) assert that there are many definitions of organizational commitment, but researchers agree that organizational commitment reflects a multidimensional psychological attachment of an individual to the organization. Vakola and Nikolaou (2005) characterized employees commitment by at least three related factors; a strong acceptance of the organization’s values and goals, a willingness to exert considerable effort on behalf of the organization and a strong desire to maintain membership in the organization. As a result, commitment is determined by a range of organizational and individual factors such as personal characteristics, structural characteristics, work experience and role related features. Chen and Wang (2007) asserts that employees’ commitment to change could be understood as a psychological reactions on the basis of a three-component model distinguishing affective, continuance, and normative commitment to change.

The importance of commitment to change can be seen through some studies which considered employee’s commitment as one of the most important factors in a successful change implementation (Conner, 1992; Kotter, 1995; Coetsee, 1999; Armenakis, et al., 2000). Many reasons can be recognized for focusing on employees’ commitment due to the findings of previous scholars. Mowday, et al. (1979) found that committed employees are more likely to remain with the organization, exert extra effort on behalf of the organization, and put forth effort toward attaining organizational goals. Conner and Patterson (1982) noted that when employees are committed to organizational change, they are more likely to get involved in the change process, demonstrate enthusiasm for the change, and take responsibility for its successful implementation. In addition, commitment to change is essential to create and sustain a healthy work climate, to establish a supportive organizational change process, and to show positive actions to the new change (Daft, 2000). Furthermore, commitment leads to several attitudes and behaviors that are beneficial to the organization, like organizational citizenship behavior, and reduced absenteeism or turnover (Watson and Papamarcos, 2002). In addition, Newman and Sheik (2012) states that committed employees to new goals, policies, and procedures of change may stand a better chance of having successful implementation for these critical business activities.

Employees’ organizational commitment is tested by using an instrument developed by Meyer and Allen (1997) called the three-component model (affective, normative and continuance commitment) then updated by Herscovitch and Meyer (2002) to test commitment to change. Affective commitment measures the employee’s emotional attachment to, identification with, and involvement in the organization. Normative commitment reflects pressures on an employee to remain with an organization resulting from organizational socialization, while continuance commitment refers to commitment associated with the cost that employees perceive are related to leaving the organization. Meyer and Allen instrument was used by (Meyer and Allen, 1997; Lok and Crawford, 1999; Ugboro and Obeng, 2001; Walsh and Taylor, 2002; Lok and Crawford, 2004; Herold, et al., 2007; Azzem, 2010; Visagie, 2010; Visagie and Steyn, 2011; Wang and Hwang, 2012).

**2.2. Communication to Change**

Communication to change is defined by Dolphin (2005) as transactions between individuals and groups at various levels and in different areas of specialization and these transactions is intended to design and redesign organization and coordinate day to day activities proposes. While planning or responding to new change process management must understand that is
very important to develop a formal, coordinated, and organization-wide internal communication system to facilitate the implementation and practice of the new change by increasing the internal communication frequency, since employees have a higher demand for information and continuous feedback (Kitchen and Daly, 2002). What should be included in communication to change are spreading a vision, minimizing uncertainty, gaining employee commitment, involving employees by seeking their input into the content and process of the change, overcoming barriers to change, and challenging the status quo (Joffe and Glynn, 2002).

The importance of communication to change was and still discussed by many authors who assert that communication is a vital link in the total change management process. Kottler (1996) states that the reasons for change have to be clear to all the people involved in the change process, and they should be aware and satisfied with the change objectives for successful implementation to change. Lewis (2006) found that communication to change is different from information exchange by considering communication to change as a dialogic process between the change management and the employee by not just explaining the reasons for change but also by encouraging the employees to be involved in the change decision making to enhance the opportunity of successful change process.

Emanuele, et al (2012) investigated communication to change from a strategic perspective through its main components (aligning, energizing, visioning, and constituting) at Ferrari Corporation. The investigation shows that the four strategic communications, if applied in an integrated manner, that will lead to successful and effective communication to change and this can be an essential lever that supports continuous improvement and helps drive organizational success. The implication of the research is seen that the research contributes to the change management literature in generally and to communication to change in specific by linking strategic communication, continuous improvement and entrepreneurial theory. On the other hand, additional research is needed to generalize the effectiveness of the proposed strategic communication model.

What role should the management play in communication to change? Allen, et al. (2007) examined the role of management in moderating the relationship between quality of communication and uncertainty. Questionnaires were distributed for employees in a government department that was undergoing change. Results indicated that employees who perceived they received quality change communication are more open to change.

In the same context, Hasmana and Elving (2008) investigated the role of management in communication to change in nonprofit organization. The findings of the study showed that the success of organizational change largely depends on the informative and communicative skills of managers at all levels. In addition, Mutihac (2010) explored and explained how internal communication to change can be effectively used within an organization undergoing change in Romanian Petroleum Company as field of the study. The conclusion of the study showed that to achieve effective internal communication to change, it is essential to know what kind of information needs to be communicated, to whom the information is relevant and what method is the most appropriate to communicate the information. Furthermore, it is important for management to think about what employees must know and should know.

To explore the correlation between communication to change and employees’ behaviors at work Nelissen and van Selm (2008) found that the most significant correlations were between employee satisfaction and communication to change. It was determined that there is a positive correlation between these two variables due to employees who are satisfied with communication to change saw more personal opportunities and had a positive state of mind on the organizational change. Similarly, Tandon and Tyagi (2012) found that unclear
communication to change or non-communication can cause dissatisfaction among the employees and interrupt the effectiveness of any organization. To test communication to change Gravenhorst, et al. (2005) developed an instrument named Communication and Organizational Change Questionnaire (COCQ). The instrument consists of 10 items to test the following scales (Necessity of the change, Goals and direction of the change, Information about the change, Communication about the change, Room for diversity, Role of top managers, Role of line managers, Uncertainty, Support for the change, and Contribution to the change). The developed instrument was used by (Frahm and Brown, 2007; Nelissen and van Selm, 2008; Mutihac, 2010; Chaoying and Yunxia, 2012).

2.3. The Relationship between Communication to Change and Organizational Commitment
Van Ruiten (2007) hypothesized that employees’ organizational commitment in times of change is positively related to effective communication to change. Multiple regression analysis from a sample of 2,291 employees working in 8 different organizations active in a variety of sectors in the UK and undergoing large scale organizational change supported the study hypotheses and indicated that there is a symbolic positive effect between employee’s commitment to change and effective communication to change. Another study was done by Smart (2010) who investigated whether the implementation of a clear change management plan could assist employees in remaining committed to their organizations. Semi-structured interviews, confidential questionnaire, and revision of organizational documentation were the three data collection methods within five South African organizations. Findings of the study showed that communications were most successful when they contained information relevant to and helpful for the specific audience being communicated with. In addition to, communication could be emphasized as the foundational blocks for expanding employees’ organizational commitment. The findings of (Van Ruiten, 2007; Smart; 2010) confirmed that there is a positive relationship between the two variables but the studies showed limited evidence of recommending appropriate strategies to enhance the level of communication to change which will affect positively enhancing the level of organizational commitment among employees’.

3. RESEARCH METHODS
3.1. Research Objectives
The general objective of this research is to contribute to the general body of knowledge and research work in the area of employee’s organizational behavior to support organizational changes. To achieve the general objective, the research specific objectives would be as follows in two objectives:

1. To examine relationship between employees’ communication to change and organizational commitment.
2. To analyze if employee’s communication to change affect employee’s level of organizational commitment.

3.2. Research Hypotheses
From the general and specific objective of the research the main hypothesis would be:

1. There is a positive relationship between employees’ communication to change and organizational commitment.
2. There is a positive significant effect of employee’s communication to change on employees’ organizational commitment.
3.3. Data Collection Method
Data collection for this study was performed by using self-administrated questionnaire. The questionnaire consisted of three parts. The first part consist general information for the study participants. The second part consists of statements relating to organizational commitment. The third part consists of statements related to communication to change. The Questionnaire used a 5 point Likert scale ranging from 1 strongly disagrees to 5 strongly agree.
Employees’ organizational commitment is tested by using an instrument developed by Meyer and Allen (1997) called the three-component model. There are 15 items measuring affective, normative and continuance commitment. 5 items measure affective commitment, 5 items measure normative commitment, and 5 items measure continuance commitment. The internal consistency in the original scale for affective commitment is 0.75, normative commitment is 0.80, and continuance commitment is 0.81.
To assess communication to change in this study 10 items divided into 4 scales are taken from Communication and Organizational Change Questionnaire (COCQ) developed by Gravenhorst, et al. (2005). The internal validity of the selected items are 0.81 for Necessity of the change, 0.82 Goals and direction of the change, 0.76 for Information about the change, and 0.77 for Communication about the change.

3.4. Respondents Demographic Profiles
Employees from different branches from the Bank X were selected to participate in the research. A total of 364 employees were employed in this bank at the time of the research, and all were invited to participate in the survey. The questionnaire was made available to respondents with a help from Human Resources Department within the Bank X. At the top of the questionnaire an explanation to the purpose of the research was written to the participants with guaranteed confidentiality of participation and responses.
The survey questionnaire was completed by 271 respondents, representing a response rate of 74.4 per cent. The conduct of this study involves a detailed account of the demographic profile of the respondents. Thus, the profile of respondents is looked upon in terms of gender, age, academic qualification, and years of experience in Bank X. The distribution of respondents in terms of their gender is seen in which shows that 67.5% of the participants were male and 32.5% were females. In terms of respondents age fourteen (30%) of the respondents were 20-30 years old. Fifty five (57.4%) of respondents were between 31-40 years old, showing that most of them were already considered as matured employees. Twenty two (5.5%) of the respondents were between 41-49 years old. Only nine (7%) of the respondents were between 50 years and above. The respondents were asked for their academic qualifications and the report shows 12% of them are high school graduate, 12.5% are diploma holders, 37.3% are bachelor holders, and 31.4% are master and 6.6% are others. The distribution of the respondents in terms of their years of experience in Bank X. Herein, it shows that 0% of the respondents have less than one year of experience, 17% have between 1-3 years of experience, 13% have between 3-5 years of experience, and 70% have over than 5 years of experience.

3.5. Descriptive Statistics for the Research Variables
Descriptive statistics analysis is applied in this study to illustrate the mean, standard deviation, minimum and maximum values for each of the variables included in this study are depicted in (Table 3.1).
Table 3.1 Descriptive Statistics for the Research Variables

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Standard Deviation</th>
<th>Minimum Value</th>
<th>Maximum Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Organizational Commitment</td>
<td>3.409</td>
<td>.5440</td>
<td>2.53</td>
<td>4.73</td>
</tr>
<tr>
<td>Communication to Change</td>
<td>3.590</td>
<td>.6429</td>
<td>2.13</td>
<td>4.88</td>
</tr>
</tbody>
</table>

As shown in Table 4.1 mean for organizational commitment is 3.40 and for communication to change is 3.59. The standard deviation for organizational commitment is .544 and for communication to change is .64. As shown in Table 3.1, organizational commitment had a mean value of 3.40 with a standard deviation of .54, communication to change have a mean value of 3.59 with a standard deviation of .64. Thus, since the standard deviation is less than 1, this indicates that 68% of research respondents lay within 1 standard deviation of the mean which shows little variance among the participants responses.

3.6. Testing the Hypotheses
To examine the relationship between employees’ communication to change and employees’ organizational commitment person correlation analysis is used to test the first research hypothesis. The person correlation matrix for the two interval-scaled variables is shown in Table 3.2. As can be seen the three types of organizational commitment (Affective, Continuance, Normative) are found to have a high negative significant correlation with communication to change at P<0.01 level (r=.662). In addition, results of the correlation indicate that the strongest effect is for continuance commitment -.243. This proves that when employees have effective communication to change they will negatively respond to the higher cost of leaving their organization. This means that fulfilling effective communication to change would cause the respondents to feel attached to the organization.

Table 3.2: Pearson correlation between Commitment to Change and Communication to Change

<table>
<thead>
<tr>
<th>Commitment to Change sub Variable</th>
<th>Communication to Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Affective commitment</td>
<td>Pearson Correlation</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
</tr>
<tr>
<td></td>
<td>-.381(**)</td>
</tr>
<tr>
<td></td>
<td>.000</td>
</tr>
<tr>
<td>Continuance commitment</td>
<td>Pearson Correlation</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
</tr>
<tr>
<td></td>
<td>-.243(**)</td>
</tr>
<tr>
<td></td>
<td>.000</td>
</tr>
<tr>
<td>Normative commitment</td>
<td>Pearson Correlation</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
</tr>
<tr>
<td></td>
<td>-.332(**)</td>
</tr>
<tr>
<td></td>
<td>.000</td>
</tr>
</tbody>
</table>

** Correlation is significant at the 0.01 level (2-tailed).

In order to examine the effect of employees’ communication to change on employees’ commitment to change which is research hypothesis 2 a multi regression analysis is applied as a testing method to examine this hypothesis. Thus, it is required to know how much of the variation in the value of the employees’ organizational commitment. As shown in Table 3.3 the value of R square is 0.159 which indicates that 15 percent of variation in employees’ organizational commitment can be explained in employees’ communication to change.

Table 3.3 Relationship between employees’ communication to change and organizational commitment (Model Summary)

<table>
<thead>
<tr>
<th>Model Summary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Model</td>
</tr>
<tr>
<td>R</td>
</tr>
<tr>
<td>1</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Communication to Change
b. Dependent Variable: Organizational Commitment
To determine the linear relationship between employees’ communication to change and employees’ organizational commitment Analysis of Variance (ANOVA) is generated in Table 3.4. The result shows that the F value is equal to 50.786 in the ANOVA which shows the reliability of communication to change to predict the organizational commitment. Thus, hypothesis 2 is substantiated because there is a significant employees’ communication to change effect on organizational commitment due to this treatment.

Table 3.4 ANOVA Analysis

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>13,644.854</td>
<td>1</td>
<td>13,644.854</td>
<td>50.786</td>
<td>0.000</td>
</tr>
<tr>
<td>Residuals</td>
<td>72,272.726</td>
<td>269</td>
<td>268.672</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>85,917.579</td>
<td>270</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Communication to Change

b. Dependent Variable: Organizational Commitment

To address the strength of communication to change effect on organizational commitment a coefficient analysis is shown in Table 3.5. The results indicate that the Beta value for communication to change is -0.399 which shows negative correlation between communication to change and organizational commitment. This concludes that positive communication to change will result in negative willingness to leave the organization in other words organizational commitment.

Table 3.5 effects of communication to change on commitment to change coefficient analysis

<table>
<thead>
<tr>
<th>Model</th>
<th>Un-standardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>T</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>104.210</td>
<td>5.496</td>
<td>18.962</td>
<td>0.000</td>
</tr>
<tr>
<td>Communication to change</td>
<td>-1.281</td>
<td>0.180</td>
<td>-7.126</td>
<td>0.000</td>
</tr>
</tbody>
</table>

Dependent Variable: Organizational Commitment

4. CONCLUSION AND FUTURE RESEARCH DIRECTION

The purpose of this research was to analyze the effects of communication to change on organizational commitment. The analysis of the results proved that employees’ communication to change significantly affects organizational commitment. This finding is critical because it sheds light on the importance of communication to organizational change and its effects to build and enhance organizational commitment.

This research followed the cross sectional design so it is suggested for future studies to follow a longitudinal study in order to assess more deeply the changes in communications to organizational change. In addition, a comparison can be made among employees working in different departments of an organization to find out if communication to organizational change work is affected by the nature of work carried out organizational identity. Finally that topic may be studied on a larger scale to make comparisons between the effects of communications to organizational change on organizational commitment in different countries. This will provide an understanding on cultural influences on organizational commitment.
LITERATURE


CRM AS A TOOL FOR INCREASED COMPETITIVE ADVANTAGE IN TERTIARY EDUCATION

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ABSTRACT
Each educational institution has to be aware that it cannot exist without their basic “customers” - students. This is especially true for tertiary education, i.e. universities, because students have a wide variety of choices and are mostly not geographically limited in their choice of studies, therefore the competition between institutions is increasingly relevant. Studies show that the use of Customer Relationship Management [CRM] is widespread in larger and progressive universities in areas of higher competition, e.g. in the USA. In the areas where competition between universities is just beginning to be a major factor, CRM use for student management is a relatively new concept. The paper aims to present some starting points and considerations when implementing CRM in tertiary education. On the base of a literature review, a survey was made among students of a Slovenian mid-sized faculty that currently does not have any advanced CRM support. The results of this survey, which were analysed using basic statistical analysis, point to a variety of factors and services that influence student satisfaction and positive attitude towards the university, while on the other side giving the university crucial information about each student and their life cycle at the university through consolidated and centralised information in the CRM environment. The paper’s added value is to analyse how universities can apply CRM use to increase their competitive advantage in comparison to other universities and provide students (as well as potential students and alumni) with superior services.

Keywords: customer relationship management, tertiary education, student satisfaction, competitive advantage

1. INTRODUCTION
Globalisation and the internet have led to a competitive situation in the education sector, particularly in tertiary education. Universities and colleges are thus increasingly competing with each other in so that they are fighting for the best students (Seeman, O’Hara, 2006). Consequently, these institutions will often endeavour to obtain some sort of advantage in comparison to others, different kinds of certifications and accreditations. They are most dedicated to the strategies, techniques or methods to improve their “brand” (Ariffin, 2013). Since tertiary education institutions are faced with increasing competition, they are also changing their concept of treating their students, graduates, teaching, administrative and technical staff. Competing demands go in the direction that it is also necessary for these institutions to regard these groups of people as customers and therefore the institutions must make an effort in deciding how they will attract, retain and care for them. To this end, a growing number of tertiary education institutions uses the concept of technology and CRM (Customer Relationship Management), with expected benefits of an increase of student-centric focus, improved customer data and process management, increased student loyalty, retention and satisfaction with the college’s programs and services (Seeman, O’Hara, 2006).
In higher education, CRM is substantially less commonly implemented than in for-profit organizations. Most institutions are however already finding it necessary to be flexible in adopting to different desires and needs of the students. Therefore, organizations in the field of tertiary education might consider implementing CRM strategies that would enable them to improve processes in conjunction with the students, the personalization of communication with students, sharing information about students between different departments and ultimately enable a higher degree of conservation of students and their satisfaction. If CRM is to be applied to the case of tertiary education institutions, it is necessary to know the life cycle of a student who progresses from a potential student to a future student who is in the process of gathering information, then to a student who has already applied to study, then enrolled students and ends with graduation, when the student becomes an alumni. In establishing CRM, objectives of CRM and organizational factors (i.e., the specificities of the institution) must also be taken into account. It should be clearly defined when the individual organizational units should be involved in each stage of the life cycle of the student (Nair, Chan, Fang, 2007). Lately, the challenge for educational institutions has not been in acquiring students, but more and more in keeping them. Traditionally, activities that would retain students focus on different orientation programs, counselling for students and various activities aimed at students (Kumar, 2008). However, Grant and Anderson (2002) propose that students nowadays expect technology to be embedded as a part of their entire educational process. This is supposed to provide greater access to information, and from the perspective of a student as a customer, the educational CRM system should take care of the interaction between students and student support departments as well as among students and other important points of assistance. Thus, one system should contain all of the services needed by the student. Students as customers of educational institutions are their most important stakeholders. CRM system should be implemented in order to facilitate and ease all administrative errands, since the possibility of anytime, anywhere registration gives options to make a payment, counselling, and individualized verification of obligations would meet all students' needs (Kumar, 2008). Nowadays, students require and demand a higher level of access to information about their chances of success and the future. Students also require that technological aids are an integral part of their learning experience (Grant, Anderson, 2002). In institutions where some form of e-learning is implemented as part of their study process, technological aspects are even more important – here, CRM can be successfully implemented alongside existing IT services, as shown by Daradoumis et al. (2010). Nelson, Quinn, Marrington and Clarke (2011) state that it is necessary to continuously measure and monitor the success of students and the number of active students, most notably first-year students, especially in institutions where there are signs of a large percentage of inactive or prematurely unenrolled students, which requires urgent action. Tertiary education institutions which tend to good relations with students, should carry out such measurements continuously, since it is the level of quality of relationships that is most reflected in the satisfaction of users. Research of the USA’s Ivy League Universities showed that the quality of relationships is strongly associated with the quality of service, trust and satisfaction of students and graduates (Lechtchinskaia, Friedrich, Breitner, 2012). Expanding the network of partners from outside the academic sphere, namely companies and other organizations, is crucial in terms of increasing the possibilities of practical training of students and faculty and increasing employment opportunities after graduation. Partnerships are important also as a way of establishing learning approaches that emphasize practical training. Promoting practical learning and offering jobs for the training of students is
becoming one of the more stable and strategic requirements for universities. In order to achieve the desired results, a good relationship with business partners is much needed and useful (Ylikoski, Kortelainen 2012). This can also be one of the areas where CRM can be a useful facilitator. Lawson, Willoughby, Mukankusi and Logossah (2011) indicate the range of factors that must be taken into account in the implementation of CRM solutions in tertiary education. Factors are divided into the following four categories:

- contextual factors: competitive pressures, environmental pressures, customer relations, mutual influence,
- organizational factors from a technical point of view: IT infrastructure, IT training, IT maintenance plan, the complexity of IT applications,
- organizational factors from a social point of view: management support, human resources management, the size of organization, change management within the organization, knowledge management,
- individual factors: user acceptance, personal innovativeness, aversion of users, computer literacy, previous experience of the user, the scope of knowledge of users depending on the requirements of IT.

According to above starting points, the importance of implementing CRM systems in tertiary education can be indicated. Even though CRM systems can be used in tertiary education institutions to support customer relations with different groups of stakeholders, such as students, employees, companies and other organizations, the research here will focus solely on students. Therefore, our research will take into account the literature review findings to further explore the CRM implementation potential and effectiveness of the system on a case of a Slovenian faculty, a member of the University of Maribor. Some beginnings of CRM are already implemented, but fragmented among different departments and services, therefore a common and integrated system is lacking. With the help of a survey among different publics, which represent different student life cycles, the study will aim to pinpoint most important aspects of CRM services from the view point of “customers” of tertiary education institutions – students.

3. METHODOLOGY
Currently, the observed faculty has study programmes on all three Bologna levels of tertiary higher education with approximately 800 enrolled students and also has over 1.000 alumni. The faculty has approximately 45 teaching and 22 administrative and supporting employees. This makes it one of the smaller faculties of the University of Maribor, which has approximately 18.000 students and 1.700 employees altogether. No existing integrated CRM system is currently in place neither university-wide not at the faculty itself. Current systems which could be seen as predecessors of CRM are not interconnected and access to them is limited even among teaching and administrative staff who would need the contained information on an everyday basis. These include:

- centralized system for tracking of grades, enrolment and exam participation for each student,
- a database of current students with contact information,
- blended learning platform,
- personal folder of all employees.
Since research and practical implications show that such a system is widely used and beneficial in the level of service, attitudes of students and student retention, a research was made into the attitudes of students towards CRM systems and their desirable elements. This was achieved with a survey among three major groups on the student side: high school enrollees as potential university students, existing students and alumni. Each survey focused on specific aspects of CRM implementation for support of relations with this target group. Due to this focus, the surveys researched respondents’ attitudes toward specific elements that were assessed as beneficial based on the literature review and not on their attitude towards CRM as a whole, since the final “customers” are generally not interested in the system which enables them the accessibility to information and services, but rather on the services and information themselves.

It has to be pointed out that the surveys were intentionally very focused on main issues and were consequently very short, in order to ensure the minimal possible drop-out rate. The surveys were web-based and differed according to target groups. Due to the mode of attaining respondent, which combined sharing the survey on social networks, e-mailing and direct contacts with representatives of target groups, it is not possible to assess the response rate. The dropout rate (respondents who began the survey but did not complete it) was 2%.

For high school students, the survey focused on their interest for cooperation with the faculty prior to their application. The number of responses from this group was a total of 52 full responses. For students, the survey focused on their satisfaction with the current systems and their desires and ideas for CRM implementation and elements at the faculty, and this survey was most comprehensive since this is the primary research focus. The number of responses from this group was 232. The survey for alumni focused on their expectations for information from the faculty and their readiness for further cooperation. The number of responses for this group was 61. Overall, the survey therefore had 345 responses.

3. RESULTS
The survey results are presented below according to responses from different target groups – high schoolers, students and alumni.

3.1. High school students
The first question asked the high schoolers whether they would like to cooperate with the faculty at a time when they are involved in education at their high school. 60% responded positively and 30% were undecided, while only 10% were disinterested. The results are quite encouraging from the perspective of the faculty, as the majority of students who were interviewed want to cooperate even before they are enrolled in college. The second and third questions referred mainly to the exchange of information between students and faculty. According to the results students are mostly interested in seeing some of the lectures before they decide to enrol to the selected college. They would also like to be able to use an application that would inform them on current enrolment deadlines and provide them with a “virtual tour” of the Faculty.

The final question inquired whether they would be prepared to give their personal information to the faculty, which is a prerequisite for CRM implementation. The majority, 86%, are willing to do so. Overall, it can be assessed that high schoolers present an important target group of tertiary educational institutions and their CRM implementation, and survey results show that their inclusion into CRM efforts is supported even from their side.
3.2. Faculty students
Firstly, it was found that 81% of students are interested in the creation of applications that make it possible to carry out all administrative matters concerning the faculty in one place. Currently, as many as 72% of students feel overloaded with a flood of notifications and emails about certain workshops, timetables, consultation hours of professors, etc., this is due to the currently decentralized system where each department sends notifications to students independently. With CRM implementation, students could filter specific functions and be registered only for information in the fields of certain topics that interest them.
When asked about satisfaction with the current notification system for events, important dates and other information relating to the respondents, students could mark their answer on a 5-point scale, where 1 meant "Not at all satisfied" and 5 "I am very satisfied". On average, current students rated their satisfaction with an average of 2.94, which means that the notification system from the students’ point of view is not satisfactory in its current configuration.
As the most suitable way of establishing contacts with faculty, respondents defined e-mail as their preferred method, followed by SMS-messages to their mobile phone and through the faculty website. Furthermore, personal contacts with representatives of the faculty, phone calls and personal “snail” mail were deemed less appropriate. Social networks and printed media such as newspapers, were assessed as least preferred with the exception of the age group between 18 and 20 years of age, who assessed social media as one of the preferred channels of communication. This points to the fact that social networks are very popular among teenagers and will probably have to be used in the future and consequently integrated into CRM systems.
When asked to what extent they are willing to offer their personal data for the purposes of additional services from the faculty and consequently personalization of information on a 5-point scale, where 1 meant "I'm not ready" and score 5 "I am very willing", students responded with an average of 3.64, which means that, for this purpose, they are ready to offer a relatively large amount of personal data.

3.3. Alumni
Most, namely 68% of graduates, would like to actively participate in future meetings of graduates and 26% are undecided. 84% of respondents are very interested in participation in a portal that brings together all graduates of their Alma Mater university or faculty.
When asked to what extent they are willing to offer their personal data for the purposes of communication with the faculty on a 5-point scale, where 1 meant "I'm not ready" and score 5 "I am very willing", the average score of responses is 3.38. Even though this is a lower score than with current students, it points to a relatively high willingness and is a good prerequisite for successful CRM implementation.
On the question of the usefulness and importance of services and content alumni would like to receive in any form from the faculty, the respondents were offered services and contents and assessed their importance on a 5-point scale, where 1 meant "not at all useful / important" and 5 meant "it is very useful / important". Very important / useful (score 5) content / services to alumni are warnings about important dates (registration, enrolment, etc.) with 86.2% of respondents recognizing this as crucial. In second place (69% of respondents) are contents regarding job opportunities. Among the more important or very important (estimated at 4 or 5 on the scale), 72.4% of respondents also considered invitations to various events from their business or study fields, and 43.7% would be interested in receiving links to content that is relevant to their activities or interests. On the contrary, 75% of respondents deem congratulations on personal holidays as not useful / important (assessment 1 or 2).
As for the mode of establishing contacts, former students prefer personal mail, followed by phone calls and notifications through e-mail or the faculty website. Social networks and similar modern communication channels are in last place.

4. CONCLUSION
The introduction of a CRM system in any organization, including tertiary education institutions, must ensure anytime, anywhere accessibility. It may not be temporally and spatially limited. The introduction of CRM support in the educational system would offer many advantages to both sides – faculty and students. From the viewpoint of the faculty, integrated information and databases of students, as well as prospective students and alumni, would mean an increase of their level of service and consequently of their competitive advantage on the ever-growing field of tertiary education. Additionally, an integrated system would enable the faculty more in-depth analysis of their stakeholders to further improve their “business” operations. To students, the availability of information, indirect and direct communication with the employees at the university, prompt notifications and improved services would mean an improved study experience and easier performing and tracking their obligations.

The research, presented in this paper, was based on a survey among crucial stakeholders of a tertiary education institution – prospective students, current students and alumni. The main and most important outcomes are in the revelation of preferences of these groups in regard to their demands of CRM systems services from their point of view. Since the survey was performed on an average faculty in regards to size, study programmes and current state of pre-CRM implementation, it can be assessed that the research results are representative and can easily be applied to the case of many other tertiary education institutions worldwide.

Topics and areas of Higher Education Marketing (as defined by Hemsley-Brown & Oplatka, 2006), present potential for furthering the research given in this paper. These are mainly advertising, public relations, personal selling, direct mail, sales promotion, promotion by word of mouth and diffusion of innovation, applied to the tertiary education field.

LITERATURE


ANALYSIS OF COMPANIES OF THE CONSTRUCTION SECTOR IN POLAND BASED ON AN EXAMPLE OF THE QUOTED COMPANIES AND THEIR FAIR VALUE

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ABSTRACT

According to forecasts of research companies, the year of 2014 will end in one-digit increase for the construction industry, and in 2015, another 8-10% will be recorded. This optimism follows from the fact that the largest construction companies, which are relatively well-off even during the recession, were qualified for the study. The construction boom has already established itself in Poland and in the world from two years, which currently results in the increase of the property prices, and the spectre of decrease in the property prices is fading into oblivion. However, it has to be borne in mind what was learnt at the turn of 2007 and 2008, where the property prices rapidly decreased, and interest rates of credit soared upwards, which resulted in collapse of the property market and large bankruptcies.

The construction boom examined and calculated by the Central Statistical Office (CSO) is not as optimistic as the ratios for the construction provided by large construction companies. The construction companies of all sizes take part in the CSO study, and the medium, small and micro companies assess the situation unfavourably. According to CSO, the construction boom was 11 minus in October 2014, and it was lower than that recorded in September, by 4 points. The construction companies quoted on the Warsaw Stock Exchange on the WIG-BUDOWNICTWO index were subjected to the study. During the study it was demonstrated how the construction companies deal on the property market and what financial results they achieve. They were subjected to a thorough economic analysis, and their value over the years was determined. At the same time, it was examined whether companies of the construction sector have the fair value or if they covered the losses from the time of the first global economic crisis and the collapse occurred at the time on the property market, in which pieces of properties can be bought even 50% cheaper.

Key words: construction sector, financial condition, profitability, fair value.

1. INTRODUCTION

After two hard years 2012 and 2013 in the construction market, finally there came the revival, of which the increase in sales and consumption of cement is the best witness. In 2012-2013, the major decrease in production of cement (-16% and -7.5% respectively) was recorded, which was reflected in the decreasing volume of sales of building and construction output. Currently, the production volume of the primary ingredient for the construction has recorded increases by approx. 53% year-on-year, and more than 100% in case of consumption since the beginning of 2014. For the entire year, however, the indices were much more moderate, but they remained to do in green numbers.

2. THE CONSTRUCTION MARKET IN POLAND

From January to October 2014, building permits were issued for the construction of 133,622 flats. This is 14.2% more than in the same period of 2013. The number of flats, whose construction has been started, also increased by about 15.6%. On the other hand, there was
2% less flats put into service compared to the same period of 2013, and 5% less compared to 2012.
Real estate developers and individual customers are the main cause of the increase in the number of flats, whose construction has begun.
In case of developers, from January to October of 2014, building permits for 64,801 flats were obtained, which is 38.8% more than in 2013, when the decrease by 23% was recorded. There has also been the increase in the number of flats, whose construction was begun by developers - up to 58,485 flats that is by 34.8% compared to 2013, when there was the decrease by 13.2%.
The situation of flats put into service by developers to use also improved. The number of such flats was by 45,888 higher that is by 3.6% more than in the first ten months of 2013. Development flats constitute 40.2% of the total number of flats put into service in the analysed period.
**Individual investors** put into service 7% less flats than in the last year - 61,947 - this is 54.2% of all flats put into service. The number of flats, whose construction has been begun by the individual investors, also increased - 67,286 that is 3% more than in the same period of the last year. On the other hand, the decrease in building permits by 0.8% was recorded. The number of flats, for which individual investors obtained building permits, was 65,688.
Producers of building materials felt these increases, and their assessments of the current year are not pessimistic any more. However, the situation of the industry is still far from being optimistic. Market experts and construction companies themselves are still waiting for the state program that will stimulate residential construction.

![Figure 1. WIG-BUDOWNICTWO in the period from 01.2005 to 01.2015(data of the stooq.pl).](http://stooq.pl)

UDIMEX and ELBUDOWA are one of the largest construction companies in Poland. They are quoted on the Warsaw Stock Exchange, where they are evaluated in terms of the market activity and the potential rate of return on funds invested by investors (Zaremba, 2014, pp. 89-91).
The WIG-BUDOWNICTWO index shown in the Figure 1 presents that, since 2012, the construction sector's companies in Poland has shown stagnation and the side trend in their values. Therefore, it could be said that their value does not reflect the market and fair values.
Analysing the WIG-BUDOWNICTWO price/earnings chart, it should be noted that it is even 83.20% of the lost value 47.60, which was recorded in 2010. Currently, this value is 8.01 in January 2015.
However, with such a variable market and reported good moods of investors, it will be able to return to the recorded maximum, as well as the fair value of the companies of the construction sector (Fisher, 2014, pp. 45-51; Katsenelson, 2013, pp. 89-94).

3. CONSTRUCTION SECTOR’S COMPANIES QUOTED ON THE WIG-BUDOWNICTWO INDEX IN POLAND.

Companies quoted on the WIG-BUDOWNICTWO index are characterized by the good financial condition (gpw.pl, 2014, data of the Warsaw Stock Exchange):

a) BIPROMET - Bipromet SA Capital Group operates in the broadly understood construction sector. The main areas of activity are: design services, general execution of investments, completion of deliveries, printing services, surveying services, rental and lease of office workplaces,

b) BUDIMEX - one of the largest construction companies in the Polish market. The general contractor in the field of road engineering, non-specialised construction, and green building.

c) CNT - Centrum Nowoczesnych Technologii SA [Centre of Modern Technologies] focuses its current activities mainly in the areas of infrastructure procurements for the local government's units within public tenders.

d) ELBUDOWA - The company is a leading contractor and supplier of medium- and low-voltage switchgears, as well as substations and power systems.

e) ELEKTROTII – ELEKTROTIM SA constructs medium- and low-voltage utility grids, low and high current systems. It integrates process and power-system automation systems, manufactures electrical medium- and low-voltage switchgears, provides maintenance services in the field of current systems and traffic engineering.

f) ELKOP - it operates in two sectors – real estate development and real estate sectors. ELKOP SA is engaged in purchase and rental of office workspace, production and retail spaces, and possesses commercial real estate and the development project in Katowice.

g) ENAP - Energoaparatura is a company with the well-proven track record on the market of specialised civil works and assembly services. It provides surveying, automation and control services, electrical and telecommunication works and the installation of the
Intelligent Building in all industrial sectors, municipal services, and environmental protection.

h) ERBUD - is a general construction group providing services in the industrial, public utility, engineering and road, and residential segments in Poland and other European countries, such as Germany, Belgium, France, and the UK.

i) HERCULES - it is a company, which previously appeared under the name of GASTEL ŻURAWIE SA. The company is engaged in hardware support of investments and construction logistics.

j) INSTALKRK - The basic operating segments of the Capital Group are the civil works and assembly services in the field of industrial plants and construction installations, manufacture of components of steel installations and structures, as well as design, production, and assembly of ventilation and air conditioning installations.

k) MIRBUD - the company operates, above all, as a general contractor or the investment general contractor in commercial-service, residential, industrial and engineering and road building on the construction market in Poland.

l) MOSTALPLC - Mostostal Płock specialises in the civil works and assembly works for petrochemical and chemical industries.

m) MOSTALWAR – Mostostal Warszawa is currently the one of the largest construction companies in Poland. It operates in the segment of non-specialised, industrial, and engineering construction, environment protection, as well as the road infrastructure, mainly on the domestic market.

n) MOSTALZAB – Mostostal Zabrze's activities include the complex buildings' execution and subcontracting of specialist works for industry and power sectors, environmental protection and public utility facilities, as well as bridges.

o) MSXRESOUR – MSX Resources SA is a construction and real estate development company present on the Polish market for over half of a century.

p) PANOMA – P.A. Nova SA is a company offering services in the execution of construction investments in the whole country.

q) PROCHEM – it is an engineering company providing services in the field of programming, design and supervision of the execution of construction and modernisation investments.

r) PROJPRZEM – Its basic activity is the non-specialised construction and civil engineering, which includes the execution of civil works and assembly works, deliveries of steel structures of buildings and civil structures, as well as manufacture of items of plant of the steel or aluminium structure.

s) RESBUD – Resbud S.A. is one of the largest construction companies in south-eastern Poland. The subject of the company's activity is the non-specialised construction, civil engineering, and manufacture of concrete mass.

t) TEGAS – the primary business of the parent company and its subsidiaries are: works related to the construction of transmission pipelines and distribution systems, services supporting the utilisation of oil and natural gas deposits, machining of metal elements, manufacture of electrical systems.

u) TRAKCJA – Trakcja SA is one of the largest companies operating in the sector of infrastructural construction and power engineering in Poland.

v) ULMA – activities of the company are focused on service of the executive construction companies. ULMA provides complex services of lease and sale of shuttering and scaffolds for execution of land construction works.

w) UNIBEP – Unibep is a construction group with the well-proven track record on the market of the residential construction of the Warsaw agglomeration. In recent years, it has built more than 50 multifamily housing estates in Warsaw.
x) ZUE –The ZUE Group, which includes ZUE S.A. and PRK S.A., is one of the leading entities operating on the construction market of urban and railway communication infrastructure.

4. ANALYSIS AND VALUATION OF THE CONSTRUCTION SECTOR COMPANIES QUOTED ON THE WARSAW STOCK EXCHANGE (WSE) IN POLAND.

In the construction sector, we can see one company, which reported its maximum on 7 January 2015, and that is BUDIMEX. While the other companies did not show its maximum value, and even fair value, though they can show the net profit and the good financial condition. Some companies were overvalued by over 80%-100%. These companies are ELKOP, HERCULES, MOSTALZAB, MSXRESOUR, PROJPRZEM, RESBUD, TESGAS, and ULMA. Only UNIBEP is trying to remain to be a flagship company, and recover its value of the previous years (Table 1).

Table 1: The construction sector’s companies quoted on the Warsaw Stock Exchange in Poland as of 7.01.2015 (own development based on the data of the Warsaw Stock Exchange, data of the Bankier.pl)

<table>
<thead>
<tr>
<th>Name</th>
<th>Average rating</th>
<th>Rating</th>
<th>Current price PLN</th>
<th>Maximum price PLN from the beginning of the stock exchange quotation</th>
</tr>
</thead>
<tbody>
<tr>
<td>BIPROMET</td>
<td>4.0/5.0</td>
<td>A-</td>
<td>3.81</td>
<td>20.46</td>
</tr>
<tr>
<td>BUDIMEX</td>
<td>4.0/5.0</td>
<td>B+</td>
<td>139.00</td>
<td>141.50</td>
</tr>
<tr>
<td>CNT</td>
<td>4.0/5.0</td>
<td>AAA</td>
<td>8.00</td>
<td>33.98</td>
</tr>
<tr>
<td>ELBUDOWA</td>
<td>4.5/5.0</td>
<td>BBB-</td>
<td>76.41</td>
<td>219.80</td>
</tr>
<tr>
<td>ELEKTROTI</td>
<td>4.0/5.0</td>
<td>AAA</td>
<td>10.15</td>
<td>31.88</td>
</tr>
<tr>
<td>ELKOP</td>
<td>3.0/5.0</td>
<td>AAA</td>
<td>1.50</td>
<td>28.84</td>
</tr>
<tr>
<td>ENAP</td>
<td>3.0/5.0</td>
<td>AAA</td>
<td>0.99</td>
<td>2.86</td>
</tr>
<tr>
<td>ERBUD</td>
<td>4.0/5.0</td>
<td>BBB</td>
<td>25.80</td>
<td>95.34</td>
</tr>
<tr>
<td>HERKULES</td>
<td>3.5/5.0</td>
<td>BBB-</td>
<td>2.80</td>
<td>26.82</td>
</tr>
<tr>
<td>INSTALKRK</td>
<td>4.5/5.0</td>
<td>A+</td>
<td>15.90</td>
<td>41.66</td>
</tr>
<tr>
<td>MIRBUD</td>
<td>4.5/5.0</td>
<td>BB+</td>
<td>1.39</td>
<td>4.25</td>
</tr>
<tr>
<td>MOSTALPLC</td>
<td>4.0/5.0</td>
<td>A-</td>
<td>10.32</td>
<td>90.47</td>
</tr>
<tr>
<td>MOSTALWAR</td>
<td>3.5/5.0</td>
<td>CCC</td>
<td>6.05</td>
<td>75.96</td>
</tr>
<tr>
<td>MOSTALZAB</td>
<td>4.0/5.0</td>
<td>BBB+</td>
<td>2.18</td>
<td>20.33</td>
</tr>
<tr>
<td>MSXRESOUR</td>
<td>3.5/5.0</td>
<td>D</td>
<td>1.07</td>
<td>327.50</td>
</tr>
<tr>
<td>PANOWA</td>
<td>4.0/5.0</td>
<td>BB</td>
<td>15.75</td>
<td>40.43</td>
</tr>
<tr>
<td>PROCHEM</td>
<td>4.5/5.0</td>
<td>AA+</td>
<td>16.65</td>
<td>98.30</td>
</tr>
<tr>
<td>PROJPRZEM</td>
<td>2.5/5.0</td>
<td>AA+</td>
<td>5.43</td>
<td>54.23</td>
</tr>
<tr>
<td>RESBUD</td>
<td>3.0/5.0</td>
<td>AAA</td>
<td>2.49</td>
<td>12.44</td>
</tr>
<tr>
<td>TESGAS</td>
<td>4.5/5.0</td>
<td>AA+</td>
<td>3.60</td>
<td>15.97</td>
</tr>
<tr>
<td>TRAKCJA</td>
<td>4.0/5.0</td>
<td>B+</td>
<td>8.24</td>
<td>41.95</td>
</tr>
<tr>
<td>ULMA</td>
<td>3.5/5.0</td>
<td>AAA</td>
<td>57.75</td>
<td>320.40</td>
</tr>
<tr>
<td>UNIBEP</td>
<td>4.0/5.0</td>
<td>BB+</td>
<td>8.05</td>
<td>9.64</td>
</tr>
<tr>
<td>ZUE</td>
<td>3.5/5.0</td>
<td>BBB</td>
<td>6.65</td>
<td>15.06</td>
</tr>
</tbody>
</table>
In table 2, the most important ratios presenting the financial condition of the construction sector's companies were presented. In 24 surveyed companies, the generated profit per share was reported in 20 companies. It shows that the construction companies prosper properly on the financial market and are able to record higher or lower profits (Parvi, 2014, pp. 262-267). The price to the operating earnings shows the losses of the company, and this state of affairs was reported in 7 examined stock exchange quoted companies (Damodaran, 2012, pp. 45-46). MOSTALPLC, MSXRESOUR, RESBUD and ULMA generated negative double-digit ratio, and ZUE – a negative three-digit ratio.

In contrast, analysing P/BV and P/P, it should be noticed that both the price to the book value and the price to profit demonstrate that nine companies operate excellently on the market and have a value of c. 1.0 and above, and the best of them are BUDIMEX and RESBUD. Other companies do not differ significantly from average values (Parvi, 2014, pp. 179-185).

Table 2: Technical evaluation of the construction sector's companies quoted on the Warsaw Stock Exchange in Poland as of 30.09.2014 (own development based on the financial data of the companies quoted on the Warsaw Stock Exchange in Poland)

<table>
<thead>
<tr>
<th>Name</th>
<th>P/OE (price/operating earnings)</th>
<th>P/BV (price/book value)</th>
<th>P/P (price/profit)</th>
<th>Profit per share</th>
</tr>
</thead>
<tbody>
<tr>
<td>BIPROMET</td>
<td>-6.53</td>
<td>0.45</td>
<td>0.54</td>
<td>-0.020</td>
</tr>
<tr>
<td>BUDIMEX</td>
<td>9.61</td>
<td>7.33</td>
<td>0.70</td>
<td>1.876</td>
</tr>
<tr>
<td>CNT</td>
<td>10.97</td>
<td>1.40</td>
<td>0.75</td>
<td>0.138</td>
</tr>
<tr>
<td>ELBUDOWA</td>
<td>9.27</td>
<td>1.08</td>
<td>0.35</td>
<td>2.982</td>
</tr>
<tr>
<td>ELEKTROTI1</td>
<td>39.82</td>
<td>1.27</td>
<td>0.50</td>
<td>0.020</td>
</tr>
<tr>
<td>ELKOP</td>
<td>6.74</td>
<td>0.38</td>
<td>4.23</td>
<td>0.030</td>
</tr>
<tr>
<td>ENAP</td>
<td>7.14</td>
<td>1.26</td>
<td>0.44</td>
<td>0.034</td>
</tr>
<tr>
<td>ERBUD</td>
<td>8.79</td>
<td>1.22</td>
<td>0.22</td>
<td>0.550</td>
</tr>
<tr>
<td>HERKULES</td>
<td>11.71</td>
<td>0.64</td>
<td>1.17</td>
<td>0.067</td>
</tr>
<tr>
<td>INSTALKRK</td>
<td>5.72</td>
<td>0.57</td>
<td>0.22</td>
<td>0.865</td>
</tr>
<tr>
<td>MIRBUD</td>
<td>3.02</td>
<td>0.39</td>
<td>0.11</td>
<td>-0.005</td>
</tr>
<tr>
<td>MOSTALPLC</td>
<td>-11.07</td>
<td>0.54</td>
<td>0.21</td>
<td>0.142</td>
</tr>
<tr>
<td>MOSTALWAR</td>
<td>-1.01</td>
<td>0.56</td>
<td>0.10</td>
<td>0.171</td>
</tr>
<tr>
<td>MOSTALZAB</td>
<td>10.22</td>
<td>1.15</td>
<td>0.41</td>
<td>0.045</td>
</tr>
<tr>
<td>MSXRESOUR</td>
<td>-11.94</td>
<td>0.12</td>
<td>4.26</td>
<td>4.199</td>
</tr>
<tr>
<td>PANNOVA</td>
<td>4.28</td>
<td>0.53</td>
<td>0.81</td>
<td>0.385</td>
</tr>
<tr>
<td>PROCHEM</td>
<td>19.14</td>
<td>0.53</td>
<td>0.43</td>
<td>0.521</td>
</tr>
<tr>
<td>PROPRZEM</td>
<td>140.83</td>
<td>0.31</td>
<td>0.18</td>
<td>0.034</td>
</tr>
<tr>
<td>RESBUD</td>
<td>-26.52</td>
<td>2.16</td>
<td>65.24</td>
<td>(I/Q 2011) -3.629</td>
</tr>
<tr>
<td>TESGAS</td>
<td>125.34</td>
<td>0.53</td>
<td>0.52</td>
<td>0.029</td>
</tr>
<tr>
<td>TRAKCIA</td>
<td>5.64</td>
<td>0.61</td>
<td>0.21</td>
<td>0.058</td>
</tr>
<tr>
<td>ULMA</td>
<td>-39.24</td>
<td>1.04</td>
<td>1.52</td>
<td>0.033</td>
</tr>
<tr>
<td>UNIBEP</td>
<td>11.60</td>
<td>1.44</td>
<td>0.29</td>
<td>0.151</td>
</tr>
<tr>
<td>ZUE</td>
<td>-275.02</td>
<td>0.83</td>
<td>0.28</td>
<td>0.093</td>
</tr>
</tbody>
</table>
In table 3, the studies concerning, among others, the net profit, depreciation, EBITDA and assets of the construction sector’s companies and the book value per share are presented. According to the obtained values, it is clear that only BIPROMET, MIRBUD and RESBUD showed a loss, which was confirmed by the previous ratios included in the table 2. Other companies showed a substantial profit generated in the third quarter of 2014.

Table 3: The technical evaluation of the construction sector’s companies quoted on the Warsaw Stock Exchange in Poland as of 30.09.2014 (own development based on the financial data of the companies quoted on the Warsaw Stock Exchange in Poland)

<table>
<thead>
<tr>
<th>Name</th>
<th>Net profit (net loss) in thousands PLN</th>
<th>Depreciation in thousands PLN</th>
<th>EBITDA in thousands PLN</th>
<th>Assets in thousands PLN</th>
<th>Book value per share in PLN</th>
</tr>
</thead>
<tbody>
<tr>
<td>BIPROMET</td>
<td>-124</td>
<td>301</td>
<td>-4</td>
<td>84419</td>
<td>8.749</td>
</tr>
<tr>
<td>BUDIMEX</td>
<td>47891</td>
<td>0</td>
<td>66334</td>
<td>3671851</td>
<td>18.006</td>
</tr>
<tr>
<td>CNT</td>
<td>1252</td>
<td>117</td>
<td>1603</td>
<td>69613</td>
<td>5.643</td>
</tr>
<tr>
<td>ELBUDOWA</td>
<td>14159</td>
<td>3398</td>
<td>21134</td>
<td>824437</td>
<td>69.461</td>
</tr>
<tr>
<td>ELEKTROTI</td>
<td>200</td>
<td>0</td>
<td>341</td>
<td>116499</td>
<td>7.666</td>
</tr>
<tr>
<td>ELKOP</td>
<td>3173</td>
<td>-79</td>
<td>2968</td>
<td>62633</td>
<td>0.530</td>
</tr>
<tr>
<td>ENAP</td>
<td>678</td>
<td>132</td>
<td>641</td>
<td>25612</td>
<td>0.783</td>
</tr>
<tr>
<td>ERBUD</td>
<td>6998</td>
<td>1827</td>
<td>11435</td>
<td>951293</td>
<td>20.709</td>
</tr>
<tr>
<td>HERKULES</td>
<td>2904</td>
<td>4143</td>
<td>9156</td>
<td>355091</td>
<td>4.413</td>
</tr>
<tr>
<td>INSTALKRK</td>
<td>6299</td>
<td>0</td>
<td>8807</td>
<td>394485</td>
<td>27.376</td>
</tr>
<tr>
<td>MIRBUD</td>
<td>-395</td>
<td>1370</td>
<td>7168</td>
<td>772486</td>
<td>2.917</td>
</tr>
<tr>
<td>MOSTALPLC</td>
<td>284</td>
<td>466</td>
<td>-278</td>
<td>74797</td>
<td>30.483</td>
</tr>
<tr>
<td>MOSTALWAR</td>
<td>3411</td>
<td>6464</td>
<td>16175</td>
<td>1554558</td>
<td>9.498</td>
</tr>
<tr>
<td>MOSTALZAB</td>
<td>6754</td>
<td>3630</td>
<td>14176</td>
<td>582533</td>
<td>1.789</td>
</tr>
<tr>
<td>MSXRESOUR</td>
<td>57544</td>
<td>0</td>
<td>-271</td>
<td>681929</td>
<td>16.296</td>
</tr>
<tr>
<td>PANOVA</td>
<td>3851</td>
<td>530</td>
<td>7801</td>
<td>589195</td>
<td>29.059</td>
</tr>
<tr>
<td>PROCHEM</td>
<td>2031</td>
<td>582</td>
<td>3210</td>
<td>196432</td>
<td>28.617</td>
</tr>
<tr>
<td>PROJPRZEM</td>
<td>207</td>
<td>0</td>
<td>213</td>
<td>148408</td>
<td>17.018</td>
</tr>
<tr>
<td>RESBUD</td>
<td>(IIQ 2011) -3048</td>
<td>(IIQ 2011) 83</td>
<td>(IIQ 2011) -3097</td>
<td>(IIQ 2011) 17818</td>
<td>(IIQ 2011) 8.830</td>
</tr>
<tr>
<td>TESGAS</td>
<td>325</td>
<td>0</td>
<td>175</td>
<td>109440</td>
<td>6.711</td>
</tr>
<tr>
<td>TRAKCJA</td>
<td>23766</td>
<td>0</td>
<td>32649</td>
<td>1684664</td>
<td>1.586</td>
</tr>
<tr>
<td>ULMA</td>
<td>173</td>
<td>16548</td>
<td>16557</td>
<td>345247</td>
<td>54.492</td>
</tr>
<tr>
<td>UNIBEP</td>
<td>5192</td>
<td>0</td>
<td>4797</td>
<td>702154</td>
<td>5.500</td>
</tr>
<tr>
<td>ZUE</td>
<td>2134</td>
<td>0</td>
<td>3531</td>
<td>457340</td>
<td>8.388</td>
</tr>
</tbody>
</table>
The book value per share shows that companies are overvalued, and those ELBUDOWA, MOSTALPLC and ULMA, and in case of two companies, such as ELKOP and ENAP, they are undervalued. However, it is important not to follow this opinion because the values are only the book values value (Froehlich, 2013, pp. 67-75), and the calculation of them is purely mathematical and financial. In case of using the economic attitude and interpretation, it would occur that the companies do not have the fair value (table 3) (Parvi, 2014, pp. 168-177).

Currently, the value of companies significantly deviates from the maximum value achieved a few years ago. The only exception is BUDIMEX, which achieved the maximum value in its history. Other companies have the value less than 50%-90% of the maximum one (table 4).

Table 4: The construction sector’s companies quoted on the Warsaw Stock Exchange in Poland as of 7.01.2015 (own development based on the financial data of the companies quoted on the Warsaw Stock Exchange in Poland)

<table>
<thead>
<tr>
<th>Name</th>
<th>Current value</th>
<th>Maximum value</th>
<th>Fair value</th>
<th>Deviation from the fair value in PLN</th>
</tr>
</thead>
<tbody>
<tr>
<td>BIPROMET</td>
<td>3.81</td>
<td>20.46</td>
<td>15.34</td>
<td>11.53</td>
</tr>
<tr>
<td>BUDIMEX</td>
<td>139.00</td>
<td>141.50</td>
<td>141.00</td>
<td>2.00</td>
</tr>
<tr>
<td>CNT</td>
<td>8.00</td>
<td>33.98</td>
<td>21.85</td>
<td>13.85</td>
</tr>
<tr>
<td>ELBUDOWA</td>
<td>76.41</td>
<td>219.80</td>
<td>176.54</td>
<td>100.13</td>
</tr>
<tr>
<td>ELEKTROTI</td>
<td>10.15</td>
<td>31.88</td>
<td>18.25</td>
<td>8.10</td>
</tr>
<tr>
<td>ELKOP</td>
<td>1.50</td>
<td>28.84</td>
<td>11.45</td>
<td>9.95</td>
</tr>
<tr>
<td>ENAP</td>
<td>0.99</td>
<td>2.86</td>
<td>1.99</td>
<td>1.00</td>
</tr>
<tr>
<td>ERBUD</td>
<td>25.80</td>
<td>95.34</td>
<td>65.41</td>
<td>39.61</td>
</tr>
<tr>
<td>HERKULES</td>
<td>2.80</td>
<td>26.82</td>
<td>16.32</td>
<td>13.52</td>
</tr>
<tr>
<td>INSTALKRK</td>
<td>15.90</td>
<td>41.66</td>
<td>24.69</td>
<td>8.79</td>
</tr>
<tr>
<td>MIRBUD</td>
<td>1.39</td>
<td>4.25</td>
<td>3.54</td>
<td>2.15</td>
</tr>
<tr>
<td>MOSTALPLC</td>
<td>10.32</td>
<td>90.47</td>
<td>32.47</td>
<td>22.15</td>
</tr>
<tr>
<td>MOSTALWAR</td>
<td>6.05</td>
<td>75.96</td>
<td>36.45</td>
<td>30.40</td>
</tr>
<tr>
<td>MOSTALZAB</td>
<td>2.18</td>
<td>20.33</td>
<td>14.78</td>
<td>12.60</td>
</tr>
<tr>
<td>MSXRESOUR</td>
<td>1.07</td>
<td>327.50</td>
<td>59.47</td>
<td>58.40</td>
</tr>
<tr>
<td>PANova</td>
<td>15.75</td>
<td>40.43</td>
<td>26.33</td>
<td>10.58</td>
</tr>
<tr>
<td>PROCHEM</td>
<td>16.65</td>
<td>98.30</td>
<td>47.89</td>
<td>31.24</td>
</tr>
<tr>
<td>PROPRZEM</td>
<td>5.43</td>
<td>54.23</td>
<td>27.49</td>
<td>22.06</td>
</tr>
<tr>
<td>RESBUD</td>
<td>2.49</td>
<td>12.44</td>
<td>7.63</td>
<td>5.14</td>
</tr>
<tr>
<td>TESGAS</td>
<td>3.60</td>
<td>15.97</td>
<td>9.87</td>
<td>6.27</td>
</tr>
<tr>
<td>TRAKCJA</td>
<td>8.24</td>
<td>41.95</td>
<td>17.55</td>
<td>9.31</td>
</tr>
<tr>
<td>ULMA</td>
<td>57.75</td>
<td>320.40</td>
<td>143.61</td>
<td>85.86</td>
</tr>
<tr>
<td>UNIBEP</td>
<td>8.05</td>
<td>9.64</td>
<td>9.60</td>
<td>1.55</td>
</tr>
<tr>
<td>ZUE</td>
<td>6.65</td>
<td>15.06</td>
<td>10.79</td>
<td>4.14</td>
</tr>
</tbody>
</table>
However, the fair value which should be reflected by the share prices of the examined companies significantly differs from the calculated value, which was presented in the table 4. In some cases, it is even 50% of the current value. However, the fair value is significantly higher than the current value of the examined companies, and in one company, BUDIMEX, it is only similar.

5. CONCLUSION
The share price of the construction sector's companies quoted on the Warsaw Stock Exchange in Poland is significantly underestimated by the current financial situation in the world (Jabłoński, 2011, pp. 32-55). Construction companies should show greater value, or at least the fair value, as property prices are stable, and they even increase, and profits of construction companies indicate the good financial condition. It particularly applies to large construction companies, such as BUDIMEX. The value of the construction sector companies should be appreciated because these companies have most of the assets expressed in inventory and real estate. Construction companies earn because they largely focus on the sale of construction materials as well as design and construction of new housing and commercial buildings, while sale prices are increasing. Construction companies achieve enormous profits, which was proved in examination of ratios in last years and a net profit in the third quarter of 2014. The fair value of the construction sector's companies quoted on the Warsaw Stock Exchange in Poland should be reached within four years, that is up to 2019, while the situation of global financial markets is improving.

LITERATURE
12. stooq.pl - portal giełdowy - http://stooq.pl/q/?s=wig_budow&c=10y&t=1&d=a=lg&b=0
EU CORPORATE GOVERNANCE, RECENT TRENDS AND DEVELOPMENTS, RELATED TO BOARD COMPOSITION AND CONFLICT OF INTERESTS

Rado Bohinc
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ABSTRACT
A modern and efficient corporate governance framework for European undertakings, investors and employees must be adapted to the needs of today’s society and to the changing economic environment. High performing, effective boards are needed to challenge executive management. This means that boards need independent non-executive members with diverse views, skills and appropriate professional experience. Such members must also be willing to invest sufficient time in the work of the board. The article addresses the following subjects which are at the heart of good corporate governance:

Comply or explain approach: The ‘comply or explain’ principle is an important tool for the application of the corporate governance rules in the EU. Most corporate governance is soft law and guidelines are included in voluntary national codes of conduct. In principle, member countries decide upon what type of legal instrument to use, in the respective field: mandatory or ‘comply or explain’.

Board of directors, structure and composition: There is no uniform approach as regard structure of corporate governance. As generally known, there are two basic concepts of the public limited (joint stock) companies’ corporate governance structures: one and two tier system. In EU, different board structures coexist. Depending on the country, listed companies may put in place either a ‘single board’ system (also called ‘monistic’ or ‘unitary board’ system), a two-tier (or ‘dual board’) system or some form of mixed system.

Non-executive or supervisory directors: The administrative, managerial and supervisory bodies should include an appropriate balance of executive (managing) and non-executive (supervisory) directors such that no individual or small group of individuals can dominate decision-making on the part of these bodies. A sufficient number of independent non-executive or supervisory directors should be elected to the (supervisory) board of companies to ensure that any material conflict of interest involving directors will be properly dealt with.

Independent directors: A director should be considered to be independent only if he is free of any business, family or other relationship, with the company, its controlling shareholder or the management of either, that creates a conflict of interest such as to impair his judgement. duties is assured (Annex II, which identifies a number of situations reflecting the relationships or circumstances usually recognised as likely to generate material conflict of interest). Boards should be organised in such a way that a sufficient number of independent non-executive or supervisory directors play an effective role in key areas where the potential for conflict of interest is particularly high.

Board committees: Nomination, remuneration and audit committees should be created. The nomination, remuneration and audit committees should make recommendations aimed at preparing the decisions to be taken by the (supervisory) board itself. The primary purpose of
the committees should be to increase the efficiency of the (supervisory) board by making sure that decisions are based on due consideration, and to help organise its work with a view to ensuring that the decisions it takes are free of material conflicts of interest.

**Keywords:** Non-executive or supervisory director, Board committees, Independent directors, Qualifications and commitment of directors, Evaluation, transparency and communication of the (supervisory) board

### 1. INTRODUCTION

The ‘Europe 2020’ Communication\(^{118}\) calls for improvement of the business environment in Europe. An effective corporate governance framework is of key **importance to society**, as well-run companies are likely to be **more competitive and more sustainable** in the long term (2102 COMMUNICATION Action Plan: European company law).

Corporate governance and company law are essential to ensure that companies are well-governed and sustainable in the long term and therefore have an important role to play in the long-term financing of the economy\(^{119}\).

Good corporate governance is first and foremost the responsibility of the company concerned. Rules at European and national level are in place to ensure that certain standards are respected. These include legislation and soft law, namely national corporate governance codes\(^{120}\).

EU Company law is lagging behind the developments in the EU and world economy. In any discussion on the future of EU company law, the financial and economic crisis that has challenged the business environment over the last years must be taken into account. It is obvious that weaknesses and malfunctions in EU company law have contributed to the crisis.

The last comprehensive analysis of European Company Law is the Plan on Modernising Company Law and Enhancing Corporate Governance in the European Union and the subsequent consultation on future priorities for this Action Plan carried out in 2005 and 2006 (2102 COMMUNICATION Action Plan: European company law).


Moreover, the Commission adopted two Recommendations regarding the role of independent non-executive directors and remuneration (Commission Recommendations 2005/162/EC and 2004/913/EC).

Besides, the Second Company Law Directive on formation of public limited liability companies and the maintenance and alteration of their capital8 and the Third and Sixth Company Law Directive on mergers and divisions have been simplified (Directives2007/63/EC and 2009/109/EC amending Directives 78/855/EEC and 82/891/EEC).

A number of legal solutions concerning the functioning of financial markets including those regulating the issues of directors’ disqualification and of the conflicts of interest arising

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\(^{120}\) 2014/208/EU: Commission Recommendation of 9 April 2014 on the quality of corporate governance reporting ('comply or explain’) Text with EEA relevance (2014/208/EU)
between shareholders and managers, and those between shareholders and creditors, turned out to be weak, and therefore inappropriate and obsolete. Harmonization can provide common rules and standards or it can remove obstacles. The choice of legal instrument ranges from directly binding regulations to directives requiring national implementation (Commission, 2011b). Mere recommendations are not sufficient any more in fields like conflict of interest and directors’ disqualification. Frankly speaking, there are some binding regulations (directives), which have been implemented into national legislations, especially in the field of financial market regulation, but this does not correspond with the emerging needs, caused by the circumstances of the crisis and nor does it aim to overcome them. Harmonization in the field of conflict of interest and directors’ boards composition would make cross-border business operations in the EU market more transparent and contribute to sufficient safeguards against abuse, and prevent people engaged in abuse in one member state from continuing to carry on their abuse in another member state.

2. COMPLY OR EXPLAIN’ APPROACH
2.1. Comply or explain approach
The ‘comply or explain’ principle is an important tool for the application of the corporate governance rules in the EU. Most corporate governance is soft law and guidelines are included in voluntary national codes of conduct. In principle, member countries decide upon what type of legal instrument to use, in the respective field: mandatory or ‘comply or explain’.

The “comply or explain” approach allows listed companies to depart from a particular recommendation of the applicable national corporate governance code, provided that they explain the reasons for doing so. In this way, it offers companies an important degree of flexibility to adapt their corporate governance to their specific situation, yet encourages them to follow corporate governance best practices. Also corporate governance codes in the EU are applied on a ‘comply or explain’ basis. This approach allows companies to depart from particular recommendations of the applicable code, provided they explain the reasons for doing so.

2.2. Mandatory corporate governance reporting
EU directive (Directive 2013/34/EU on the annual financial statements) requires companies to include a corporate governance statement in their management report if their transferable securities are admitted to trading on a regulated market of any Member State (see also Directive 2004/39 on markets in financial instruments);

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According to the ‘comply or explain’ principle (Article 20 of Directive 2013/34/EU) companies that depart from the relevant corporate governance code are required to explain in their corporate governance statement which parts of the code they depart from and the reasons for doing so.

2.3. Shortcomings in the way of the ‘comply or explain’

In many Member States there is insufficient monitoring of the application of the codes. The informative quality of explanations published by companies departing from the corporate governance code’s recommendation is - in the majority of the cases - not satisfactory. The quality of the corporate governance reports produced by listed companies has been subject to criticism. The explanations provided by companies are often insufficient. They either simply state that they had departed from a recommendation without any further explanation, or provide only a general or limited explanation (Study on Monitoring).

There are shortcomings in the way the ‘comply or explain’ principle is applied. Companies often do not provide appropriate explanations when they depart from corporate governance codes. There is too much of flexibility in the implementation of the ‘comply or explain’ approach. This makes it more difficult for investors to take informed investment decisions; they are in favour of better quality explanations (2011 Green Paper)

2.4. Directive, rather than recommendations

Companies should provide better explanations for departing from codes’ recommendations. In some Member States discussions have been initiated or guidelines issued on the quality of explanations (2102 COMMUNICATION Action Plan: European company law).

However in order to maintain the key role of codes of conduct in ensuring good corporate governance and their legitimacy, more decisive action at EU level is needed. However the existing recommendation (2014 Recommendation on ‘comply or explain’ reporting) is not sufficient in order to implement EU guidance, across the EU. A directive, based on national best practices, legally binding for listed companies, investors and national monitoring bodies would be needed to improve the quality of disclosures and ensure better transparency.

National binding rules for companies, following the directive, should provide guidance on how they followed the relevant corporate governance codes on the topics of most importance for shareholders, in order to improve transparency and quality of corporate governance reporting and on how listed companies should explain their departures from the recommendations of the relevant corporate governance codes.

To what extent and how apply the ‘comply or explain’ approach (governance code recommendations) as opposed to compulsory regulation should depend on the corporate governance tradition and the level of business ethic in a respective country. Universal patterns and recipes for each country, regardless its corporate history and tradition, is wrong approach.

3. BOARD OF DIRECTORS

3.1. No uniform approach as regard structure of corporate governance

As generally known, there are two basic concepts of the public limited (joint stock) companies' corporate governance structures: one and two tier system. As concerns the legal regulation of the governance structures there is the approach of compulsory one tier system (like USA, UK and the followers) or compulsory two tier system (Germany, Austria and the followers). In addition, there are countries which leave shareholders to decide upon introduction on one or two tier system, according to Articles of Incorporation as France, Finland or for example Slovenia. There are also countries with different types of two tier
system, with different competences and legal position of the Supervisory body, which range
from more or less classical supervisory board, to supervisory or other monitoring and auditing
bodies with limited competences. In addition there are legislations, with conditional and/or
limited one or two tier system of corporate governance.
On a unitary board, one way to ensure this is that the roles of chairman and chief executive
are separate; in the case of unitary and dual boards, one option may be that the chief executive
does not immediately become the chairman of the (supervisory) board.
In EU, different board structures coexist. Depending on the country, listed companies may put
in place either a ‘single board’ system (also called ‘monistic’ or ‘unitary board’ system), a
two-tier (or ‘dual board’) system or some form of mixed system. These board structures are
often deeply rooted in the country’s overall economic governance system.

3.2. Other stakeholders’ participation
It is important to underline that different governance systems have very little to do with the
participation of other but capital stakeholders in in governance and appropriation in the profit
of a corporation. All the different systems of corporate governance follow the same concept,
the concept of one share one vote. The differences are not related to diversified stakeholders’
participation in governing and supervising bodies (like labour) but rather to different
organization of managerial and supervisory functions.
Yet there are systems, that permit more influence to employee representatives in management
or supervisory board, however that should be considered as mere correction of dominant
capital based corporate governance rather than corporate governance reform in the terms of
changing the relationship between labour and capital.

3.3. Board composition
The composition of the board has to suit the company’s business. Non-executive board
members should be selected on the basis of a broad set of criteria, i.e. merit, professional
qualifications, experience, the personal qualities of the candidate, independence and diversity
(professional, international and gender). Diversity in the members’ profiles and backgrounds
gives the board a range of values, views and sets of competencies. It can lead to a wider pool
of resources and expertise. Different leadership experiences, national or regional backgrounds
or gender can provide effective means to tackle ‘group-think’ and generate new ideas. More
diversity leads to more discussion, more monitoring and more challenges in the boardroom
(2011 Green paper).

122 Basically there are three different approaches:
1. There is only two-tier management system under German law and Austrian (G AktG) for
stock corporation (AG).
2. The French Societe anonyme (SA) can be, like Public Limited Company in some other
countries managed in one of two ways either under a two tier-board, or under a single board.
It is up to shareholders to decide on the system of corporate governance, but so far in France,
unlike some other countries one tier system, by far, prevails.
3. US and UK corporate law only provide for a single board system with no compulsory
labour representation. There is no two tier system under US and UK law.
In addition there is a number of other countries with one tier system only, or at least
predominant one tier system, like Finland, Spain, Sweden, Greece, Cyprus, Turkey, Canada,
etc. On the other hand there are many countries with predominant, but not exclusive two tier
system, or with different mixed systems, some of which we are presenting in this article.
Diversity of competences and views among the board’s members is very important. It facilitates understanding of the business organization and affairs and thus enables the board to challenge the management’s decisions objectively and constructively. In contrast, insufficient diversity could lead to a so-called group-think process, translating into less debate, fewer ideas and challenges in the boardroom and potentially less effective oversight of the management board or executive directors. Increased transparency as regards board diversity policy (including gender balance among non-executive directors) could make companies reflect more on the issue (2011 GREEN PAPER Anex 2).

In order to encourage companies to enhance board diversity and give greater consideration to non-financial risks, disclosure requirements with regard to their board diversity policy was strengthened through amendment of the accounting Directive.

4. CONFLICTS OF INTEREST

4.1. Independent directors on the board

Independent representatives on the board, capable of challenging the decisions of management, is widely considered as a means of protecting the interests of shareholders and other stakeholders. In companies with a dispersed ownership, the primary concern is how to make managers accountable to weak shareholders. In companies with controlling shareholders, the focus is more on how to make sure that the company will be run in a way that sufficiently takes into account the interests of minority shareholders. Ensuring adequate protection for third parties is relevant in both cases (2003 Action Plan ‘Modernising Company Law).

A sufficient number of independent non-executive or supervisory directors should be elected to the (supervisory) board of companies to ensure that any material conflict of interest involving directors will be properly dealt with.

4.2. Profile of independent non-executive or supervisory directors (for listed companies)

A director should be considered to be independent only if he is free of any business, family or other relationship, with the company, its controlling shareholder or the management of either, that creates a conflict of interest such as to impair his judgement. duties is assured, which identifies a number of situations reflecting the relationships or circumstances usually recognised as likely to generate material conflict of interest).

There is no definition and legal regulation of “independence” in the context of directors, in any of the laws analysed. The independency of directors is not a legal obligation to be taken into consideration for the composition of corporate boards.

On the other hand, there are explanations in different codes and EU recommendations on this. However, the respective recommendation leaves it to the member countries to decide whether to implement the recommendation in the company legislation or to use the principle to explain or comply with the corporate governance codes. Unfortunately, the great majority of EU member countries decided for the latter, the consequence of which is poor implementation of legal remedies for solving conflicts of interest in European corporate legislation.

4.3. Criteria for independency

Criteria for independency, which should be, for listed companies, tailored to the national context, should be based on due consideration of at least the following situations (Anex II to Recommendation 2005/162 on the role of non-executive or supervisory directors):
(a) not to be an executive or managing director of the company or an associated company, and not having been in such a position for the previous five years;

(b) not to be an employee of the company or an associated company, and not having been in such a position for the previous three years, except when the non-executive or supervisory director does not belong to senior management and has been elected to the (supervisory) board in the context of a system of workers’ representation recognised by law and providing for adequate protection against abusive dismissal and other forms of unfair treatment;

(c) not to receive, or have received, significant additional remuneration from the company or an associated company apart from a fee received as non-executive or supervisory director. Such additional remuneration covers in particular any participation in a share option or any other performance-related pay scheme; it does not cover the receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the company (provided that such compensation is not contingent in any way on continued service);

(d) not to be or to represent in any way the controlling shareholder(s) (control being determined by reference to the cases mentioned in Article 1(1) of Council Directive 83/349/EEC (1));

(e) not to have, or have had within the last year, a significant business relationship with the company or an associated company, either directly or as a partner, shareholder, director or senior employee of a body having such a relationship. Business relationships include the situation of a significant supplier of goods or services (including financial, legal, advisory or consulting services), of a significant customer, and of organisations that receive significant contributions from the company or its group;

(f) not to be, or have been within the last three years, partner or employee of the present or former external auditor of the company or an associated company;

(g) not to be executive or managing director in another company in which an executive or managing director of the company is non-executive or supervisory director, and not to have other significant links with executive directors of the company through involvement in other companies or bodies;

(h) not to have served on the (supervisory) board as a non-executive or supervisory director for more than three terms (or, alternatively, more than 12 years where national law provides for normal terms of a very small length);

(i) not to be a close family member of an executive or managing director, or of persons in the situations referred to in points (a) to (h);

4.4. Requirements for disclosure
In the majority of the EU countries, directors must make full disclosure of all the relevant facts referring to the contract concluded on his own behalf in the field of companies business activities. However, only in some legislation is it a legally binding provision rather than a recommendation of the code. Declaring interest in an existing transaction or an arrangement
under UK Law requires a director to declare any interest (direct or indirect) that he or she has in any transaction or arrangement entered into by the company.

There are four types of transaction requiring the approval of members in the Companies Act 2006: long-term service contracts, substantial property transactions, loans, quasi-loans and credit transactions and payments for the loss of office.

According to French law, the annual report gives details of the total remuneration and benefits of all kinds paid to each executive during the financial year from the company and controlled companies. The annual report also includes a list of all the posts and functions that each of those executives occupied in any company during the financial year. Contracts in which French directors are interested must be approved by the board, notified to the auditors and submitted to the general meeting.

According to the Slovenian Code, all legal transactions between the company and a member of the management board, as well as transactions between the company and persons or companies related to the member in whom he is personally involved are recommended (rather than legally defined as mandatory) to be concluded by observing the code of good practices and be publicly disclosed.

4.5. Non-executive or supervisory directors

Effective oversight of the executive directors or the management board by the non-executive directors or supervisory boards leads to successful governance of the company. Boards need non-executive (or supervisory board) members with diverse views, skills and appropriate professional experience. Board members must also be willing to invest sufficient time in the work of the board. (2011 GREEN PAPER Anex 2).

The administrative, managerial and supervisory bodies should include in total an appropriate balance of executive/managing and non-executive/supervisory directors such that no individual or small group of individuals can dominate decision-making on the part of these bodies. On a unitary board, one way to ensure this is that the roles of chairman and chief executive are separate; in the case of unitary and dual boards, one option may be that the chief executive does not immediately become the chairman of the (supervisory) board. (Recommendation 2005/162 on the role of non-executive or supervisory directors).

The EU position (Recommendation 2005/162 on the role of non-executive or supervisory directors) as to the role of non-executive or supervisory directors is, that in key areas where executive directors clearly have conflicts of interest (i.e. remuneration of directors, and

123 AFG recommends that at least one-third of the board be composed of members free from conflicts of interest; this is therefore not a legal obligation for the composition of a French board. To be qualified as being free from conflicts of interest a director must not be in a situation of a potential conflict of interest. In particular, therefore, he or she is recommended (this is not a legal obligation) not to:

- be a salaried employee or executive director of this company or of any company of the same group, nor to have been in such a position at any time during the past five years;
- be a salaried employee or executive director of a significant shareholder of this company or of any company of the same group;
- be a salaried employee or executive director of a significant or frequent commercial, banking, or financial partner of this company or of any company of the same group;
- have been the auditor of the company during the previous five years; nor
- have been a board member of this company for more than 12 years (AFG, 2001).
supervision of the audit of the company’s accounts), decisions in listed companies should be made exclusively by non-executive or supervisory directors who are in the majority independent.

Non-executive or supervisory directors are recruited by companies for a variety of purposes. Of particular importance is their role in overseeing executive or managing directors and dealing with situations involving conflicts of interests. Boards should be organised in such a way that a sufficient number of independent non-executive or supervisory directors play an effective role in key areas where the potential for conflict of interest is particularly high.

4.6. Role of the committee’s vis-à-vis the (supervisory) board
The nomination, remuneration and audit committees should make recommendations aimed at preparing the decisions to be taken by the (supervisory) board itself. The primary purpose of the committees should be to increase the efficiency of the (supervisory) board by making sure that decisions are based on due consideration, and to help organise its work with a view to ensuring that the decisions it takes are free of material conflicts of interest.

4.7. Qualifications and commitment
The (supervisory) board should ensure that it is composed of members who, as a whole, have the required diversity of knowledge, judgement and experience to complete their tasks properly. The members of the audit committee, should, collectively, have a recent and relevant background in and experience of finance and accounting for listed companies appropriate to the company’s activities.

Each director should devote to his duties the necessary time and attention, and should undertake to limit the number of his other professional commitments (in particular any directorships held in other companies) to such an extent that the proper performance of his duties is assured.

5. CONCLUSION
The company laws in EU member countries in the field of structure and composition of the board of directors and conflicts of interest and is not harmonized; there are separate and very diverse national pieces of legislation in this regard. Rules on diversity in composition and on independent directors and also on conflicts of interest at the EU level are mainly recommendations, rather than binding legal rules, which leave it to the member countries to decide either to implement the recommended concepts by legislation or merely in corporate governance codes (comply and explain).

Unfortunately, the voluntary principle “explain or comply” in corporate governance codes has been widely applied, as opposed to legislative implementation in EU member countries, which appears not to be the most appropriate and effective method of regulation, especially not in the times of world economic and financial crisis.

There are substantial and important differences in the legal regulation of board’s members’ position and conflicts of directors’ interests between the EU countries. Bearing in mind that the world economic and financial crisis was to an important extent caused by inefficient corporate governance regulation, especially in financial services, a substantial harmonization of the EU regulation in the field of board director’s diversity and independence, directors’ disqualification and conflict of interest would be welcome.
The financial crisis has highlighted how important it is for legislators to react to the changing business environment and to react in due time with efficient legal tools. Further harmonization of company law, not in general but in particular fields of company law (like board director’s diversity and independence, directors’ disqualification and conflict of interest) is more than needed. Due to the financial roots of the economic crisis, this is especially true for financial service companies and listed companies, dealing with a broader public in a very sensitive financial field.

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THE IMPACT OF PRODUCT INNOVATION ON THE MARKET POSITION AND PERFORMANCE OF THE COMPANY

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ABSTRACT
This article deals with the measurement of customer satisfaction among 320 randomly selected customers of the company, who have made the purchase in the last three months. The subject of the research is the size of the impact of the changed sales method (the way of selling), which represents an innovation in the process of selling company's products, on customer satisfaction. The study includes four of the company's relevant factors of customer satisfaction. These are: understandability of presentation, length of presentation, the (time of) product delivery and customer expectations of the product. The study is based on a survey, which was carried out as a telephone interview. The main question is whether a buyer is satisfied with the implementation of the sale and purchased product. The survey results confirm, that a majority of respondents is satisfied with the sales method and is up to buy any other product of the company. Among the objectives of the measurement of customer satisfaction, the most important for the company, is maintaining the contact with customers and expanding sales. There is a correlation between established innovation and customer satisfaction. There is also a correlation between customer satisfaction and his loyalty. More, as the company considers how to innovate the selling process, what will bring better perception of customer's needs and satisfying the identified needs, the more it can increase the market share and thereby the profits of the company.

Basic finding of this article is that introduced innovation into the sales process had positive impact on the customer satisfaction, with existing, as well as with new customers. Customers, because of theirs current satisfaction with a way of selling and satisfaction with product, indicate they are willing to buy also other kinds of products of the company.

Keywords: marketing innovation, company (enterprise), customer (buyer), satisfaction, loyalty.

1. THE IDEA, INVENTION, INNOVATION
The progress, caused by development of different technologies, requires from companies rapid adjustment to changing market conditions. The emergence of new companies and products greatly increases the competitive struggle for the market share. A company has to constantly innovate in the field of organization and management, products and technologies in order to maintain a competitive advantage on the market. Innovation in the field of products affect the rise of demand, innovation in the field of technology helps to reduce costs, while innovation in the field of organization and management affect the faster flow of information and creative potential of employees. According to the survey, which was carried out by Taghizadeh and Rahman (2013) there a lot of information available about the innovation and its impact on the company's success, particularly in the manufacturing sectors. In this, they rely on the research of the authors (Armbruster, Bikfalvi, Kinkel and Lay, 2008; Cetindamar & Ulusoy, 2008; Gunday et al, 2011; Kirner, Kinkel, and Jaeger, 2009; Lin et al, 2010). The results of the research show that innovation management in the services, have a strong impact on the overall performance of the company (Jiménez-Jiménez & Sanz-Valle, 2011; Ottenbacher, 2007; Sin, TSE, Heung, and YIM, 2005). Companies that are very focused on the innovation management in services, are more successful in the marketing of new products.
and supply of services, which contributes to the improvement of their performance (Eisingerich, Rubera, and Seifert, 2009) and competitive advantage (Chapman, Soosay, and Kandampully, 2003). J. Tidd, Bessant and Pavitt (2005) claim, that the management of innovation services, has a direct and positive impact on the improvement of business and growth, while improving the efficiency, productivity, quality, competitive position and market share. The method of innovation management in the company has a strong impact on the acquisition of new consumers, on the way of entering a new market, increasing a market share, maintaining customer, on customer satisfaction, the development of new products with the distribution, and process improvement (Hull, 2003, Hull and Tidd, 2003; Ottenbacher, 2007; Son et al., 2005). Innovation capacity of the company is reflected in the ability of the timely creation of inventions, based on the available science, and converting inventions into innovations that are reflected as a new product or service. Among inventions are also included processes of creation a new knowledge, which is based on the observation of the state of environment and thinking of how to improve the existing knowledge or adapt to specific conditions (Devetak in Likar, 2001, p. 17).

There are many definitions of innovation, for us it is interesting Schumpeter's division of innovation (Stanovnik and Kavas, 2004, p. 17), which is divided into:
- production, which include the introduction of new products,
- the process, which include the introduction of new methods of production,
- the market, which include the opening of new markets,
- entry, covering the conquest of new sources of raw material,
- organizational, which include the introduction of new organizational solutions.

The innovation process, which, due to selection process does not have a linear connection from invention to diffusion, Schumpeter divided into three phases:
- invention, which includes the generation of new ideas,
- innovation, which represents the conversion of new ideas into the form of new products and processes for commercial purposes,
- diffusion or spread.

The idea represents the wellspring of human activity (Makarovic, 2003, p. 25). New ideas can provoke the need for new methods of operation, new views on things and situations, new ways of organizing and presenting things, and finally new ideas on the ideas (De Bono, 2006, p. 24).

### 2. THE SATISFACTION AND LOYALTY OF CUSTOMERS

A major change that has occurred in the market of supply and demand, is that the market is on the demand side or on the customer side. A wide range of both, producers and variants of products and services, has enable the customers to put high requirements for the quality, prices and delivery times (Stanovnik and Kavas, 2004, p. 87).

Customer satisfaction in its essence is the emotional reaction of the customers, having purchased product or service. The buyer at the time of purchase detects a certain level of well-being, resulting a comparison between the perceived outcomes of the product or service, and personal expectations. Before the purchase a buyer has certain expectations. If they are satisfied after the purchase, he feels a sense of satisfaction. If its previous expectations are not satisfied, a buyer feels a sense of dissatisfaction, as it occurs a gap between expected and perceived quality (Potocnik, 2000, p. 181).

Customer satisfaction evokes a pleasant feelings, which means an emotional reaction of the customer, enjoying the benefits of the purchased product or service. When the buyer at the
time of a purchase does not receive the desired benefits, he feels a sense of dissatisfaction, that leads to unpleasant feelings, which reflect the specific problems, he is faced with. (Ule and Kline, 1996, p. 248). When making purchases a buyer acquires experience, on which he forms his expectations. These expectations represent a specified standard to the buyer, which is the basis for comparison of the quality and performance of the product or service after the purchase. The result of the comparison between the expected and the obtained value of the product is satisfaction or dissatisfaction. Satisfaction with the product encourages the buyer to re-purchase the product of a particular company, also he remains true to the company in the long run (Mozina, Zupancic and Stefanic Pavlovic, 2002, p. 200).

In the relationship with customers the companies want to create satisfaction, as satisfied customers transfer a positive experience to their environment and have a direct impact on the performance of the company, at the same time they remain potential candidates for repeated purchase. The loss of existing customers affects the profitability of the company, as according to some estimates, the cost of acquisition of new customers is five times greater than the cost of satisfying existing customers (Kotler, 2004, p. 85).

Damjan and Mozina (1999, p. 144), define loyalty as the emotion, that arises due to the belonging of the individual to some idea, person, or object. Loyalty and satisfaction are strongly mutually connected. Satisfaction represents the basic condition for loyalty, although the company can build the loyalty of the customer also through other factors. Oliver (1999 in Mozina et al., 2002, p. 210) identifies the most important elements, that influence the loyalty of the customer:
- More perceived value of a product or service,
- Personal strength of the buyer (eg. Susceptibility to change)
- Social determinacy of the buyer at the institutional level and
- Social determinacy of the buyer on a personal level.

3. MARKET SHARE, REVENUE AND PROFIT

Among results of innovation activity, the most important for the company is to increase of the market share, since it increases the revenue and profit (Likar and Kopac, 2007). Innovation income and profit are generated as a part of newly created value and are the result of innovation. The market determines their height. Innovation and innovation income represent the basis for the high competitiveness and for the investment and development skills (Earring, 2000, p. 377).

The competitiveness of a company represents its ability to use a competitive advantage in a given environment. The company can achieve a competitive advantage over its rivals in different ways. An advantage may be a new product, the better quality of products or better distribution. Competitive advantage is dynamic and short-term, which in the eyes of the customer is relative, as he compares it with competitors. The acquisition of competitive advantages companies form in different ways, with the understanding, that the most effective competitive advantage is based on knowledge and innovation (Pretnar, 2002, p. 33-34).

4. A SURVEY ON THE IMPACT OF INTRODUCED INNOVATION ON A CUSTOMER SATISFACTION

A survey on the measurement of customer satisfaction in the company X was carried out in the year of 2014 and is based on 320 randomly selected customers in the period of three months (from March to May). The object of the survey is a question, whether the introduced innovation had a positive influence on customer satisfaction. The survey includes four, for the company important factors of customer satisfaction. These are: understandability of presentation, length of presentation, the delivery of the product and the expectations of the
product. The research is based on the use of a survey, which was carried out as a telephone interview. The questionnaire consists of 9 questions, with a grade scale from 1 to 5, and is related to the measurement of customer satisfaction. In the assessment used numbers mean as follows: number 1 = very dissatisfied, number 2 = dissatisfied, number 3 = neutral, number 4 = satisfied, number 5 = very satisfied. The following 3 questions are closed-ended and refer to the existing customer cooperation with the company.

Results of the survey show that 86 (26.88%) of respondents participated in the old and the new method of presentation. Almost all customers, who had visited the old and the new presentation (84 persons) answered, that to them the new way of presentation is more likeable, as the old one. Only 2 respondents, who had participated in both ways of presentation, answered that they liked the old way of presentation more. Customers, that are familiar with both methods of presentation, are the most important to assess the introduction of the innovation, as they compare both ways of presentation, the old and the new one, due to their knowledge of both ways of presentation. Although the percentage of customers, who had participated in both ways of presentation is low, it is an important indicator of whether the introduced innovation has been successful.

Another important indicator of customer satisfaction and customer loyalty are the answers, provided by respondents referre to the question, if in the future they will decide to purchase in our company. From all of the 320 respondents, 99 answered with a yes. This means that 30.94% of the respondent customers had proved their loyalty to the company, although we do not know, whether they will actually make the purchase.

The percentage of rating values, made by all respondent customers, are shown in Table 1:

<table>
<thead>
<tr>
<th>Assessment</th>
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<tr>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>The clarity of the presentation.</td>
<td>0,00</td>
<td>0,00</td>
<td>1,56</td>
<td>46,88</td>
</tr>
<tr>
<td>The time (length) of the presentation.</td>
<td>0,00</td>
<td>0,00</td>
<td>0,31</td>
<td>34,69</td>
</tr>
<tr>
<td>The friendliness and accessibility of the sales staff.</td>
<td>0,00</td>
<td>0,00</td>
<td>2,50</td>
<td>27,50</td>
</tr>
<tr>
<td>The evidence about the quality of the presented products.</td>
<td>0,00</td>
<td>0,00</td>
<td>0,63</td>
<td>24,06</td>
</tr>
<tr>
<td>The understandability and completeness of the offer.</td>
<td>0,00</td>
<td>0,00</td>
<td>0,31</td>
<td>10,94</td>
</tr>
<tr>
<td>The speed and accuracy of the product delivery.</td>
<td>0,00</td>
<td>4,00</td>
<td>2,50</td>
<td>28,44</td>
</tr>
<tr>
<td>The product is surely met your expectations.</td>
<td>0,00</td>
<td>1,00</td>
<td>0,31</td>
<td>20,94</td>
</tr>
<tr>
<td>The assessment of the product in comparison with similar products.</td>
<td>0,00</td>
<td>0,00</td>
<td>0,94</td>
<td>38,44</td>
</tr>
<tr>
<td>The speed and efficiency of resolving complaints - in so far you practice it.</td>
<td>0,00</td>
<td>0,00</td>
<td>1,88</td>
<td>0,31</td>
</tr>
</tbody>
</table>

Source: own.
The analysis of the survey results shows, that there are 4 customers, who made a complaint, with their assessment of solving the complaint 4 or 5. The assessment 2 respondents commented on two set out arguments in terms of satisfaction, namely: the speed and accuracy of the product delivery (1,25% of all respondents), and satisfaction of the customer expectations about the product (0,31 % of all respondents). These two areas represent to the company the possibility for improving processes and increasing customer satisfaction in the future.

Most estimates, made by customers regarding satisfaction, are distributed between the ratings from 3 to 4, with the highest percentage of assessments of a particular parameter by rating 5. Customers gave the best assessment to the parameter «comprehensibility and completeness of the offer» - the average value is estimated at 4.88. The products met their expectations well, since the average value of ratings is 4.78. The average assessment on the evidence about the quality of the presented products is 4.75. The sales staff is friendly and accessible and therefore, they received an average rating of 4.68. The time or length of the presentation was estimated by the average value of 4.65. The speed and accuracy of the product delivery was estimated by the average value of 4.63. The average assessment on the comparison of the product with similar ones is 4.60, and the average assessment on the clarity (understandability) of the presentation is 4.50. All of the estimates, regarding the parameters of satisfaction, made by customers, are high. From this we can conclude, that the company sells high-quality products, which meet the customer expectations well. The introduction of innovation in the sales process is associated with customer satisfaction, regarding the clarity of the presentation and its length. Although these two parameters have not received the highest average ratings, they suggest, that the introduction of the innovation is successful.

Comparison of turnover during the years 2013 and 2014 for the same three-month period (March to May) shows a smaller increase, namely 2,34%.

5. CONCLUSION
Companies that are able to exploit their innovative potential, can successfully maintain or enhance their market position. Innovations significantly affect the revenue and profits of the companies. With systematic management of innovation processes in the company and with enhancing knowledge, customer added value can be increased. Customer satisfaction has significantly grown in importance because it represents an evaluation of the purchase made by a single buyer. In this the buyer compares his expectations about the quality of a product or service with the facts. These expectations are strongly influenced by experience. With customer satisfaction the company preserves the basis for successful business and growth. Customers who at the purchase feel satisfaction also grow pleasant feelings towards companies. These emotions create a positive opinion about the company and the willingness to remain faithful to that company in the future.

Companies verify the satisfaction of its customers in various ways. Given that companies are aware of the importance of customer satisfaction and that customer satisfaction is being measured, it is important that the results are usefully used. These results can be a source of new ideas for innovative work processes or products and services. Systematic management of innovations can ensure that a company becomes more competitive than others. By doing so, the company enables market success and long-term economic viability.

The survey revealed that customers of the company that introduced the innovation are happy and show loyalty to the company. The best confirmation that the introduced innovation had a positive impact on customer satisfaction is the satisfaction of those customers who participated in the old and new presentation methods. The customers who are familiar with both methods are most important for evaluating the introduction of the innovations since they
have knowledge of both presentation ways and can compare them to each other. Although the percentage of customers who participated in both ways of presentation is low, it is an important indicator of whether the introduced innovation is successful. Results from a customer satisfaction survey after innovations were introduced suggest, that innovation was successful. Introduced innovation in the sales process had a positive impact on satisfaction with existing and new customers. Customers due to existing satisfaction with the sales process and of the product indicate, that they are willing to buy other types of products from that company. Sales comparison for the same three-months period between 2013 and 2014 also confirms a slight but significant increase in sales.

LITERATURE
EVALUATION OF ACCOUNTING LEGAL REGULATION AND ITS ROLE IN THE QUALITY OF FINANCIAL REPORTING (AN ACTUAL OVERVIEW IN REPUBLIC OF KOSOVO)

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ABSTRACT
In order to ensure optimal conditions in the business entity, where all business operators should take right and effective decisions, it is necessary to provide basic information, which will help in this process. In this case, because of its special role and importance, we highlight the information that is generated by accounting.

In developing the accounting of a country, there are different factors that affect and not only economic, but also legal, social, cultural, and not just accountants but also users of accounting information. The change of these factors has resulted in the change of their impact on the development of accounting.

For the accounting to be understandable and credible, it must be constructed in accordance with the rules and specific instructions. This results in the necessity of accounting adjustments to provisions and harmonization with international standards. Like in all countries, as well as in Kosovo, there must exist and function the accounting regulator in full compliance with the standards of the country and, where appropriate, in coherence with the International Accounting Standards / International Financial Reporting Standards.

Based on statistical and econometric analysis of primary data collected, this paper will present a picture of the current accounting and financial reporting regulations in Kosovo, including the level of standardization of accounting as a tool for unifying the language of business to open the way for further development and integration.

Keywords: accounting, accounting information, accounting regulations, accounting and financial reporting standards, econometric model, financial reporting.

1. INTRODUCTION
The reason for appropriate regulations in the field of accounting and financial reporting based on best practices, meets the need for economic development, globalization of the economy, increased effectiveness in economic decision-making, especially in the growth of domestic investors and attracting investors outside, increasing the safety and reliability in obtaining accounting information. All these, and many other reasons, lead to the necessity of appropriate accounting regulations and obvious changes, additions or the relevant improvements.
2. ACCOUNTING REGULATIONS IN KOSOVO - AN OVERVIEW

Given the fact that in the postwar period in the economic life of our country were presented major changes, it has become necessary to review and improve the legal regulation of accounting, in order to be able to respond to new phenomena presented by the impact of modern developments. New phenomena arise frequently, so it is an imperative to develop accounting in accordance with these developments, in order to present economic events accurately and faithfully. For successful implementation of this process, there must be commitment by accountants and professional organizations for professional education, then the full harmonization of accounting legislation with other laws, such as commercial companies legislation, tax legislation, etc. In an economic environment very dynamic and oriented towards integration, through which the Kosovo economy is moving now, regulations are very essential in combating the informal economy\textsuperscript{126} and, among others, with aim to improve and enhance the quality of services provided by accounting for internal users as well as those external.

Effective accounting will help in the growth and development of businesses, and in order to achieve this serves as a mechanism Law no. 04 / L-014 (2011)\textsuperscript{126} for Accounting, Financial Reporting and Auditing, with the objective of increasing the quality of financial reporting in Kosovo. This law regulates the accounting system and financial reporting of companies, powers and responsibilities of the Kosovo Financial Reporting Council (hereinafter KFRC), audit requirements, qualifications for professional accountants, licensing of auditors and domestic and foreign firms to audit.\textsuperscript{127}

Businesses should prepare financial statements for general purposes by applying standard accounting administrative regulations and guidelines issued by KFRC, or may prepare financial statements in full compliance with international financial reporting standards (IFRS) by notifying the KFRC in. These standards are issued by the Board for International Accounting Standards (IASB), and which are approved by KCRF. Consolidated financial statements of these companies are prepared under Directive 78/660 / EEC EU and IFRS. KCRF will appoint committees as necessary, to ensure implementation of relevant standards\textsuperscript{128}. Categories of businesses for the purpose of financial reporting are classified under this law.\textsuperscript{129} The financial statements of these businesses include:

- \textit{Statement of financial position;}
- \textit{Statement of income and expenses;}
- \textit{Statement of changes in equity;}
- \textit{Statement of cash flows;}
- \textit{Documents accompanying financial statements.}

With this, based on the current level of economic development, is managed to create infrastructure and business environment, to provide more realistic information, in order to raise the level of reliability and attractiveness of our country internationally. Regarding this, at what level is estimated to be reliability that provide financial statements for decision making process, the information is provided based on data collected from the questionnaire

\textsuperscript{125} Dr. Florentina Xhelli Krasniqi, PhD Dissertation
\textsuperscript{126} Based on Article 65 (1) of the Constitution of the Republic of Kosovo.
\textsuperscript{127} Law 04/L-014, article 1
\textsuperscript{128} UE Asquis Communautaire, Directive no. 78/660/EEC, no. 83/349/EEC and no. 84/253/EEC of UE, article15, Law 04/L-014.
\textsuperscript{129} Article 4, Businesses are classified into large, medium, small and micro-enterprises.
designed for this purpose. On the question raised about the level of reliability that provide financial statements of businesses in general, they result in a high percentage of reliability, maybe not at all and this gives reason to understand that they should make further efforts to fully implement the accounting standards, which would result in a high level of reliability. As is known, the reliability of financial statements is also one of the qualitative characteristics, given that financial statements are the basis of economic decision-making for internal and external users of financial information. Meanwhile, the question addressed regarding the business environment and current accounting regulations, How do you see the current developments in the field of accounting regulations, the results are as follows: 66% of respondents are of the opinion that current developments in the field of accounting are good and necessary, while 20% of them think that such developments are not sufficient at present, so it should work even more in the future to ensure full implementation of these regulations (see diagram no. 1).

The indicator that is presented above is positive and shows good premise for further development of accounting in Kosovo. From this results transparency in reporting, then the comparability of our statements with those of other countries, creating a balance that exceeds the interest group and the creation of a compromise among business, and preparation of business reports with full legitimacy and credibility.

3. EMPIRICAL ANALYSIS THROUGH ECONOMETRIC MODELS

In this study, regression analysis was also performed, using ordered logit and ordered probit model on the probability of implementation of IAS by the business community in Kosovo.

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130 The questionnaire was realized with accountants employed in small, medium and large businesses, including those manufacturing, trade, service, financial institutions, and other participants from accounting field. The questionnaire was prepared in 5 levels, whereas, the selected sample is 400 persons.

131 Econometrics Analysis, William H. Greene, chapter 19, Models with Discrete Variables, Ordered Data
Regression or regression analysis means the study of dependence of one variable (characteristic), that is called the dependent variable by one or more other variables (explanatory), in order to predict or estimate the average value of the first variable according to last values already known or fixed (through repeated selection).

4. METHODOLOGY

According to questionnaire design, from the empirical perspective, is found a probabilistic functional dependency between the questions outlined above, which in our case we have treated as dependent variables, and business characteristics, which we treat as variables independent.

Considering the answers of respondents and characteristics of businesses, which had not quantitative but qualitative values, then to find out the functional dependency, is used multiple regression with additional variables (dummy variables)\(^{132}\).

Also, considering the responses of the interviewers into five levels, with quality characteristics, of which we have coded with discrete values listed (ordered) then is used ordered logit model and ordered probit, models which have helped us calculation of regression parameters through Stata software, and depending on the relevant parameters significance we have provided comments on the achieved results. Once ordered logit and ordered probit give approximately the same results and differ only in the distribution at the edges, then we used both models, which means that regardless of which of them is taken, we will have the same results.

5. DATA ANALYSIS

As dependent variables are taken questions from a questionnaire designed for this purpose, which is marked by \(Y_i\), where \(i=1,2\)\(^{133}\), while with \(X_i\), where \(i=1,2,3,...,7\)\(^{134}\) we present the independent variables, where the independent variables are discrete variables.

5.1. Results

In this paper we analyzed the probability functional dependence between the level of accounting regulations in Kosovo and businesses by size and sector that they belong. Functional dependency between dependent and independent variables\(^{135}\), which means that we take enterprises by size and sectors that they belong to, where \(X_1 = \) small enterprise, \(X_2 = \) medium enterprise, \(X_3 = \) large enterprise (taken as a basis), \(X_4 = \) commercial enterprises, \(X_5 = \) service enterprises, \(X_6 = \) manufacturing enterprises, \(X_7 = \) financial enterprises that are taken into account.

In this case, using ordered logit and probit model, we have the following results:

| \(Y_1\) | \(L\) | \(-0.0951596\) | \((0.3039107)\) | \(-0.4256368\) | \((0.3203218)\) | \(0.0388386\) | \((0.377252)\) | \(0.4715763\) | \((0.6981015)\) | \(0.6406466\) | \((0.6336841)\) | \(Nr. obs = 278\) | \(LRchi2(5)=3.66\) | \(Prob>chi2=0.59\) | \(Pseu R2=0.0055\) |
| \(Y_1\) | \(P\) | \(-0.0389746\) | \((0.1756939)\) | \(-0.2352295\) | \((0.1867034)\) | \(0.0276433\) | \((0.2272769)\) | \(0.2639781\) | \((0.379527)\) | \(0.4567166\) | \((0.3623394)\) | \(Nr. obs = 278\) | \(LRchi2(5)=4.22\) | \(Prob>chi2=0.51\) | \(Pseu R2=0.0064\) |


\(^{133}\) \(Y_i = \) How do you see the current developments in the field of accounting regulation?

\(^{134}\) \(X_1...X_7 = \) Businesses by size and sectors that they belong.

\(^{135}\) With ***, **, *, we present significance from 1%, 5%, 10% respectively, meanwhile the standard deviations of the parameters are shown in brackets.
In this case, it is analyzed the probability of independent variable significance taken all together, to the dependent variables.

6. CONCLUSION

New phenomena arise frequently, so it is an imperative to develop accounting in accordance with these developments, in order to present economic events accurately and faithfully.

Effective accounting would help in the process of growth and development of businesses, and one of the main objectives of Law on Accounting, Financial Reporting and Auditing is to increase the quality of financial reporting in Kosovo.

Businesses should prepare financial statements for general purposes by applying accounting standard, regulations and administrative guidelines issued by KFRC, or may prepare financial statements in full compliance with international financial reporting standards (IFRS) by notifying the KFRC.

Implementation of standards should be implemented in its entirety, to achieve the high level of reliability. Increasing the size of enterprises, enhances the reliability of accounting information in their financial statements.

So, with increasing the opportunity for these enterprises to apply international accounting standards in their financial reporting will increase the reliability that contain those reports.

Regarding the business environment and current accounting regulations, in the question: how do you see the current developments in the field of accounting regulations, the results were: 66% see current developments in the field of accounting as good and very good, and necessary, while 20% of them think that such developments are not sufficient at present, so it should work even more in the future to implement the entirety of these regulations.

In this paper we analyzed the probability functional dependence between the level of accounting regulations in Kosovo and businesses by size and sector that they belong.

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14. www.IOSCO.org;
THE IMPACT OF CORPORATE GOVERNANCE ON BANKS PERFORMANCE AND LOAN QUALITY: EVIDENCE FROM ITALIAN CO-OPERATIVE BANKS

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ABSTRACT
In the banking system, a context characterized by growing instability and by the speed of evolution of business dynamics, the system of corporate governance plays a key role, both for large banks and for banks with a smaller size.
The paper aims to investigate the influence of corporate governance of the banks that operate in the cooperative credit system on performance and quality of loans, over the years 2010-2012.
The analysis is conducted on a sample composed of 48 Italian banks, divided into 24 cooperative banks and 24 popular banks. The sample is made up of banks from all over Italy and very different in terms of dimension. The methodology of analysis is based on multivariate OLS regressions.
The main results refer to the presence of significant relationships between board dimension and the quality of loans, and among the number of committees and performance and the quality of loans.
The presence of a significant and negative relationship between the board dimension and the ratio of impaired loans to gross loans, indicates the possibility that enlargement of board dimension allows a better quality of loans.
The presence of a positive relationship between the number of committees and the ratio of impaired loans to gross loans signals the possibility that a greater number of committees can produce a worse quality of loans. The presence of a negative relationship between the number of committees and bank performance suggests to limit and manage the complexity of governance in banks operating in the cooperative credit system.
Keywords: bank, corporate governance, performance.

136 This paper is the result of a joint effort and a continuous exchange of ideas between the three authors. The individual parts are attributed as follows: Candida Bussoli has written paragraph 1 and 4, Marisa Gigante has written paragraphs 2.1 and 3.3, Maria Bruna Tritto has written paragraphs 2.2, 3.1, 3.2.
1. INTRODUCTION
In the Italian banking system, Cooperative Credit System has become increasingly important, and in spite of the dramatic recession, it has been particularly strong. This is mainly due to its structure, historically characterized by the prevalence of credit intermediation in favor of families and enterprises, by strong local roots and a balance-sheet structure which is broadly balanced. Co-operative banks and popular banks have small propensity to take risky choices thanks to their proximity to customers/members and the effective understanding of their needs and creditworthiness. The mentioned aspects represent strong points for banks operating in the cooperative credit system, but these banks are also characterized by weak points, such as a limited number of options in raising capital and a complex governance model, exposed to unstable conditions, that can also affect negatively the performance and the efficiency of banks (Fonteyne, 2007; Mottura, 2011).

The literature on the relationship between corporate governance and performance has produced mixed results, often discordant, but feeds a growing debate regarding the importance of corporate governance to achieve conditions of sound and prudent management and overall performance.


The paper aims to investigate the impact of the dimension and structure of the board, that characterize institutions working in the field of cooperative credit, on the functions carried out by the Board of Directors and, consequently, on bank performance and on the quality of its credits.

The analysis is conducted on a sample composed of 48 Italian banks, divided into 24 cooperative banks and 24 popular banks. The sample consists of banks located throughout the country in order to represent the likely cooperative credit system in Italy.

The main results show a significant and negative relationship between board dimension and loans quality, a significant and positive relationship between the number of committees and the ratio of impaired loans to gross loans, and a negative relationship between the number of committees and performance. These results suggest to limit and to manage the complexity of governance in banks operating in the cooperative credit system.

Furthermore, these results highlight how committees, which can undoubtedly offer support and assistance to the Board, make the governance structure more complex and this can adversely affect performance and credit quality.

The paper is composed as follows: section 2 is devoted to a brief review of literature on the topic, in particular it deals with the contributions focused on the relationship between corporate governance and performance in financial and non-financial companies (2.1) and in banks (2.2). Section 3 shows the empirical analysis in terms of methodology (3.1), sample (3.2) and main results from the analysis (3.3). Last section summarizes some brief conclusions.

2. REVIEW OF LITERATURE AND RESEARCH HYPOTHESIS
The literature examined on the issue of governance is oriented towards two lines of development: the relationship between corporate governance and performance in financial and non-financial companies and the impact of corporate governance on banks performance.
2.1. The Impact of Corporate Governance on the financial and non-financial companies performance

Considering the literature related to the relationship between corporate governance and companies' performance Jensen and Meckling (1976, pp.359-360), focused on the relationship between top management and owners, whether shareholders or creditors of the organization. The authors conclude that decreasing the interest of ownership of managers, the incentive to maximize their business performance reduces and thus the value of the company. Therefore, good corporate governance could have a positive relationship with the corporate performance when the property is dispersed.

With particular reference to the composition of the board, some scholars have attempted to assess the contribution of independent directors. Baysinger and Butler (1985, pp. 101-124) detect the presence of best performances in companies whose board includes a higher number of independent directors, unlike Yermack (1996, pp. 40-185-211) who, however, assert the presence of negative relationship between the proportion of independent directors and company's performance.

As part of the works referred to the importance of board dimension, Jensen (1993, pp. 831-880), Lipton and Lorsch (1992, pp. 59-77) have argued that higher board dimensions corresponds to the overall reduced corporate performance. The reasons underlying this hypothesis are essentially attributable to the fact that when the board dimensions are too high, board’s tasks become rather symbolic and dissociated from managerial processes.

Yermack (1996, pp. 40-185-211) tested the effect of board dimension on performance and management efficiency. The main hypothesis of this work is that board dimension represents an important determinant of the performance of companies and the results refer to the existence of an inverse relationship between the board dimension and enterprise value.

In support of this thesis, Eisenberg (1998, pp. 35-54) have identified a negative correlation between board dimension and company's performance, represented by Tobin's Q.

Hermalin and Weisbach (2003, pp. 7-26) confirm these results, claiming that the consensus of the literature is geared to support the hypothesis that a wider board compromises the performance of the company.

In contrast to these results, other authors argue that the increased board dimension can be beneficial, as it can increase the skills and the resources available to the organization (Dalton et al. 1999, pp. 674-686).

In order to verify the impact of corporate governance on performance, many authors have focused on the organizational characteristics of the Board, that is, on the presence of committees and on the frequency of meetings, as these factors can affect the quality of governance and corporate performance. Regarding the presence of committees, it seems to have a positive effect on corporate performance; this can be explained by referring to the complexity of tasks, whose growth requires the creation of organizational structures increasingly articulated. In support of this evidence, Klein’s theoretical contribution (1998) examined the effect arising from the existence of the committees on performance and indicated as the latter is positively related to their presence and to that of independent directors who hold executive positions within them.

Regarding the frequency and operative methods of board meetings, Carretta (2011) stated that increasing the frequency of the meetings, the possibility of control on the top management could grow. The frequency of the meetings cannot be a synonym of the efficiency of the Board of directors if participation of directors is low, if the information system for the Board is inadequate and if their carrying out does not allow to achieve shared results. Vafeas (1999, pp. 113-142) argued that the frequency of meetings of the Board is negatively related to performance, consequently, more frequent meetings of the Board result in worse performance.
The issue of board diversity has been investigated only marginally and literature has come to different conclusions about the impact of the presence of female directors on performance. Schwizer et. al (2012, pp.24-36), have studied the impact of board diversity on the number of meetings held by the Board. Regarding the presence of independent women in the Board, the results of the investigation point out a direct and significant relationship with the number of annual meetings held by the Board. Therefore, the Board of directors tends to meet more frequently if they are composed of independent women.

2.2. The Impact of Corporate Governance on banks performance

On the second line of research that examines the impact of corporate governance on banks performance, literature leads to mixed results (Bussoli, 2012). Considering board dimension, Adams and Mehran (2003, pp. 123-142) noted that the banking companies have wider Boards than industrial firms, due to the complex organizational structure and, subsequently, they examined the relationship between the board dimension of banks and their performance, approximated by a measure of Tobin's Q. In contrast to the evidence noted for non-financial companies, they show a positive relationship between the board dimension and Tobin's Q measure. Belkir (2009, pp. 201-221) has led to a positive relationship between board dimension and performance in a sample of banks and financial companies. The analysis shows that this relationship may depend on the positive effects of an expansion of banks board dimension in response to the increase in size of the same, as a external growth resulting from Mergers & Acquisitions operations. Finally, several authors have found, in contrast to the literature, that board dimension has no effect on banks performance. More precisely, Mayur and Saravanan (2006, pp. 1-17) analyzed the impact of corporate governance on banks performance, measured by Tobin's Q and by the Market to Book ratio. The results of the work have shown the absence of a dependency relationship between bank performance and board dimension. These results are interesting as made in a context in which the system of corporate governance is evolving.

A further aspect refers to the board composition, in particular the impact of the presence of female directors on the boards of the banks. According to Adams and Ferreira (2009, pp. 291-309), the Boards of directors are more effective when they can have a larger number of talented individuals and, in particular, women have a different approach than men, they have greater ease in managing relationships, having diversified personal profiles (Fields and Keys, 2003, pp. 1-24). However, according to Eisenhardt (1998, pp. 35-54), increasing of gender differentiation could lead to the reduction of harmony within the “team” of directors, since it can affect the confidence among members of different genders and their willingness to cooperate. This would result in the need to replace the whole trust with alternative mechanisms of coordination of behaviors and decisions, with an increase of organizational costs. Sufficient empirical evidence still lack, however, it can be argued that the evolution of the board role requires, especially in banks, in the light of the renewed framework of the system of internal and external controls, a greater diversity of skills and behavior of its members in any case. For this reason, a greater presence of women in the Board could quickly lead to a general improvement in the overall quality of the organization and of functioning of the Board. The reference literature, especially internationally, is wide, but it comes to mixed results and feeds a growing debate regarding the importance of governance to achieve conditions of sound and prudent management and overall performance (Bussoli, 2013, pp. 28-41). Therefore, the present work aims to investigate, in the cooperative credit system, the influence of board dimension and board structure on performance and credit quality.
In order to achieve this aim, the following research hypotheses have been formulated:

Hp1: there is a statistically significant relationship between the size and the structure of the Board and banks performance operating in the cooperative credit system;
Hp2: there is a statistically significant relationship between the size and structure of the Board and the credit quality of banks operating in the cooperative credit system.

3. EMPIRICAL ANALYSIS
3.1. Methodology
In order to test the research hypotheses multivariate OLS regression models have been used. The first and second model allow to verify the first research hypothesis: the dependent variable is represented by performance measures such as Roaa and Roae. The third model allows to verify the second research hypothesis: the dependent variable is the ratio of impaired loans to gross loans.

\[ Roaa = \beta_0 + \beta_1Lbdim_i + \beta_2Wom_i + \beta_3Lcn_i + \beta_4Tcr_i + \beta_5Ldim_i + \beta_6Gtl_i + \varepsilon_i \]
\[ Roae = \beta_0 + \beta_1Lbdim_i + \beta_2Wom_i + \beta_3Lcn_i + \beta_4Tcr_i + \beta_5Ldim_i + \beta_6Gtl_i + \varepsilon_i \]
\[ Credet = \beta_0 + \beta_1Lbdim_i + \beta_2Wom_i + \beta_3Lcn_i + \beta_4Tcr_i + \beta_5Ldim_i + \beta_6Gtl_i + \varepsilon_i \]

The dependent variables considered for the years 2010, 2011 and 2012 are:
- Roaa: Return on Average Assets, expresses the efficiency with which the bank uses its assets to generate income, and it is calculated as the ratio between net income and the average value of total assets in the financial year; data collected from the database Bankscope;
- Roae: Return on average equity, is the rate of return on equity, calculated as the ratio between net income and average value of the equity in the financial year; data collected from the database Bankscope;
- Credet: indicates the quality of the loans of the bank and is calculated as the ratio of impaired loans to gross loans; data collected from the database Bankscope.

The examined independent variables for the years 2009, 2010 and 2011 are as follows:
- Lbdim_i: board dimension, expressed in natural logarithm of the number of board members; data collected from the balance sheet and websites of banks;
- Wom_i: percentage of the female directors, measured by the ratio between the number of women in the Board and the total number of board members; data collected from the balance sheet and websites of banks;
- Lcn_i: number of committees set up in the banks expressed in natural logarithm and extrapolated from the data of balance sheet;

The control variables examined for the years 2009, 2010 and 2011 are as follows:
- Ldim_i: bank size, measured by the natural logarithm of total assets, based on the data of balance sheet;
- Tcr_i: total capital ratio, indicates the capital adequacy ratio according to Basel rules, as provided by the database Bankscope;
- Gtl_i: growth of gross loans extracted from the database Bankscope.

The dependent variables are related to the years 2010-2011-2012, while the independent variables refer to the years 2009-2010-2011; so, the analysis explores the existence of a statistically significant relationship between dependent variables whose measures are subsequent to the measures of independent and control variables, in order to reduce potential endogeneity problems.

3.2. Sample
The analysis has been conducted on a sample of 48 Italian banks, divided into 24 cooperative banks and 24 popular banks, distributed evenly throughout the country and considered in the three years 2010-2011-2012. In particular, the sample is composed of an equal number of
cooperative banks and popular banks, in order to represent likely the cooperative credit system in Italy. The analysis refers to the years 2010, 2011 and 2012, but for the construction of delayed variables, the series also includes the year 2009. For the sample construction, data relative to governance of banks were collected from the balance sheets and websites in the period from June to August 2014. Financial-economic data were collected from the "Financial Statements" and from database "Bankscope".

3.3. The Impact of Corporate Governance on banks performance: main results of the analysis

The results of the empirical analysis are illustrated, taking into account the results of the regression models. Regarding the verification of the research hypotheses, the analysis was conducted by performing multivariate OLS regressions in periods 2010-2011-2012. The OLS models are supported by the results of the analysis of collinearity and heteroskedasticity. The result of collinearity tests allows to exclude problems of collinearity among the variables. The White-tests allows to exclude problems of heteroskedasticity. However, in all years under observation, robust standard errors analyses were carried out for a better quality of the results. The table 1 shows the results of the analysis related to 2010, taking into account the Roaa dependent variable. The analysis was repeated for the Roae performance index (table 2). The models do not have a statistical significance. The results underline the influence of both the number of committees within the banks and the board dimension on Roae. In particular, a greater number of committees leads to a deterioration of bank performance, while widening the board dimension there is an improvement of the return on equity.

From this study, it can be argued that the first research hypothesis is not verified for both Roaa and Roae dependent variables in 2010.

Table 1: OLS Model-Regression-Roaa (2010)  

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Std. coeff.</th>
<th>t-statistic</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>-1.2341</td>
<td>-1.564</td>
<td>0.128</td>
</tr>
<tr>
<td>Ldbrm</td>
<td>0.2826</td>
<td>0.911</td>
<td>0.369</td>
</tr>
<tr>
<td>Worn</td>
<td>-0.3543</td>
<td>-0.481</td>
<td>0.633</td>
</tr>
<tr>
<td>Lcn</td>
<td>-0.1411</td>
<td>-1.344</td>
<td>0.189</td>
</tr>
<tr>
<td>Tor</td>
<td>-0.0080</td>
<td>-0.656</td>
<td>0.517</td>
</tr>
<tr>
<td>Ldbr</td>
<td>0.0847</td>
<td>0.132</td>
<td>0.266</td>
</tr>
<tr>
<td>Gli</td>
<td>0.0003</td>
<td>0.155</td>
<td>0.877</td>
</tr>
</tbody>
</table>

R² = 0.168313  
F(6,29) = 0.876970  
White test = 31.945976

P-value (F) = 0.523840  
P-value (F) = 0.234691

Level of Significance *10%; **5%; ***1%

Table 2: OLS Model-Regression-Roae (2010)  

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Std. coeff.</th>
<th>t-statistic</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>13.9459</td>
<td>2.229</td>
<td>0.033</td>
</tr>
<tr>
<td>Ldbrm</td>
<td>3.9009</td>
<td>2.093</td>
<td>0.050</td>
</tr>
<tr>
<td>Worn</td>
<td>-6.4124</td>
<td>-1.080</td>
<td>0.289</td>
</tr>
<tr>
<td>Lcn</td>
<td>-1.4752</td>
<td>-1.917</td>
<td>0.066</td>
</tr>
<tr>
<td>Tor</td>
<td>0.1198</td>
<td>-1.407</td>
<td>0.170</td>
</tr>
<tr>
<td>Ldbr</td>
<td>0.7832</td>
<td>1.456</td>
<td>0.156</td>
</tr>
<tr>
<td>Gli</td>
<td>0.1560</td>
<td>0.401</td>
<td>0.891</td>
</tr>
</tbody>
</table>

R² = 0.260029  
F(6,29) = 1.992562  
White test = 27.066936

P-value (F) = 0.113590  
P-value (F) = 0.469193

Level of Significance *10%; **5%; ***1%

Considering the Credet dependent variable, the model referred to the year 2010 presents a significant p-value and a value of R-square equal to 0.269. The governance variable with a greater impact on credit quality is the number of committees (Lcn), while a lower incidence is found for the total capital ratio (Tcr), expression of the capital adequacy ratio. Therefore, for the year 2010, it can be stated that the second research hypothesis is verified for the Credet dependent variable.

In 2011, the regression models relating to performance measures are statistically significant, and the value of R-square is good, as the studied independent variables explain respectively 48.2% of the Roaa dependent variance, and 53.8% of the Roae dependent variance.
These indices present a negative and significant relationship only with the total capital ratio, explaining how the increase in the capital adequacy ratio causes a reduction of the cooperative banks performance. From the obtained results, it can be asserted that the first research hypothesis is not verified for both Roaa and Roae dependent variables, for the year 2011.

Table 6 shows the results of the regression analysis conducted for the dependent variable, relative to the quality of the loans (Credet), highlighting the goodness of the model ($R^2 = 0.30$) and a significant $p$-value. The analysis illustrates that loans quality is influenced mainly by the number of committees set up in each bank (Lcn), as well as by bank size (Ldim) and the capital adequacy ratio (Tcr). The relationship between loans quality and the number of committees is positive, thus increasing the number of committees implies the increasing of impaired loans to gross loans. In smaller banks, as co-operative banks and small popular banks, where there is not complexity of the tasks, the presence of a greater number of committees can make the banking activity more difficult because of the greater complexity of the structure of governance, and it may be counterproductive if it is not commensurate to the effective management complexity. The relationship between loan quality and bank size, measured by the natural logarithm of total assets, is negative, then a variation of the latter generates an improvement of loan quality. The results suggest that, in the context of cooperative credit, greater banks may show greater capacity of assessment and selection of loans. Finally, a positive relationship with the total capital ratio implies that an increase in capital adequacy ratio generates a deterioration in loan quality. For the year 2011, these results show that the second research hypothesis is verified for the Credet dependent variable.
The analysis of regression models observed in 2012 outlines a good value of R square for both models, relating to Roaa and Roae dependent variables, as the independent variables explain respectively 36.9% of the Roaa dependent variance and 33.6% of the Roae dependent variance. Both models have a significant p-value. In 2012, the variable that has a greater impact on the performance variables is the size of the bank, which is expressed by the natural logarithm of total assets. The results underline a negative and significant relationship with the two indices Roae and Roaa. For both models, the relationship between the performance indices and the governance variable, relative to the number of committees set up in the banks, is negative; therefore, the presence of greater number of committees in a cooperative or popular bank reduces the bank performance.

The first research hypothesis is therefore verified.

Considering the analysis conducted on loans quality for the year 2012, it is possible to note that the dependent variable (Credet), measured by the ratio of impaired loans to gross loans, is influenced by the number of committees and the board dimension. As regards the number of committees, the relation with the dependent variable is positive, that is, increasing Lcn the loan quality worsens. As it has already been noted in the regression model referring to the years 2011-2010, in smaller banks there is not complexity of the tasks and the presence of a greater number of committees can make more difficult the banking activity. The relationship between loan quality and board dimension is negative and significant, thus increasing the number of directors in the Board allows to improve the credit quality.

As argued in the literature, a large board can make the management of the bank more efficient and effective, as the skills and resources available to the organization increase.
However, a large number of board members may cause a deterioration of decision-making and a lack of responsibility of the directors. The analysis conducted with the regression model relative to loans quality of the examined banks suggests that the second research hypothesis is verified in the year 2012.

Table 9: OLS Model-Regression -Credet (2012)

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Std. coeff</th>
<th>t-statistic</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>43,0375</td>
<td>2.724</td>
<td>0.010</td>
</tr>
<tr>
<td>Lbrm</td>
<td>-6,8712</td>
<td>-1.854</td>
<td>0.072</td>
</tr>
<tr>
<td>Wm</td>
<td>2,4209</td>
<td>0.369</td>
<td>0.714</td>
</tr>
<tr>
<td>Lcn</td>
<td>3,0130</td>
<td>2.742</td>
<td>0.009</td>
</tr>
<tr>
<td>Tcr</td>
<td>-0.0348</td>
<td>-0.218</td>
<td>0.828</td>
</tr>
<tr>
<td>Ldfr</td>
<td>-1,1825</td>
<td>-1.546</td>
<td>0.187</td>
</tr>
<tr>
<td>Off</td>
<td>0,0107</td>
<td>1.300</td>
<td>0.201</td>
</tr>
<tr>
<td>R²</td>
<td>0,198600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>F(6,35)</td>
<td>1,870347</td>
<td>P-value (F)</td>
<td>0.113643</td>
</tr>
<tr>
<td>White test</td>
<td>33,790638</td>
<td>P-value(w2)</td>
<td>0.172221</td>
</tr>
</tbody>
</table>

Level of Significance *10%; **5%; ***1%

4. CONCLUSION

In the paper has been analyzed how the governance of popular banks and cooperative banks influences the performance and quality of their loans. Two research hypotheses were formulated: the first hypothesis refers to the existence of a statistically significant relationship between the dimension and structure of the Board and banks performance; the second hypothesis refers to the possible existence of a statistically significant relationship between the dimension and structure of the Board, and the quality of the loans. The results of this work confirm the research hypotheses but not in all years under observation. The existence of a significant relationship between governance variables and performance variables is observable only for the Roae dependent variable in 2010. Instead, for the year 2012, the first research hypothesis is verified, since both performance variables have a significant relationship with the number of committees set up in banks considered in the sample.

The result highlights that the high number of committees within a credit cooperative bank or a popular bank can have negative effects on business management and its performance. In smaller and local banks, with lower complexity of tasks, the presence of a greater number of committees (therefore a more complex board) can make less efficient the development of banking activity. The conducted analysis also reveals that the second research hypothesis is verified for the year 2011. In fact, the quality of loans is affected by the Lcn governance variable, that is, the increase in the number of committees causes a deterioration of the quality of loans. For the year 2012, the second research hypothesis is verified. The ratio of impaired loans to gross loans, therefore, is influenced by board dimension and the number of committees. As noted in the previous year, the relationship between credit quality and committees number is positive, therefore also in this case, the increase in the number of committees causes a deterioration of loans quality. Instead, the relationship between the dependent variable and the board dimension is negative, indeed, a larger board causes a beneficial impact on the quality of the loans. The result is in line with part of the literature which argues that larger boards can make the management of the bank more efficient and effective, as the skills and the resources available to the organization increase (Dalton 1999, pp. 674-686; Belkhir, 2009, pp. 201-221; Adams and Mehran, 2003, pp. 123-142).

The future perspectives of this work will lead to broaden both the sample of reference and the period of observation.
LITERATURE
ORGANIZATIONAL FLEXIBILITY AND CHANGE FOR MANAGING THE BUSINESS CONTINUITY

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ABSTRACT
The contemporary tendency of any advanced business entities is predominantly aimed at establishing a model through which they would simultaneously recover from business disruptions, distortions, conjunctions, loose of public image and other manifestations of organizational crises and at the same time build-up skills and capabilities to prevent and further anticipate the potential for future mismanagement related their processes and behavior. In effecting the above objectives, a proper, consistent, integrated and standard-based managerial approach is crucial for creating the Business Continuity Management (BCM) as a continuous struggle for an integration of stability and change, flexibility and continuity, as well as stimulus that leads to harmonization of processes of external adaptation and internal integration.

Managers are increasingly attempting to measure and manage an optimal developmental path, in which the clear determination of signs of crises possesses not only external, but more intensively internal managerial implication. The importance of applying the BCM model is predominantly expresses at organizational, but also at group/team level, as well on personal managerial and non-managerial degree, aimed at increasing the organizational effectiveness and efficiency.

Keywords: Flexibility and change, Organizational resilience, Business continuity management (BCM), British Business Standard 25999

1. INTRODUCTION
The overall business intention to incorporate the model of organizational stability while planning and implementing the change models and techniques is, in fact, a managerial orientation to a modern managerial structuring of every business system, determined in our profound researches as:

- **fundamental (core) business processes and relationships** - that create new (added) business value and are focal for a thorough life cycle analyses and changes, and

- **instrumental and anticipatory business segments** - which are aimed at predicting, enabling and supporting the achieved level of business stability, analyzed with an excessive usage of standardized procedures.

Organizational resilience is often perceived as a managerial stimulus that is oppose to lean, agile and green change management action programs, predominantly owing to the necessity of increasing the organizational capacity for effective response to all unforeseen, but influential disruptions to the achieved phase of the organizational life cycle.
In this context, organizational resilience is quite frequently a popular managerial approach, owing to the fact that it encompasses opposite models compared to the lean production. For instance, lean leads to decrease in raw materials, unnecessary technology elimination, minimization of the employee scope and capacity, whereas an essential part of the organizational resilience is developing the business potential for a proper and secure return to the previous or future desired changes situation, what is an initial element in building the competitive advantage of every systemic model. Therefore, organizational changes are expected to be planned and continuous, in order to support the overall business process standardization, a managerial concept which, in return, leads to advancing the cooperation among all employees, particularly their mutual trust and respect, as integral elements of the prevalent concept of organizational culture.

2. FLEXIBILITY AND CONTINUOUS CHANGE FOR BUSINESS ADVANCEMENT
Managerial orientation for a harmonization of strategic, tactical and operational level of performing leads to simultaneous development and active usage of concepts of organizational stability, flexibility and changes. In this context, a clear clarification of forces of continuity and change (Gupta, 2010, p.41), that is at the same time inter-connected to the strategic flexibility, leads to the following determinants:

1. **Continuity Forces**
   - Customer Base
   - Infrastructure
   - Technology
   - Core Competence
   - Supply Chain and Distribution Network
   - Culture
   - Performance

2. **Change Forces**
   - Globalization
   - New Opportunities
   - Competition
   - Customer Needs
   - New Technologies
   - Mergers and Acquisitions
   - Governmental Policy

The integration of the continuity and change forces is conducted through forces that are driving the organizations’ pursuit for flexibility and continuous change (Leana & Barry, 2000, p.754), primarily determined as the following:

- **Adaptability** - external, environmental adaptation is essential in introducing an organic model of organizational structures, processes and behavior, which is fundamental base for long-term flexibility and continuous change.

- **Cost Containment** – internal, transactional model, such as outsourcing of non-core processes, downsizing the overall employee number regardless of their qualifications, skills and abilities, should be transformed into benefit oriented model,
a fact that pays dominant attention to processes and behavior that add value to the product/service,

*Impatient Capital Markets* – external pressure for risk deployment of the capital and for achieving short-term profit targets is related to worsening the conditions and availability of capital, needed especially for investment projects,

*Control* – increase in the controlling mechanisms, spots and involved individuals leads to accenting the hierarchical, centralized and non-creative procedures; on the contrary – decentralized, empowered and highly skilled employees contribute entirely to a desired business advancements,

*Competitive Advantage* – selected model of competitiveness must incorporate the demands for a sustained and stimulated change, which contributes to the potential for integrating the prior forces in the strategic documents, as well as adding significant influence to simultaneous increase of the predictability of change pathways.

By specific application of numerous parameters within the forces of continuity and change is created a *Matrix for continuity and change*, detailed on the following Figure 1:

![Continuity and Change Matrix at SCM (Gupta K.V., 2010, Vol.11, No.3, p.43)](figure1)

It is evident in the above Matrix that various combination of forces bear different type of change strategy, as well as category of individuals which are necessary for their planning and implementation.

3. **FUNDAMENTAL DETERMINATION OF BUSINESS CONTINUITY MANAGEMENT**

Regardless of the fact whether all potential threats to the enterprise are of an economic, technical, informational, environmental or other type of nature, it is important to anticipate, or
at least to manage the ongoing and future predicted ones, with a managerial model that identifies the influence of the threats to the core business processes and relationships, on one side, and to develop a methodological instruments for testing and improving the efficiency of the used techniques as remediation steps, on the other side.

The most prominent methodology that every form of organizational system is expected to follow in achieving the above goals is the Business Continuity Management (BCM), a managerial model that secures a permanent availability of all required resources for the process of adding contribution to processes that are critical for solving the on-going business disruptive tendencies.

In accordance with the Publicly Available Specification by the British Standards Institute (BSI), PAS 56, Business Continuity Management (BCM) is determined as a holistic management process that identifies potential impacts that threaten an organization and provides a framework for building resilience and the capability for an effective response that safeguards the interests of its key stake-holders, reputation, brand and value creating activities (BSI, 2006, p.1). As an integral managerial change approach, applied in times of internal or external crisis, the dominant area of applying of the BCM lies in attempting to create completely new, added value, even in periods of turbulent business environment.

In essence, Business Continuity Management model, in our profound analyses, creates a measurable and controllable instrument which is needed in ‘standardizing not only the internal, but also the external manifestation of processes and behavior’. It is widely used in majority of industrial and non-industrial sectors, but especially in the energy and water supply, infrastructure, transport and supply chain management etc.

It is important clearly to detail the areas of difference of Business Continuity Management (BCM) with the Enterprise-wide Business Continuity (EBC), in terms that the latter isn’t just about putting in place better plans so that the organization has a greater chance of withstanding the crises. It’s about understanding the business better – knowing where the risks are, what impact they might have and whether enough is being done to mitigate them (Baker, 2012, p.40).

The initial analyses while facing a certain form of business disruption or failure implies to a clear clarification of the options for recovering the existing situation, usually referring to the ones in the following Table:

<table>
<thead>
<tr>
<th>Act in times of disruption or failure</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Perform without change</td>
<td>Create an environment for ‘outside of the office’ performing</td>
</tr>
<tr>
<td>Combine machine and manual work</td>
<td>Secure permanent analyses of the products and/or services</td>
</tr>
<tr>
<td>Deliver continuous satisfaction at employees</td>
<td>Intensify the cooperation with familiar suppliers</td>
</tr>
<tr>
<td>Enable a climate for organizational resilience</td>
<td>Manage unpredicted shock and its aftermaths</td>
</tr>
</tbody>
</table>

Each of these alternatives possesses a various potential for embedding within the prevalent model of organizational culture, dominantly depending on the phase within the BCM Lifecycle, best illustrated on the following Figure 2:
The applicative importance of the above Figure relates to an understanding of the existing organizational problem – a stage that leads to the managerial capacity to distinguish influential from non-influential problems, followed by determining the BCM strategy and developing and implementing BCM response, stages that are related to creating Business Impact Analysis (BIA), as a managerial pre-condition for applying the first segment of the BCM Standard 25999. In the final phase, the implementation results are exercised, maintained and reviewed, in order to determine the deficiencies in processes and behavior, which are subject to continuous change, implying to the second segment of the standard 25999.

The very Business Impact Analysis (BIA) refers to a specific type of analytical framework which is a continuation of the risk determination, and is predominantly aimed at clearing up the influences from losing certain business resources, capabilities, structures and relationships. The key objectives of BIA (Tammineedi, 2010, p.42) are categorized as the following:

- **Determine the potential impact to the organization in the event of an outage,**

- **Identify critical services/processes and their maximum tolerable period of disruption (MTPoD), recovery time objectives (RTOs) and recovery point objectives (RPOs),**

- **Determine the sequence of recovering business functions and data in the event of an outage,** and

- **Identify recovery strategies, minimum resources and vital records that are necessary for business continuity.**

It is rather important to point out that the application of the second objective of BIA varies from sector to sector, meaning that it is not entirely useful in utility and power plants, distributive companies, as well in monopoly or duopoly type of market position of a certain company.
4. APPLICATIVE IMPORTANCE OF THE BUSINESS STANDARD 25999

As developed since the 1970’s, Business Continuity Management (BCM) is a prominent managerial response to specific forms of organizational crises, which have initially been manifested in the operations of IBM model 360 in 1965, as well as in the model 370 in 1970, in order to categorize the various modalities of crises such as interruptions, distortions, non-functionality etc. This evolutionary development approach to BCM would best be illustrated through the following Table 2:

**Table 2: The development of Business Continuity Management – Period, Drivers and Practice (Herbane, 2010, p.992)**

<table>
<thead>
<tr>
<th>Period</th>
<th>Drivers</th>
<th>Practice</th>
<th>Nature of Progress</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mid 1970s to Mid 1990s</td>
<td>Emerging legislation</td>
<td>Disaster Recovery Planning to Business Continuity Planning</td>
<td>Development</td>
</tr>
<tr>
<td>Mid 1990s to 2001</td>
<td>Emerging standards</td>
<td>Business Continuity Management (BCM)</td>
<td>Development</td>
</tr>
<tr>
<td>2002 – 2005</td>
<td>Acceleration and focus</td>
<td>BCM</td>
<td>Diffusion</td>
</tr>
<tr>
<td>2006-2010</td>
<td>Competing standards and breakout</td>
<td>BCM</td>
<td>Standardization</td>
</tr>
</tbody>
</table>

The process of entering into the standardization phase implies establishing a separate standard for BCM – the *British Business Standard (BS) 25999*. The fundamental importance of this standard lies in its potential for determining and further managing the structured and overall *business compliance*, in order to decrease the degree of unforeseen negative implications from business decisions. In this matter, the concept of compliance is not an exclusive model, but far more designed to apply to all organizations, from SME to the multi-national business, depending on the industry, size, nature and on culture of the organization (Gallagher, 2007, p.35).

Fundamentally created in November 2006 by the British Standards Institution, *BS 25999 intends to manifest itself into a European and international business continuity standard*, although the American National Standards Institute (ANSI) has undertaken immense activities to develop a separate US Business Continuity Standard. In fact, BS 25999 in itself is incorporating the following integral segments, described as:

1. *Code of Practice* – details the scope, terms, objectives, policy, guidance, terminology, recommendation etc., as a framework for implementing the standard, enabling the following, second segment,
2. Specifications – precisely stating the requirements from every BCM model to be certifiable, externally comparable and auditable, meaning that this segment of the standard tends to secure certain compliance of the performances to those stipulated in the standard.

The ultimate objective while applying the BS 25999 is to reach certain Business Continuity Competence Maturity Model, categorized in 6 levels (Tammineedi, 2010, p.48), fundamentally determined on the following approach:

- Level 1 – Self – governed
- Level 2 – Supported self – governed
- Level 3 – Centrally governed
- Level 4 – Enterprise Awakening
- Level 5 – Planned Growth
- Level 6 – Synergistic

The first three levels imply that specific organizational system hasn’t entirely yet implemented the program for business continuity, whereas the remaining three levels up to the sixth level manifest an evolutionary and partly transformational capacity for implementing this kind of change program. Higher the achieved maturity level, the more the BCM culture would be enhanced and embedded.

It is useful to clarify that one of the week applicative dimensions of the BS 25999 is its homogeneity, meaning that every company undergoing a BCM initiative must make sure that the strategy fits the ongoing interests of the company and its shareholders, is in line with the company’s risk tolerance, and is actually achievable given the amount of manpower and budget allocated for the initiative (Garcia, 2008, p.34).

5. CONCLUSION
The contemporary tendency of any advanced business entities is predominantly aimed at establishing a model through which they would simultaneously recover from business disruptions, distortions, conjunctions, loose of public image and other manifestations of organizational crises and at the same time build-up skills and capabilities to prevent and further anticipate the potential for future mismanagement related their processes and behavior. In effecting the above objectives, a proper, consistent, integrated and standard-based managerial approach is crucial for creating the Business Continuity Management (BCM) as a continuous struggle for an integration of stability and change, flexibility and continuity, as well as stimulus that leads to harmonization of processes of external adaptation and internal integration. Organizational resilience is often perceived as a managerial stimulus that is oppose to lean, agile and green change management action programs, predominantly owing to the necessity of increasing the organizational capacity for effective response to all unforeseen, but influential disruptions to the achieved phase of the organizational life cycle. The integration of the continuity and change forces is conducted through forces that are driving the organizations’ pursuit for flexibility and continuous change, primarily determined as adaptability, cost containment, impatient capital markets, control and competitive advantage.
The most prominent methodology that every form of organizational system is expected to follow in achieving the above goals is the Business Continuity Management (BCM). In accordance with the Publicly Available Specification by the British Standards Institute (BSI), PAS 56, Business Continuity Management (BCM) is determined as a holistic management process that identifies potential impacts that threaten an organization and provides a framework for building resilience and the capability for an effective response that safeguards the interests of its key stakeholders, reputation, brand and value creating activities. The applicative importance of the Business Continuity Management Lifecycle relates to an understanding of the existing organizational problem – a stage that leads to the managerial capacity to distinct influential from non-influential problems, followed by determining the BCM strategy and developing and implementing BCM response, stages that are related to creating Business Impact Analysis (BIA), as a managerial pre-condition for applying the first segment of the BCM Standard 25999 – Code of Practice. In the final phase, the implementation results are exercised, maintained and reviewed, in order to determine the deficiencies in processes and behavior, which are subject to continuous change, implying to the second segment of the standard 25999 - Specifications. Business Impact Analysis (BIA) refers to a specific type of analytical framework which is a continuation of the risk determination, and is predominantly aimed at clearing up the influences from losing certain business resources, capabilities, structures and relationships. The process of entering into the standardization phase implies establishing a separate standard for BCM – the British Business Standard (BS) 25999. In this matter, the concept of compliance is not an exclusive model, but far more designed to apply to all organizations, from SME to the multi-national business, depending on the industry, size, nature and on culture of the organization. The ultimate objective while applying the BS 25999 is to reach certain Business Continuity Competence Maturity Model, categorized in 6 levels: self-governed, supported self-governed, centrally governed, enterprise awakening, planned growth and synergistic. Higher the achieved maturity level, the more the BCM culture would be enhanced and embedded.

LITERATURE

ANALYSIS OF THE ROLE OF INSTITUTIONAL INVESTORS IN THE IMPLEMENTATION OF THE CORPORATE GOVERNANCE IN CROATIA

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ABSTRACT
In order to determine the role of institutional investors in the implementation process of corporate governance companies, which have submitted an annual survey on the Code of Corporate Governance for the year 2013, were analysed. Various data regarding investments, shares and financial information were collected from financial statements of chosen companies. An analysis of the collected data was performed in order to give insight in investors and to determine the role of institutional investors in the implementation process of corporate governance.

Keywords: institutional investors, corporate governance, Croatia

1. CORPORATE GOVERNANCE
Corporate governance (CG) is related to the modern corporation, respectively to a form of companies in which the owners are not responsible for the obligations that the company creates. At the beginning of the 20th century, the development of the modern corporation was mostly influenced by the use of the legal form of a joint stock company. Most companies were established as joint stock companies due to the possibility of financing entrepreneurial activities. Increasing the number of companies with dispersed ownership the capital market was developed. The modern corporation accelerated the economic growth, contributing to the efficient allocation of resources, creation of new products, technology development, and thus increasing productivity. The most important role of the modern corporation is creating wealth for all stakeholders (investors, employees, customers, suppliers) (Tipurić, 2008, pg. 11-13). Corporate governance framework needs to encourage efficient and transparent market. During its development, it was necessary to bear in mind how it affects the market and its participants. Legal and regulatory provisions relating to corporate governance have to be transparent and enforceable. Various state authorities clearly define the division of responsibilities. Decisions taken by the supervisory and regulatory authorities must be timely, transparent and explained in detail (OECD, 2004, pg. 12). The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have legal protection in case of violation of
their rights (OECD, 2004, pg. 15). Corporate governance framework should recognize the rights of interests groups and provide them with the necessary information. Its importance lays in the cooperation with companies, which can have a significant impact on the wealth creation (OECD, 2004, pg. 16). Corporate governance is not mandatory, although companies, which want to be successful, should adopt CG as one of the basic prerequisites for success.

2. INSTITUTIONAL INVESTORS IN CROATIA

Institutional investors own and accumulated capital invested in the securities portfolio, with the aim of risk diversification. Due to the large capital, they can influence the price movements at the capital market. Throughout the history capital markets were mostly dominated by wealthy individuals, and in the early 19th century insurers and insurance policy became significant and through it the importance of institutional investors grow. In Croatia, banks and individual investors first dominated the capital markets (Stimac, 2010). Shareholders affect the successful development of corporate governance. If shareholders have greater control of managers, managers will seek to manage the company in interest of shareholders, not in their own. However, shareholders, due to the high ownership dispersion, have a low capacity of control. For this reason, an increasingly important role have institutional investors. Opposed to individual investors, institutional investors can have a significant impact on corporate governance (Jiang, and Anandarajan, 2009). Institutional investors have available information on investments and can respond more quickly to changes on the financial market (Ciric and Njegomir, 2012).

2.1. Investment funds

Investment funds are institutional investors which, through a public offering collect funds and then with the principles of safety, profitability, liquidity and risk invest these funds in securities and real estate as well as in deposits in financial institutions (Moric et. al., 2006). An investment fund can be formed as UCITS fund or alternative investment fund. UCITS Fund is an open-end fund which funds raised by public offering invests in securities and other liquid forms of assets. Units in fund at the request of the holder can be purchased. The law governing the establishment and management of alternative investment funds determines alternative Investment Fund (Act on Open-Ended Investment Funds with a Public Offering (Official Gazette 16/13)

$Chart 1: Net assets of UCITS fund$

Source: Authors' work according to HANFA, (available 26.07.2014. on: http://www.hanfa.hr/nav/106/statistika.html)
Chart 1 shows that the net assets of UCITS funds in February 2014 decreased significantly compared to January. From March to May, net assets slightly increased, and in June, it fell again. Alternative investment fund raises funds by public or private offering in order to invest in different types of assets for the benefits of holders of alternative investment fund. Alternative Investment Fund (AIF) can be formed as an opened and as closed AIF (Alternative Investment Funds Act (Official Gazette 16/13). In the Republic of Croatia in June 2014, 78 of the UCITS funds were active, of which 21 were money market fund, 8 bond funds, 11 mixed and 30 equity funds and 8 others. There were 26 alternative investment funds of which 5 were funds with a public offering, 14 with a private offering and 7 venture capital funds (HANFA, statistics 2014).

2.2. Pension Fund

Pension funds are separate assets without legal personality, established as a special kind of funds, for the gathering of funds in the form of contribution from a pension fund members and investing those funds to increase the value of pension fund assets (Mandatory Pension Funds Act (Official Gazette 19/14).

The main purpose of the first pillar (pillar I pension fund) is the stabilization of the pension system, but it proved to be insensitive to the growth of unemployment and the slowdown of the world economy. For these reasons, all the problems of the previous pension system maintained active. Due to the increase of life expectancy, and therefore increasing the number of pension beneficiaries, on the other hand the decreasing of the birth rate, the ratio of deposits and withdrawals in the pension systems based on generation solidarity became unfavorable (Altaras Penda, 2009). The introduction of the second pillar (pillar II pension fund) as mandatory pension based on individual capitalised savings of members with the aim of investing in the capital market, wanted to create the impression of citizens' responsibility for their future retirement. However, citizens do not have a high ability to influence, only in choosing between four mandatory pension funds which have been authorized by the Croatian Agency for Supervision of Financial Services: AZ Mandatory Pension Fund, Erste Plavi mandatory pension fund, PBZ Croatia pension funds, Raiffeisen Mandatory Pension Fund (Altaras Penda, 2009).

Unlike the first and second pillar which are regulated by law, the third pillar affects the citizens themselves, and they decide which amount and when they allocate savings for their pension insurance. Thus, the funds raised by voluntary pension funds are invested in the capital market. When they want, citizens can get out of the voluntary pension fund significantly easier than from the mandatory pension fund (Altaras Penda, 2009). An additional incentive for investment in pillar III is given by the state authorities through government incentives which can amount up to 15% of the total amount paid for each member for the previous calendar year (Voluntary Pension Funds Act (Official Gazette 19/14).

Pension funds can be mandatory and voluntary. Mandatory pension funds, according to the principles of investment, may be in A, B or C category. Assumed risk is highest in the fund category A, and the lowest in the fund category C. Voluntary pension funds can be open-end and close-end. Open voluntary pension fund can enroll all individuals. In the closed pension fund, members are individuals who are employed, or are union members, members of the self-employed or self-employed persons Voluntary Pension Funds Act (Official Gazette 19/14).
Chart 2: Trends in number of pension funds in the period from 2002 to June 2014

Source: Authors research, according to HANFA, (available 26.07.2014., on: http://www.hanfa.hr/HR/nav/106/statistika.html)

Chart 2 shows trends in the number of pension funds from 2002 to June 2014. In that period, the lowest number of mandatory pension funds is present. There were 6 open-end voluntary funds from 2005 to June 2014. The number of closed-end pension fund fluctuated, and since 2013, there are 16 different closed pension funds.

Table 1: Net assets of mandatory pension funds (000 HRK)

<table>
<thead>
<tr>
<th>Name</th>
<th>May 2014.</th>
<th>June 2014.</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Amount</td>
<td>Share</td>
<td>Amount</td>
</tr>
<tr>
<td>AZ OMF</td>
<td>24.147,917</td>
<td>40,24%</td>
<td>24.680,837</td>
</tr>
<tr>
<td>Erste Plavi OMF</td>
<td>7.910,103</td>
<td>13,18%</td>
<td>8.041,992</td>
</tr>
<tr>
<td>PBZ/CO OMF</td>
<td>9.650,534</td>
<td>16,08%</td>
<td>9.889,252</td>
</tr>
<tr>
<td>Raiffeisen OMF</td>
<td>18.299,838</td>
<td>30,50%</td>
<td>18.776,039</td>
</tr>
<tr>
<td>Sum</td>
<td>60.008,392</td>
<td>100,00%</td>
<td>61.388,121</td>
</tr>
</tbody>
</table>

Source: Monthly Report (available 01.08.2014. on: www.hanfa.hr/getfile/41211/mi%2007_14.xlsx)

Table 1 shows the net assets of mandatory pension funds. It is evident that in June the total net assets of mandatory pension funds has increased compared to May. Each of the mandatory pension funds had in June greater net assets value than in May. In both months, the highest share in total net assets was occupied by the AZ fund. In May AZ fund occupied 40.24%, and
in June 40.20% of the total net assets. Erste Blue Mandatory Pension Fund occupied the smallest share of net assets in both observed months.

2.3. Commercial banks
Commercial banks in CG appear in two roles, as creditors and as shareholders of the company. In companies, where debit is dominant versus equity, commercial banks can play an important role in the implementation process of corporate governance. This is done based on the information available to them as insiders (Tipurić, 2006). According to data from the consolidated balance sheets of credit institutions the total assets in May 2014 amounted to 409,246,600,000, 00 HRK (Croatian national bank, bulletin 2014). It is interesting that from 2008 until May 2014, total assets recorded mostly growth, with exception 2012, and April and May 2014 in which a slight decline was recorded.

Through investing assets in securities, banks can achieve dividends on shares and interest on debt securities. Optimization of resources is conducted through investment in different securities that are liquid and carry minimal risk (Jurman, 2006). Saunders and Sinkey (2000, according to Jurman, 2006, p. 21) point out that an investment bank in securities does not necessarily mean an outflow of funds. If investments in securities are done, whose issuers are deposits with that bank, the funds will be retained in the system, thus strengthening the financial and credit potential of banks (Jurman, 2006). Members of the board of directors and supervisory board need to have knowledge in order to manage and supervise the companies’ business. They should be able to take decisions in the interests of banks, shareholders and other all the stakeholders. Board of directors and supervisory board have to determine business objectives, risk strategy and policies that will achieve goals of the whole company. Banks need to establish a procedure for the assessment of their internal capital to adequately identify measure and calculate the risk in order to ensure that the bank has sufficient internal capital relative to its risk profile, and to use appropriate risk management system (Croatian national bank, The views of the Croatian National Bank on Corporate Governance in Banking, 2007). A bank without a good corporate governance cannot affect changes in CG in companies in which it holds stakes. This stems from the fact that it cannot affect change in a particular company if the company does not know how to affect change in its own business.

2.4. Insurance companies
The insurance company is company licensed by the Croatian Agency for Supervision of Financial Services to conduct insurance activities of the. Insurance activities mean the conclusion and fulfilment of the contract of non-life and life insurance and reinsurance (Insurance Act (Official Gazette 151/05). Insurance companies have an important role in the development of economic and financial system where they enable all participants’ sustainable business and savings in a stable environment. In addition to the function of insurance and compensation of damage, insurance companies have an important role in gathering financial resources and their allocation and investment, thus affecting the development of the economy (Croatian Insurance Bureau, 2010). Insurance companies are important investors in the country and the economy on the financial markets. Their total assets amounted to 34.6 billion, largely invested in bonds (Croatian Insurance Bureau, 2014).

3. DATA COLLECTION, METHODOLOGY AND RESEARCH RESULTS
Research on the role of institutional investors in the implementation process of CG was conducted using data from the annual financial statements of those companies which have submitted an annual survey on the Code of Corporate Governance for the year 2013. The sample consisted of 130 companies. For all companies in the annual financial reports the
shares of investment funds, pension funds, commercial banks and insurance companies in the share capital as at December, 31 2013 were analysed. Shares of each of the institutional investors are expressed in absolute terms. Based on the collected data presents the analysis in the statistical tool R Commander.

Summary (Companies)

<table>
<thead>
<tr>
<th>Corporate Governance</th>
<th>Investment Funds</th>
<th>Pension Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Min. :1</td>
<td>Min. :0.00000</td>
<td>Min. :0.00000</td>
</tr>
<tr>
<td>1st Qu.:1</td>
<td>1st Qu.:0.00000</td>
<td>1st Qu.:0.00000</td>
</tr>
<tr>
<td>Median :1</td>
<td>Median :0.00000</td>
<td>Median :0.00000</td>
</tr>
<tr>
<td>Mean :1</td>
<td>Mean :0.02729</td>
<td>Mean :0.01808</td>
</tr>
<tr>
<td>3rd Qu.:1</td>
<td>3rd Qu.:0.00000</td>
<td>3rd Qu.:0.00000</td>
</tr>
<tr>
<td>Max. :1</td>
<td>Max. :0.80000</td>
<td>Max. :0.41050</td>
</tr>
</tbody>
</table>

Corporate governance results are based 1, because for the sample, companies’ annual questionnaire on the Code of Corporate Governance was used. In addition, because of the calculation in the R Commander all variables must be quantitatively expressed. In this case, to all CG variables a value of 1 is assigned because all companies submitted the annual questionnaire on the Code of Corporate Governance. The minimum share of investment funds in the selected companies is 0% and the maximum is 80%. The minimum share of pension funds is 0%, and the maximum 41.05%. The minimum share of commercial banks is 0%, and the maximum 84.47%. The minimum share of insurance companies is 0%, and the maximum share of 56.34%.

Chart 4.1: The frequencies histogram for investment funds
The chart 4.1 presents the frequency histogram for investment funds. It can be observed that in most companies, mutual funds have a 10% share of the total share capital. The shares of investment funds in the total share capital of the company in range of 60-80% can be considered unusual values (outliers), because none of the investment funds have 30 to 60% shares in companies.

*Chart 4.2: The frequencies histogram for pension funds*

The chart 4.2 shows the frequency histogram for pension funds. Most pension funds have up to 5% of the total share capital in companies, followed by 5-10%, and 10-15%. In the small number of companies, pension funds have from 25% to 45% of the total share capital.

*Chart 4.3: The frequencies histogram for commercial banks*

The chart 4.3 shows the frequency histogram for commercial banks. It can be observed that in most companies the commercial banks occupied up to 15% of the total share capital, then 15-20%, and 20-25%. Hence, there is not a single commercial banks which occupied 45-80% of the total share capital.
The chart 4.4 shows the frequency histogram for insurance companies. It presents that in most companies insurance companies had up to 5% of the total share capital. Equal number of companies had from 5 up to 15% of insurance companies in the total share capital. There are not companies in which insurance companies take up 20-45% of total equity. Therefore, the share of insurance companies in the range 45-50% and 55-60% of the total share capital may be considered as unusual. From the above presented histograms can be concluded that in most of the observed companies institutional investors take up to 5% (pension funds and insurance companies) or 10% (mutual funds and commercial banks) of total share capital. This paper seeks to identify the role of institutional investors in the implementation of corporate governance; multiple regression was implode for this reason.

Terms of linear model of the basic set is (Sosic, 2006):
\[ y_i = \alpha + \beta_1 x_{i1} + \beta_2 x_{i2} + \ldots + \beta_j x_{ij} + \ldots + \beta_K x_{ik} + e_i, \ i = 1, 2, \ldots, n \]

In this model, \( y_i \) is the value of dependent variable, and \( x_{ij} \) are independent variables. Table 2 below shows residuals and coefficients.
Table 2: Residual and coefficients results

**Residuals:**
- Min: $-1.128 \times 10^{-15}$
- 1Q: $8.070 \times 10^{-18}$
- Median: $1.058 \times 10^{-17}$
- 3Q: $1.084 \times 10^{-17}$
- Max: $1.084 \times 10^{-17}$

**Coefficients:**

|                     | Estimate | Std. Error |   t value | Pr(>|t|) |
|---------------------|----------|------------|-----------|----------|
| (Intercept)         | 1.000e+00| 1.031e-17 | 9.694e+16| <2e-16 ***|
| Investment funds    | 4.934e-18| 7.919e-17 | 6.200e-02| 0.950    |
| Pension funds       | 2.683e-17| 1.320e-16 | 2.030e-01| 0.839    |
| Commercial banks    | 2.565e-17| 8.428e-17 | 3.040e-01| 0.761    |
| Insurance companies | 1.596e-17| 1.231e-16 | 1.300e-01| 0.897    |

Signif. codes:  0 ‘***’ 0.001 ‘**’ 0.01 ‘*’ 0.05 ‘.’ 0.1 ‘ ’ 1

Residual standard error: 1.014e-16 on 125 degrees of freedom
Multiple R-squared: 0.4897, Adjusted R-squared: 0.4734
F-statistic: 29.99 on 4 and 125 DF, p-value: < 2.2e-16

*Source: Authors research*

A conducted multiple regression, regression equation for the dependent variable corporate governance is as follows:

Corporate governance = $1.000e + 00 + 4.934e - 18 x_1 + 2.683e - 17 x_2 + 2.565e -17 x_3 + 1.596e -17 x_4$

In absolute values:

Corporate governance = $1.00000 + 4.934 \times 10^{-18} x_1 + 2.683 \times 10^{-18} x_2 + 2.565 \times 10^{-18} x_3 + 1.596 \times 10^{-18} x_4$

Where $x_1$ are investment funds shares, $x_2$ pension funds shares, $x_3$ and commercial banks shares and $x_4$ are insurance companies shares. The regression coefficient with $x_1$ can be interpreted as follows: Raising the share of investment funds for a 1, while the shares of pension funds, commercial banks and insurance companies remain unchanged, the quality of corporate governance will be in average increase for $4.934 \times 10^{-18}$. The regression coefficient with $x_2$ can be interpreted as follows: Raising the share of pension funds for a 1, and shares of investment funds, commercial banks and insurance companies remain unchanged, the quality of corporate governance will be in average increase for $2.683 \times 10^{-18}$. The regression coefficient with $x_3$ can be interpreted as follows: Raising the share of commercial banks for a 1, and shares of investment funds, pension funds and insurance companies remain unchanged, the quality of corporate governance will be in average increase for $2.565 \times 10^{-18}$. The regression coefficient with $x_4$ can be interpreted as follows: Raising the share of insurance companies for a 1, and shares of investment funds, pension funds and commercial banks remain unchanged, the quality of corporate governance will be an average increase for $1.596 \times 10^{-18}$. Based on the regression coefficients it can be concluded that the most important role in corporate
governance play the pension funds, followed by commercial banks, then insurance companies and mutual funds.

4. CONCLUSION
Institutional investors recently became important participants at the organized capital market. Corporate governance defines the relationships between managers and other stakeholders’. The establishment of good corporate governance is important due to the separation of ownership from control of the company. The existence of privatization investment funds did not promote the improvement of corporate governance because of high management costs and inability determine the net asset value. Institutional investors are becoming more important in the implementation process of corporate governance. Because of investing in more securities institutional investors can lower the risk of their portfolio through diversification. For the analysing of the role of institutional investors in the implementation process of corporate governance in Croatia the multiple regression was used. According to the regression coefficients, the biggest role have pension funds, followed by commercial banks, then insurance companies and mutual funds.

LITERATURE
13. HANFA, available 02.08.2014. on: http://www.hanfa.hr/registar/27/
15. HANFA, available 24.08.2014. on http://www.hanfa.hr/registar/16/drustva-za-osiguranje-i-reosiguranje?
THE IMPACT OF INTANGIBLE ASSETS ON FINANCIAL PERFORMANCE OF CROATIAN COMPANIES

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ABSTRACT
Intangible assets are identified as important factor which can significantly contribute to financial position and profitability of a company. Recently, importance of intangible assets is considerably increasing what is indicated by higher investments that companies make in this component of non-current assets. The main objective of this paper is to identify relationship between investment in intangible assets represented by intangible assets to total assets ratio and financial performance of companies represented by various financial ratios. Also, relationship between investment in intangible assets and bankruptcy status will be determined. Mainly, profitability ratios as Return on Assets, Return on Equity, Net Profit Margin, Gross Profit Margin etc. are used as measures of financial performance. The empirical findings are based on sample which consists of companies that operated in Republic of Croatia. Financial information was obtained from annual financial statements which are publicly available on Croatian Financial Agency website. The sample comprises of two groups. First group consists of companies which opened a bankruptcy proceeding and second group consists of companies which haven't opened a bankruptcy proceeding. Information about bankruptcy status was obtained from Croatian Official Gazette website. The companies included in sample are classified in two activities - manufacturing industry and wholesale and retail industry.

Keywords: Bankruptcy, Croatia, Financial Performance, Intangible Assets

1. INTRODUCTION
Key drivers of change in modern economy are based on new possibilities which have originated from enhanced knowledge and more intensive application of different forms of technology. Alongside with these definitions there is a requirement for reorganization of economy from aspect of doing business. Relations in so-called industrial economy and modern economy also imply changes in various aspects and, among others, company's non-current resources aspect. Changes in non-current resources structure occurred in the structure of durable assets which indicates that the tangible assets have started to cede their place to the intangible assets items.
Therefore, companies were more dependant on real capital (immovables, movables) two or more decades ago, while trends in modern economy dictate higher participation of intangible assets. Accurate monitoring of changes in economic environment of a company assumes business activity adjusted to the market requirements and requirements of the capital maintenance as well as the establishment of durable assets of a company which will enable positive financial performance and business continuity.
2. BASIC DEFINITIONS

Intangible assets as business resources of a company can be analyzed from several aspects. Basic rules of their measurement and recognition are regulated by financial reporting standards. National economies have possibility of regulation system duality defined with particular national and international financial reporting standards. Republic of Croatia accepted Croatian Financial Reporting Standards and International Financial Reporting Standards.

Croatian Financial Reporting Standard 5 (NN 30/08) regulates mentioned field. Intangible assets are non-monetary assets without physical characteristics that can be identified. They comprise of following categories of assets: research and development, patents, concession rights, trademarks, software, permissions for fishing, franchises and other rights, goodwill, advance payments for purchase of intangible asset and other intangible assets. For these assets categories same definitions are applied as for the tangible assets: systematical depletion/amortisation, fair value, impairment losses.

One segment of companies in Republic of Croatia is obliged to apply International Accounting Standard 38 (IAS 38) which regulates acquisition and valuation of intangible assets. According to this standard, intangible assets usually represent broader term for software, patents, copyright, video, list of customers, lien, fishing permissions, import quotas, franchises, relationship with customers and suppliers, customer loyalty, market share and marketing rights.

According to paragraph 10 and paragraph 9, intangible assets items won't meet the definition of intangible assets, unless they fulfil these requirements: identifiability, control over a resource and future economic benefits. If some item comprised by this standard doesn't meet the definition of intangible asset, the expenditure to acquire it or generate it internally is recognised as an expense when it incurred.

The segments of their recognition of intangible assets intrigue the topic of this paper. In other words, companies have different structure of their non-current resources. Another important segment is existance and intensity of intangible assets impact on financial performance of companies. It is the result of resource controlling by the management and consequentially existance of future economic benefits and financial performance.

Great competition, macroeconomic environment, political environment, legal system, internal factors, including inadequate management, result in bankruptcy of a company. The task of the company’s management is to efficiently manage the resources of a company. It implies resource management that leads to future economic benefit which means the potential to contribute direct or indirect inflow of cash or cash equivalents (Croatian Financial Reporting Standard-1.t.1.6.). Future economic benefits through efficient management of resources can be monitored and analysed through performance ratios like Return on Assets, Return on Equity, Net Profit Margin, Gross Profit Margin.

The efficiency of conducting business policy is associated to recognition of early warning signals that a crisis occurred. In this sense, management of a company has to timely diagnose causes of a crisis, which pose a threat to its business continuity (Bubic, J. & Mijac, O.I., 2011, pp. 233-242). It is necessary to make decisions and take actions during the crisis, including activities of CMT, to determine the nature of the crisis, assess the losses, evaluate recovery options and communication with the public. If the crisis continues for a longer time, the chances for company's recovery are reduced.

Furthermore, it is important that management of a company monitors all business indicators in order to eliminate causes of crisis and works on improvements at all business levels and areas of business. Inadequate resource management, in the specific case of investment in intangible assets which is analyzed in this paper, consequentially has resulted in negative
impact on financial performance. If a company has negative financial performance for a long period of time, it leads to uncertainty of business continuity and consequentially to bankruptcy.

In situations when there is evidence about existence of at least one bankruptcy reason, the bankruptcy proceedings are opened. Bankruptcy proceedings are type of extra-contentious civil judicial processes which are conducted against debtor. Their goal is to achieve settlement for creditors by monetizing debtor’s assets and allocating collected resources to creditors (Bankruptcy law, NN 44/96, 29/99, 129/00, 123/03, 82/06, 116/10, 25/12, 133/12).

3. LITERATURE REVIEW

Majority of researches regarding intangible assets are focused on large companies which are listed on stock exchange. Some among them which investigate impact of intangible assets on company’s profitability like Tudor et al. (2014, pp. 283–293) used intangible to total assets ratio as a measure of intangible assets and Return on Assets, Return on Capital Employed and Gross Margin as measures of profitability. Li and Wang (2014, pp. 98–113) also examined this relationship, but they analysed different components of intangible assets as R&D costs, sales training etc. They also used Return on Assets as a measure of profitability. De Lima Castro and Benetti (2013) examined the relationship between non-recorded intangible assets and market value of the company. Tudor et al. (2014, pp. 283–293) mentioned findings of some other researches like Becalli (2007, pp. 2205–2230) who discovered “profitability paradox” regarding investment in IT software and services, Hidayati et al. (2012) who investigated connection between signalling to the market and market response to the level of intangibles and Megna and Muller (1991, pp. 632–642) who determined positive connection between intangibles and profitability.

4. EMPIRICAL RESULTS

4.1. Data and methodology

Financial information used in research was gathered from annual financial statements publicly available on the Croatian Financial Agency website. Information about bankruptcy status was obtained from Croatian Official Gazette website. Annual financial statements were obtained for financial year 2011 and information about bankruptcy status (bankrupted or normally continued business) was obtained for 2012. The companies included in sample belong to two activities (manufacturing industry, wholesale and retail industry) based on Croatian National Classification of Activities. Small, medium and large enterprises are included in this research and majority of them (90%) are small enterprises.

The aim of the research defines and sets the hypotheses as follows:

Hypothesis 1 – assumes the existence of relationship between intangible assets and profitability financial ratios,

Hypothesis 2 – assumes the existence of relationship between investing in intangible assets and opening bankruptcy proceeding.

The sample consists of 100 companies and it is divided in two groups. First group comprises 50 companies which opened a bankruptcy proceeding in 2012 and second group comprises 50 companies which haven't opened a bankruptcy proceeding and continued doing business normally in 2012. In this research data is statistically analyzed using correlation, linear
regression, chi-square and independent samples t-test. Statistical Package for Social Sciences (SPSS) was used for statistical analysis of data.

4.2. Results
Following financial ratios were used in statistical analysis:

**Table 1. Abbreviations for financial ratios included in research**

<table>
<thead>
<tr>
<th>Abbrev.</th>
<th>Ratio</th>
<th>Abbrev.</th>
<th>Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>IA/TA</td>
<td>Intangible Assets to Total Assets Ratio</td>
<td>ROCE</td>
<td>Return on Capital Employed</td>
</tr>
<tr>
<td>GPM</td>
<td>Gross Profit Margin</td>
<td>EBIT</td>
<td>Earnings before Interest and Taxes</td>
</tr>
<tr>
<td>NPM</td>
<td>Net Profit Margin</td>
<td>EBITDA</td>
<td>Earnings before Interest, Taxes, Depreciation and Amortization</td>
</tr>
<tr>
<td>ROE</td>
<td>Return on Equity</td>
<td>IA</td>
<td>Investment in IA (1 - invested, 0 - didn't invest)</td>
</tr>
<tr>
<td>ROA</td>
<td>Return on Assets</td>
<td>BNKR</td>
<td>Bankruptcy (1 – bankrupted, 2 – non-bankrupted)</td>
</tr>
</tbody>
</table>

Chi-square test for independence was applied to determine the relationship between bankruptcy and investment in intangible assets.

**Table 2. Chi-square crosstabulation table (Investment in intangible assets and bankruptcy status)**

<table>
<thead>
<tr>
<th>IA</th>
<th>Count</th>
<th>BNKR</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>0</td>
<td>30</td>
<td>17</td>
<td>47</td>
</tr>
<tr>
<td></td>
<td>60,0%</td>
<td>34,0%</td>
<td>47,0%</td>
</tr>
<tr>
<td>1</td>
<td>20</td>
<td>33</td>
<td>53</td>
</tr>
<tr>
<td></td>
<td>40,0%</td>
<td>66,0%</td>
<td>53,0%</td>
</tr>
<tr>
<td>Total</td>
<td>50</td>
<td>50</td>
<td>100</td>
</tr>
<tr>
<td></td>
<td>100,0%</td>
<td>100,0%</td>
<td>100,0%</td>
</tr>
</tbody>
</table>

Table 2. shows that 60% of companies which didn't invest in intangible assets during the last four years (2008 – 2011) bankrupted in 2012 and 66% of companies which invested in intangible assets during the last four years (2008 – 2011) haven't bankrupted and continued doing business in following year (2012).

**Table 3. Chi – square table**

<table>
<thead>
<tr>
<th>Chi-Square Tests</th>
<th>Value</th>
<th>df</th>
<th>Asymp. Sig. (2-sided)</th>
<th>Exact Sig. (2-sided)</th>
<th>Exact Sig. (1-sided)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pearson Chi-Square</td>
<td>6,784</td>
<td>1</td>
<td>.009</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Continuity Correction</td>
<td>5,781</td>
<td>1</td>
<td>.016</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Likelihood Ratio</td>
<td>6,865</td>
<td>1</td>
<td>.009</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fisher's Exact Test</td>
<td></td>
<td></td>
<td></td>
<td>.016</td>
<td>.008</td>
</tr>
<tr>
<td>Linear-by-Linear Association</td>
<td>6,717</td>
<td>1</td>
<td>.010</td>
<td></td>
<td></td>
</tr>
<tr>
<td>N of Valid Cases</td>
<td>100</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. 0 cells (0.0%) have expected count less than 5. The minimum expected count is 23,50.
b. Computed only for a 2x2 table
As we can see in table 3, minimum expected frequency count assumption is met because all cells have expected count higher than 5. We can conclude that Chi-square value is significant because it is smaller than .05 and that there is a statistically significant relationship between investing in intangible assets during the last four years and opening a bankruptcy proceeding.

Table 4. Correlations between intangible assets to total assets ratio and other financial ratios included in research

<table>
<thead>
<tr>
<th>Correlations (Non-bankrupted companies)</th>
<th>BPM-11</th>
<th>NPM-11</th>
<th>ROE-11</th>
<th>ROA-11</th>
<th>ROCE-11</th>
<th>EBIT-11</th>
<th>EBITDA-11</th>
</tr>
</thead>
<tbody>
<tr>
<td>IA/TA_11 Pearson Correlation</td>
<td>-.046</td>
<td>-.046</td>
<td>-.139</td>
<td>-.138</td>
<td>-.139</td>
<td>.923**</td>
<td>.905**</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.778</td>
<td>.779</td>
<td>.335</td>
<td>.341</td>
<td>.335</td>
<td>.000</td>
<td>.000</td>
</tr>
<tr>
<td>N</td>
<td>40</td>
<td>40</td>
<td>50</td>
<td>50</td>
<td>50</td>
<td>50</td>
<td>50</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Correlations (Bankrupted companies)</th>
<th>BPM-11</th>
<th>NPM-11</th>
<th>ROE-11</th>
<th>ROA-11</th>
<th>ROCE-11</th>
<th>EBIT-11</th>
<th>EBITDA-11</th>
</tr>
</thead>
<tbody>
<tr>
<td>IA/TA_11 Pearson Correlation</td>
<td>.047</td>
<td>-.086</td>
<td>-.042</td>
<td>-.056</td>
<td>-.042</td>
<td>.041</td>
<td>.041</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.853</td>
<td>.734</td>
<td>.783</td>
<td>.710</td>
<td>.783</td>
<td>.785</td>
<td>.784</td>
</tr>
<tr>
<td>N</td>
<td>18</td>
<td>18</td>
<td>46</td>
<td>46</td>
<td>46</td>
<td>46</td>
<td>46</td>
</tr>
</tbody>
</table>

**. Correlation is significant at the 0.01 level (2-tailed).

Analysis conducted for non-bankrupted companies has shown that there is very strong correlation between IA/TA and EBIT (.923) and also IA/TA and EBITDA (.905). Other ratios included in analysis had slightly negative correlation with IA/TA ratio but they weren't statistically significant. It is important to highlight that all correlations between analysed ratios and IA/TA ratio for bankrupted companies showed weak correlation and weren't statistically significant.

Table 5. Linear regression between intangible assets to total assets ratio and other financial ratios included in research

<table>
<thead>
<tr>
<th>Variables</th>
<th>Bankrupted companies</th>
<th>Non-bankrupted companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent variable</td>
<td>Independent variable</td>
<td>Relationship</td>
</tr>
<tr>
<td>EBITDA_11</td>
<td>IA/TA_11</td>
<td>Positive</td>
</tr>
<tr>
<td>EBIT_11</td>
<td>IA/TA_11</td>
<td>Positive</td>
</tr>
<tr>
<td>ROCE_11</td>
<td>IA/TA_11</td>
<td>Negative</td>
</tr>
<tr>
<td>ROA_11</td>
<td>IA/TA_11</td>
<td>Negative</td>
</tr>
<tr>
<td>ROE_11</td>
<td>IA/TA_11</td>
<td>Negative</td>
</tr>
<tr>
<td>NPM-11</td>
<td>IA/TA_11</td>
<td>Negative</td>
</tr>
<tr>
<td>BPM-11</td>
<td>IA/TA_11</td>
<td>Positive</td>
</tr>
</tbody>
</table>

Table 5. shows that only EBITDA and EBIT as dependent variables have statistically significant positive relationship with IA/TA but only for non-bankrupted companies. It implies that when investment in intangible assets measured by IA/TA ratio is higher, profitability ratios EBIT and EBITDA will consequentially increase. Other ratios didn’t have statistically significant relationship with IA/TA ratio.
Table 6. Independent samples t-test (bankrupted and non-bankrupted companies)

<table>
<thead>
<tr>
<th></th>
<th>Levene's Test for Equality of Variances</th>
<th>t-test for Equality of Means</th>
<th>95% Confidence Interval of the Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>F</td>
<td>Sig.</td>
<td>t</td>
</tr>
<tr>
<td>ROE_11</td>
<td>Eva*</td>
<td>.575</td>
<td>.45</td>
</tr>
<tr>
<td></td>
<td>Evna*</td>
<td>*</td>
<td></td>
</tr>
<tr>
<td>ROA_11</td>
<td>Eva*</td>
<td>3.27</td>
<td>.07</td>
</tr>
<tr>
<td></td>
<td>Evna*</td>
<td>*</td>
<td></td>
</tr>
<tr>
<td>BPM-11</td>
<td>Eva*</td>
<td>5.35</td>
<td>.02</td>
</tr>
<tr>
<td></td>
<td>Evna*</td>
<td>*</td>
<td></td>
</tr>
<tr>
<td>NPM-11</td>
<td>Eva*</td>
<td>5.84</td>
<td>.01</td>
</tr>
<tr>
<td></td>
<td>Evna*</td>
<td>*</td>
<td></td>
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<tr>
<td>ROCE_11</td>
<td>Eva*</td>
<td>575</td>
<td>.45</td>
</tr>
<tr>
<td></td>
<td>Evna*</td>
<td>*</td>
<td></td>
</tr>
</tbody>
</table>

*Eva - Equal variances assumed  
**Evna - Equal variances not assumed

Independent samples t-test has shown that there is no statistically significant difference between financial ratios of the companies which made an investment in intangible assets and companies which haven’t made investment in intangible asset (all t-test Sig. values in table 6. are above .05).

5. CONCLUSION

According to numerous researches, importance of intangible assets in total non-current assets is continuously increasing. The aim of this paper was to analyze the impact which intangible assets have on profitability of a company. Among analyzed financial ratios only EBIT and EBITDA had statistically significant, strong, positive correlation with IA/TA ratio (only for non-bankrupted companies) while BPM, NPM, ROE, ROA, ROCE didn't. As for the regression, EBITDA and EBIT also had positive relationship with IA/TA ratio, but it was statistically significant also only for non-bankrupted companies. T-test has shown that there isn't statistically significant difference between analyzed financial ratios of companies which have invested and companies which haven’t made investment in intangible assets. We can conclude that there isn't strong evidence in favour of positive relationship between investment in intangible assets and profitability, with exception of EBIT and EBITDA.

On the other side, another aim of this paper was to determine relationship between bankruptcy and investment in intangible assets. The results have shown that there is statistically
significant relationship between bankruptcy status (bankrupted or non-bankrupted), which means that companies which invested in intangible assets were less likely to open the bankruptcy proceeding.

In conclusion, it can be said that the modern business requires companies to invest in intangible assets. However, investment in intangible assets also requires management to use them efficiently in order to create new value and preserve the business continuity.

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INTRODUCING CRM CONCEPT AND ACCOMPANYING ORGANIZATIONAL CHANGE IN PUBLIC COMPANY AS A POSSIBILITY FOR IMPROVING SATISFACTION OF RESIDENTS

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ABSTRACT
One stage in development of marketing as a business function was the introduction of customer relationship management (CRM) concept. Organizations recognized the potential for generating additional value and competitive advantage by moving their orientation from products and services towards customers. Directions for improvement derived from the environment became as significant as those designed internally, by organization itself. Public companies also became aware of the influence of customer satisfaction on business performance and financial results. CRM idea was adopted worldwide by government representatives, who realized that the best value in public service delivery can be achieved by focusing on the needs of customers, or in this case residents. However, although the benefits which this concept can provide in public enterprises were emphasized by many researchers, its implication on public service is still far from reaching its full potential, particularly in developing and underdeveloped countries. Nevertheless, the use of customer orientation idea in public companies remains to be widely spread and it should represent the guideline for local authorities in such countries. It is not necessary for public companies to buy expensive CRM applications in order to improve customer satisfaction and customer knowledge. In the beginning they can use the data stored in their current information system database for establishing CRM principles in their business, with only minor adoptions. In this way certain benefits can be achieved without implementing radical organizational change. This paper aims to propose a possible solution for adopting CRM concept and improving customer satisfaction in public company which is providing parking service in capital of one developing country from Europe.

Keywords: CRM, Customer Relationship Management, Marketing, Parking, Public Company, Public Service, Organizational change, Organizational structure, Satisfaction of residents
1. INTRODUCTION
Marketing management considers identifying and satisfying the needs of customers in a profitable way (Kotler, Keller, 2006). The discipline of marketing is constantly being reshaped by internal and external forces (Day, Wensley, 1983). At some point, marketing as business function entered into declining phase of its life cycle and the requirement of revival and further development was in accelerated adoption and implementation of the dramatic changes in communication activities (Kostic-Stankovic, 2013). Customer relationships were seen as the key strategic resource of the business (Webster, 1992). Many organizations realized that by moving their orientation from products and services towards customers they will gain the potential for generating additional value and competitive advantage. Therefore organizations were increasingly recognizing the importance of managing customer relationships, and numerous organizations turned to “customer relationship management” (CRM) to better serve customers and facilitate closer relationships with them (Teo, Devadoss, Pan, 2006).

From the production orientation of business at the start of 20th century to relationship building 100 years later, marketing has become focused on customer satisfaction, customer service, and value for the long-term benefit of the company and the customer (Barnes, 2000). CRM represents the process of establishment and maintenance of customized business relationships built on mutual trust, open-mindedness, shared risk and reward (Lovreta, Petkovic, Berman, Veljkovic, Crnkovic, Bogetic, 2010). It is a process of managing detailed information about single customer and careful handling all points of contact, for the purpose of maximizing customer’s loyalty (Kotler, Keller, 2006). By following the CRM strategies, companies can reduce overall marketing costs, increase overall customer response rates, and, most importantly, increase overall customer and firm profitability (Kumar, 2011).

However, when it comes to the implementation of CRM concept in an organization, the problem is that CRM means different things to different people (Winer, 2001). As a consequence, organizations approach CRM differently. For example, some may view CRM as a technology tool while others may view it as an essential part of business (Teo, Devadoss, Pan, 2006).

Different authors point out very strong connection between CRM and ICT. Information technology, in the form of sophisticated databases fed by electronic commerce, point-of-sale devices, automated teller machines (ATMs) and other customer touch points, is changing the role of marketing and managing customers (Swift, 2001). According to Kristin and Carol (2002), CRM represents the use of information systems for data collection, monitoring and satisfying customers’ needs. Modern approach to CRM involves the installation of a comprehensive software platform that includes multiple applications (Pan, Lee, 2003). This is a reason why the term “electronic customer relationship management” (e-CRM) can often be found in literature.

Nevertheless, in spite of the rather close association between implementation of CRM concept and application of relevant IT solutions, CRM should not be observed exclusively through the prism of technology. Organization's CRM resources consist of not only tangible hardware and software but also a number of intangibles such as customer-oriented people, process, organization, and culture (Kim, Kim, Park, 2010). In their conceptual model, Melville, Kraemer and Gurbaxzni (2006) emphasize that a company should align not only IT resources such as technical IT resources and human IT resources, but also complementary
organizational resources including non-IT human resources, culture, policies, and rules to create value generating processes. Hence, there is a need for a holistic approach by organizations to integrate IT with its business processes and customer service delivery (Teo, Devadoss, Pan, 2006). It is possible to say that CRM presents the alignment of business strategy, company organizational structure and culture, customer information and information technology in order to meet customer needs and achieve business advantages and additional profits (Kostic-Stankovic, 2013). For this reason, successful putting into practice CRM concept is necessarily followed by adequate organizational change.

It can be concluded that CRM is an IT-driven strategy whose implementation can lead towards significant benefits in term of improving business performance and achieving organizational goals, despite the type of organization. This article will propose the introduction of CRM in the public utility company which provides parking services in the city of Belgrade, for the purpose of improving satisfaction of residents. Authors of the paper were hired as business consultants in this company on a restructuring project in year 2014. All the data presented in the article were gathered during work on that project.

Second paragraph will be focused on the specificities of CRM in public enterprises. Third section will describe current business model and organizational structure of the public company which is providing parking services in Belgrade, as well as ongoing key business processes. In chapter four will be identified and presented the possibilities for improving resident’s satisfaction with parking services through the introduction of CRM concept, as well as the possible solution and accompanying organizational change. In final paragraph will be given concluding remarks and proposed directions for further research.

2. CRM IN PUBLIC ENTERPRISES
Public enterprises are usually financed from the community budget, and their existence is not conditioned by successful business results (Cudanov, Jasko, Sâvoiu, 2012). They are not profit-oriented to the same extent as private companies, since their main task is to ensure reaching of widely accepted living standards (Todorovic, Cudanov, Komazec, 2014). For this reason, certain dissimilarities in managing public and private enterprises can be identified. While there is a level of generality at which management is management, whether public or private, functions that bear identical labels take on rather different meaning in public and private settings (Allison, 1992). Public sector managers have both to manage within an environment of rationing and other special public sector characteristics and also be competitive (Flynn, 2007). Excellence in the public sector management requires treating the public as the clients, consumers and indeed partners of government services (Mayne, Zapico-Goñi, 2007). Public administrators should focus on their responsibility to serve and empower citizens as they manage public organizations and implement public policy (Denhardt, Denhardt, 2000).

Although public companies are often described as rigid, traditional and bureaucratic organizations, it does not mean that innovations are forbidden in public sector management. New Public Management appeared as an administrative philosophy with the viewpoint that there needs to be greater emphasis on results in the public sector (West, 2005). Successful innovations, especially those that increase efficiency in the delivery of services and improve receptiveness to public expectations, elicit a positive response (Paquin, 1998). Modern and inventive approaches such as CRM are more than welcome to be applied in public entities. Only in case of public entities citizens are taught of as customers and government agencies
are expected to become more entrepreneurial and innovative in their use of public money (West, 2005). CRM applications is positively associated with improved customer knowledge and improved customer satisfaction (Mithas, Krishnan, Fornell, 2005). As it was previously explained, from the aspect of public enterprises residents represent customers. Government worldwide realized that the best result in public service delivery can be reached by focusing on the needs of customers, or in this case residents (Wisniewski, 2001). Satisfaction of residents with concrete public service has become important for management of each public company, because of its effect on company’s reputation, influence and position that company representatives will occupy in the negotiations with community authorities about funds distribution (Todorovic, Cudanov, Komazec, 2014). Understanding of the interrelationship among different resident satisfaction components has important implications for improving quality of public services (Chou, Boldy, Lee, 2002).

The use of customer service ideas in government continues to be widespread, although the concept and its implications for public sector service production and delivery remain poorly developed (Fountain, 2001). For managers in public sector it is not an easy decision to invest in marketing when they have constant pressure to reduce the expenses (Kotler, Lee, 2008). This scenario is particularly present in developing and underdeveloped countries, where public companies have infrastructural barriers for implementing CRM. However, managers of such public enterprises are suggested to hold positive attitudes towards CRM since the scientific research showed that there is no significant relationship between the type of the transactional information system used and the extent to which customer satisfaction research is performed by the organizations (Stefanou, Sarmaniotis, Stafyla, 2003). It means that public companies can use existing data about the residents, which are already stored in their databases, in order to start using CRM concept. They do not need to invest in rather expensive advanced technological solutions for CRM in the very beginning. Certain benefits can be achieved only by adjusting communication, business model and business processes to CRM without implementing radical organizational change (Pan, Tan, Lim, 2006), as will be described in this paper.

3. CASE STUDY: PUC FOR MANAGING PUBLIC PARKING IN BELGRADE

According to Law on Communal Activities in Republic of Serbia (2011), management of public parking is communal service under the jurisdiction of municipalities. In the city of Belgrade, parking services related to public parking space are delegated to public utility company (PUC) named “Parking Service Belgrade”. The core activities of PUC “Parking Service Belgrade” are managing, exploitation and maintenance of public car parks and garages in the city of Belgrade. Management of public parking in Belgrade can be divided into three basic groups of activities:

1. Towing away illegally parked and broken-down vehicles
2. Managing public garages and car parks
3. Parking control in zone system

PUC “Parking Service Belgrade” is a founder of Serbian Parking Association of 28 members, and itself is a member of European Parking Association. Organizational structure of the company, as can be found on official website, is presented on Figure 1. Three core businesses which were mentioned previously occur in three separate organizational units on top hierarchical level: Exploitation and Maintenance of Vehicles Unit, Garages and Car Parks Unit and Parking Control Unit, respectively. Complete core business is under the governance of Technical Director, who is in charge for complete management of public parking in the city of Belgrade.
Non-core activities are grouped under Corporate Affairs Director and divided into four sectors at top level of hierarchy.

3.1. Towing away illegally parked and broken-down vehicles
PUC “Parking Service Belgrade” takes part in maintaining the communal law and order in Belgrade by offering services of towing away illegally parked and broken-down vehicles as well as those which have been involved in traffic accidents, by using a special tow truck called “spider”. Company also uses specially designed cranes to lift and freight bulky loads, buses and trucks when necessary.

It is very important to emphasize that all towing services are carried out only by police or municipal inspection order.

Following the report, policemen or municipal inspectors issue the order to the owner of the illegally parked vehicle to remove it within the three minutes deadline. If the driver fails to move the vehicle and it remains on the restricted area, policeman or inspector issues the warrant for the removal of the illegally parked vehicle, after which the “spider” hauls the vehicle to the nearest pound.

Company equipment is also used in states of emergency such as heavy traffic congestions, natural disasters and interventions of fire fighters, emergency squads and communal services. In addition to this, the Company takes part in directing traffic during important public events and similar organized mass gatherings, when certain vehicles parked on the street need to be moved.

If their vehicles were removed due to illegal parking, the citizens have to pay a prescribed towing fee in order to take over their vehicles, and they are also charged the fine to the police, which can be paid after the car was taken. On the other hand, if their car was removed for any other reason by the order of policeman or municipal inspector, citizens can take over their cars free of charge.
3.2. Managing public garages and car parks

PUC “Parking Service Belgrade” manages, exploits and maintains 8 public garages, 26 garages with reserved parking places, 20 car parks, all equipped with cutting-edge automatic systems, as well as toll stations, which has contributed to the faster flow of the vehicles and more reliable payment control. More than 10,000 places are found in garages and car parks. Through info-boards, Internet and mobile site the drivers can be informed about the current number of available spaces in the garages and parking lots, at any given time.

When it comes to payment for parking in public garages and car parks, residents are offered two models for all objects, and one additional model for specific car parks:

1. by the commenced hour
2. monthly subscription (several types)
3. daily parking, which is provided in specific car parks

Any resident can apply for monthly subscription in any garage or car park, and he or she will be issued the go-card if there is available space in the demanded object. If all the spaces scheduled for monthly subscription are occupied, the waiting list is formed. The list is based on first-in-first-out (FIFO) principle, which means that the resident who first applied for parking space in the object which is full will be first offered monthly subscription if available space appears.

3.3. Parking control in zone system

On-street parking places in central Belgrade are in time-restricted zones, while parking in areas with lower demand is not time-restricted. There are over 22,500 on-street parking places in zone system.

The center of Belgrade is divided into three zones: red, yellow and green, which are established, based on the criteria of congestion in certain city parts. In many cities worldwide congestion is controlled by managing prices of parking. The zones have time limits for maximum stay of one, two or three hours respectively, and are paid according to the predetermined tariff system. After the maximum parking time expires, the vehicle cannot be parked in the same zone in the next 30 minutes. Parking charges in red, yellow and green zone are applied Monday to Friday, 7 a.m. till 9 p.m. and Saturday 7 a.m. till 2 p.m.

Certain street fronts, based on traffic situation, are marked as blue zone, which is a parking zone without a time limit. This zone enables parking to be paid for as long as needed. It can be paid per hour or with multi-hour parking ticket. In blue zone parking is charged Monday to Friday from 8 a.m. to 9 p.m. and on Saturdays from 8 a.m. to 2 p.m.

Parking ticket should be placed inside the vehicle, with marked date and time of parking, or it can be bought via SMS. In second case vehicle is automatically registered in the system, and parking control is notified of the zone, date and time of purchase. If the vehicle is found parked on on-street parking space in any zone without a parking ticket, a daily ticket is being issued to the owner at price of cca. 40 hourly tickets. Daily ticket is starting from the moment of delivering. Through such a high price of daily ticket, which is authorized by local government, PUC “Parking Service Belgrade” is trying to reduce the congestion in central part of the city. Different authors pointed out that congestion can be reduced by increasing prices (Glazer, Niskanen, 1992; Arnott, Inci, 2006).
Belgrade citizens who live in the streets which are part of zone system can apply for a privileged ticket. It is issued for the vehicle which is in applicant’s ownership, only for the zone he or she lives in. Privileged ticket allows the residents to park their vehicle at the first available place without the time limitation. The residents of the particular zone can park their car without the time limit only if they find the parking place themselves in the appropriate zone they. Privileged tickets for the residents who live in a zone area are issued only for the zone they live in.

4. POSSIBILITIES FOR THE APPLICATION OF CRM CONCEPT

As presented on Figure 1, PUC “Parking Service Belgrade” is functionally organized company. Core activities are divided to separate organizational units, and level of cooperation among them is very low, due to high specialization. Functional organizations are characterized by formation of organizational silos, where knowledge, power and information can often be trapped and secluded from other parts of organization, among other structural weaknesses (Todorovic, Cudanov, Komazec, 2014). As a consequence, knowledge transfer is restrained among functions in individual organization. The residents use the services of Garages and Car Parks Unit and Parking Control Unit, but the company does not have the unique database, which is a barrier for getting insight into full performance of single customer. For example, Garages and Car Parks Unit has the list of customers who have monthly subscription for car parks, while in Parking Control Unit can be found complete data about the usage of zone system for all customers have ever parked their car in any of the zones. However, there is no connection between these databases, which disables the analysis of total revenues gained from single customer. It could be done manually, but in that case employees from different sectors would need to ask each other for the information whenever dealing with a customer. And number of customers in a city with almost two million residents is huge, so such business organization would not be sustainable.

Furthermore, in case of requests and complaints, each of three main sectors is processing them individually, depending on the subject. Although the referent could check the history of the customer and offer certain benefits for “good” customers, which is not done currently, he would not be able to get complete picture due to lack of data access. A customer who is a regular owner of monthly subscription for most wanted garage may have large debt for parking in zones, for example. In that case maybe some other resident who is frequently using and regularly paying for parking services and who applied for same garage but was not offered a subscription due to lack of capacity should get his parking space.

In order to apply CRM concept PUC “Parking Service Belgrade” should implement certain infrastructural development and accompanying organizational change.

Infrastructural development refers to the linkage of databases in order to enable full customer analysis. Since most of the data are stored in Parking Control Unit database, it should be the ground stone and leading node in future network. Parking Control Unit has most of the data because it provides the only parking service which includes vehicle identification every time. Whenever a car parked on-street is controlled, a record containing registration number, zone, date and time is added to the database. On the other hand, Exploitation and Maintenance of Vehicles Unit registers the vehicle only when it is removed by the order of police or municipal inspection. Same way, Garages and Car Parks Unit gets the customer data only if the application for monthly subscription is received, since registration numbers are not noted when a vehicle is entering the garage or car park, unless it is a subscriber with a go-card.
Figure 1 shows that the company has a whole sector for IT services. Considering the number of employees, available knowledge capacity and current stage of development, the assumption is that all described infrastructural improvements can be done in-house, which means that they do not require significant financial investments.

After securing the infrastructural background for CRM introduction, company should implement certain organizational change in order to build the capacity for CRM application. This refers to defining a single point in organization for communicating with residents. Currently, the company has a Customer Service Unit, but it is not shown on organizational structure presented on Figure 1 since it is on lower level of hierarchy. In present organization, Customer Service is directly under Managing Director, dealing mostly with receiving requests and complaints. However, the complaints regarding zone system can be submitted directly to the Parking Control Unit, since it has its own shelters for receiving parties. As it was mentioned previously, the idea is to have unique place in the organization for receiving customer requests, where they will be processed by the employees who can access all the relevant data, and then forwarded to the appropriate organizational unit with added customer background and the proposition for handling them. Optimal place for Customer Service in current organizational structure is under Technical Director, since all the stakeholders are there: three sectors where core activities are performed and IT sector.

Having performed described infrastructural and organizational change, company needs to develop CRM operating strategy, define the directions for communication with residents and educate the employees for new tasks. After that, CRM concept can be fully applied in everyday work with residents.

5. CONCLUSION
Company image among Belgrade citizens is on a rather low level, which is somewhat expected considering the core business of PUC “Parking Service Belgrade”. It is perceived as a monopolist which is not focused on improving service quality but only on gaining profits, which residents consider unacceptable for public enterprise. Possible explanation of such situation may lie in residents’ inability to realize the benefits gained by the company. They are in direct contact with the company only if they park a vehicle inappropriately or forget to buy a ticket in zone. And in that case they are charged considerable amount of money, although they pay for parking services normally, so their impressions with the company are not expected to be good.

When business processes are analyzed, it can be concluded that the company is currently not trying to establish closer connections and improve communication with residents who use parking services frequently and pay for them regularly, although it possesses all the necessary data in its databases. Main problems are functional organization and organizational silos which prevent mutual cooperation between different organizational units on data analysis. Distributed information system does not allow any sector manager to have complete access to customer data and to use them for improving customer relationships.

By networking the databases which are currently dispersed and positioning Customer Service as the only organizational unit for communication with residents on right place in organizational structure, the company would provide all the preconditions for the introduction of CRM concept without capital financial investments. As it was explained in this paper, CRM is positively correlated to customer satisfaction, and since in case of PUC “Parking
Service Belgrade” customers are Belgrade residents, satisfaction of residents can be improved. When the residents realize that company is focusing on their needs and that their loyalty and regular settlement of liabilities are appreciated, it is reasonable to expect that their satisfaction with parking services will be better. In that case the company could also count on word of mouth marketing and its viral effect, which could help in improving damaged reputation. Since all proposed solutions are on company level, further research in this area may be focused on implementing CRM concept at the city level, since much more significant results regarding satisfaction of residents can be achieved at higher level.

LITERATURE


EXAMINE THE RELATIONSHIP BETWEEN BOARD CHARACTERISTICS AND PERFORMANCE FIRMS LISTED IN TEHRAN STOCK EXCHANGE BASED ON FUZZY REGRESSION

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ABSTRACT
The present study is the relationship between the characteristics of the Board of Directors of the Company. Characteristics considered in this study consists of non-duty members of the board, separating the functions of chairman of the board of management, board size, changes in members' gender diversity on the Board of institutional owners. In this paper, variable size, operating cash flow and leverage as control variables have been considered. To conduct the study, companies listed in Tehran Stock Exchange for 83 to 88 years were examined and 159 companies were selected. In this study, the ratio of return on assets is represented as a function of the applied. To test the hypothesis, the fuzzy linear regression coefficients were used. The results show that, compared with other members of the Board shall, segregation of duties, the Board, gender diversity and leverage are negatively correlated with performance. In this study, changes in the Board of Directors, the Company's operating cash flow and have a direct relationship with firm performance. The study found no association between institutional ownership and firm performance.

Keywords: board of director characteristics, performance, return on assets, fuzzy regression

1. INTRODUCTION
In the current business structure, separation of ownership from management is inevitable and the lack of an effective monitoring mechanism for the management of such companies is likely inefficient allocation of resources, reduce performance and increase the development of organizational problems. The purpose of this legislation was to improve the efficiency of board of directors and other management companies. Efforts to establish an effective monitoring mechanism on corporate performance Iran has also led to the development of a Corporate Governance Code (corporate governance) has been in Tehran Stock Exchange. The main objective of this study was to investigate the relationship between board characteristics and firm performance. For this, some of the variables that have been studied in the areas of company stock Such changes in the Board and gender diversity is studied. Namazi, Mohammad and colleagues (2007) by examining the relationship between institutional ownership current financial performance of the companies listed in Tehran stock exchange on the results achieved that there is a significant relationship between institutional ownership and firm performance, the relationship is positive.
Shin and Tseng Hsin Ping (2009) presented the relationship between an internal management and institutional property on the performance of listed companies in Taiwan Stock Exchange in the period 1994 to 2003. Their results showed that using a combination of data between internal ownership and firm performance relationship is inverted U-shaped as well as between the government and property ownership in a firm institutional performance, there was a significant negative correlation during the study.

Sabor and Mullah Omar al-Faruq and Rasool
Karim (2008) discussed the effect of the relationship between ownership structure and board structure and financial performance. Their research was concluded there was no difference between the company's corporate governance system, due to the difference in performance was measured. Among the reasons they cited in their study on the capital market is different in the different combination. Gira Yamsry and Syrbama County Hras (2009) focused on the research firm corporate value. Their research examined the impact of the board of directors and non-financial performance of 245 companies surveyed. The result of their research disapproval significant impact on improving the value of board companies. The present study sought to examine the relationship between the characteristics of CEO duality (when the CEO is also the chairman of the board of directors). Than non-duty members, board members, changes in members of the board of directors and gender diversity of institutional owners of the Company. In this study, to reduce error in fuzzy regression was used to test the hypothesis.

2. THEORETICAL FRAMEWORK
Personal representative of the owner to another person as a representative in order to perform specific tasks and to achieve a certain goal is empowered. In this connection, the representative of the owner is obliged to Kargyrd their skills to ensure the expected benefits Owner. The common element is that all of the account numbers that are valuable and useful to have significant correlation with the stock market value. There is much empirical evidence of the relationship because of poor earnings - returns to low information content of reported earnings call. This issue is related to the representation theory.
Improve the corporate governance structure of the board as one of the mechanisms through align the interests of managers and shareholders to assist investors and financial reliability of financial reporting and to enhance the convergence process.

3. LITERATURE:
The relationship found between any of the features and performance of the Company's Board of Directors has been studied in previous research.

3.1. Outside directors and firm performance
From the standpoint of representation, the presence of outside directors (non-executive) of the Board and their oversight function as independent individuals, to reduce conflicts of interest between shareholders and managers at board meetings, the remarkable help. Vyanar Research (2007) indicated that there was a positive correlation between the ratio of the outside and firm performance. Gravl Literature and fruit (1966) Non-member board of directors shall have a negative effect on firm performance. The lack of research on the relationship between the duty and function of other members of the team. Separation of the functions of Chairman and CEO of the company, While some studies have shown that the separation of duties, significant improvement in performance. (Rchnr and Dalton, 1991; Peel and O'Donnell, 1995), some of the positive correlation between lack of segregation of duties and performance have been mentioned (Ward, 1995; Batyvla, 2008). Some researchers also believe that the difference between separation or lack of segregation of duties is not detected (Daily and Dalton, 1997; Dalton et al., 1998).

3.2. Gender diversity and corporate performance:
3.3. Institutional Ownership and Corporate Performance

Short and Jelly (1997) and Ho (2005) stated that the active role of institutional owners can have a positive effect on the financial performance of corporations. In this regard, the ownership structure of companies listed in Tehran Stock Exchange shows that More than 65% of institutional ownership in the stock of companies and organizations, governmental and quasi-governmental Such organizations and foundations are expanding.

4. RESEARCH HYPOTHESIS

According to the research objectives, research hypotheses can be described as follows:

1- ACombination between outside directors board of directors and stock returns, there is a significant relationship.
2- The division of responsibilities between the chairman of the board of management of stock returns are statistically significant.
3- The number of board members and there is a significant correlation of stock returns.
4- Between changes in board members or their representatives in the current year compared to the year before there is a significant relationship between stock returns.
5- Gender diversity on the board and there is a significant correlation of stock returns.
6- There is between institutional ownership and stock returns.

Variables and Methods:

Table 1: dependent variables, independent and control

<table>
<thead>
<tr>
<th>variable dependent:</th>
<th>Operational definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock returns</td>
<td>To calculate the efficiency of capital stock of the companies surveyed, the source of capital and capital increase should be considered. Due to these factors, the following formula to calculate the output is.</td>
</tr>
<tr>
<td></td>
<td>Ke = \frac{(1+\alpha_1+\alpha_2)P_1 + DPS - P_0 - \alpha_1 (par value)}{P_0 + \alpha_1 (par value)}</td>
</tr>
</tbody>
</table>

The equation P1 stock price at the beginning of the year, DPS dividend, P2 stock price at the end of the year, α1, the percentage of receivables and has a cash capital increase, α2, the percentage increase is the capital of the reserves.

Independent variables:

Outside directors

Some of the members of the Board of Directors of the Company shall (with executive responsibility) and some other are non-required (no executive responsibilities) . Non-executive members of the Board of Directors by dividing the number of outside directors on the Board of Directors is achieved.

Segregation of duties, the President of the Board of Management

In case of separation of duties, the President of the Board of Management of a dummy variable Otherwise the dummy variable is zero.

The number of board members

This variable is an indication of the company's
Board of Directors.

If the Board of Directors this year are unchanged from the previous year, the dummy variable is a dummy variable and zero otherwise available to it.

Gender diversity on the board

In the case of a female member of the board of directors of a dummy variable and otherwise the dummy variable is zero.

Institutional owners

The total shares owned by shareholders who possess more than five percent of the company’s total shares.

Control variables:

Company Size

Size using the natural logarithm of total assets at the end of the period is calculated.

Operating cash flow

In this study, the ratio of operating cash flow to assets is considered as a control variable.

Lever

In this study, the use of long-term debt to total assets ratio is calculated by the end of the fiscal period.

The study population for this study, all firms listed in Tehran Stock Exchange has approved the 1382 Stock during the study of signs and symbols are trading foreign exchange is not. In this study, the fuzzy regression was used to test the hypotheses. In regression analysis, statistical, computational error between observed data and regression model, a random variable with normal distribution. However, based on the phase error of the fuzzy regression model.

Therefore, in order to eliminate the need for an alternative and disadvantages of the classical regression model, in this paper, fuzzy linear regression coefficients were used. General model is:

\[ \hat{Y} = \hat{A}_0 + \hat{A}_1 x_1 + \hat{A}_2 x_2 + \cdots + \hat{A}_n x_n \]

Where \( \hat{Y} \) is the dependent variable and fuzzy, \( x = (x_1, x_2, \ldots, x_n) \) Vector of independent variables with real values and coefficients it is \( A = \{\hat{A}_0, \hat{A}_1, \ldots, \hat{A}_n\} \) a set of fuzzy numbers.

In the study of triangular fuzzy numbers are used to determine the coefficients of the model. The triangular fuzzy number by three regular \( \tilde{A} = (a, s^L, s^R) \). It is shown that \( a \) the cursor and \( s^L \) and \( s^R \) are the width of the left and right. If \( s^L \neq s^R \) is the asymmetrical triangular fuzzy number. And assuming \( s^R = ks^L \) we have (k Positive integer and real).

\[ \hat{A}(x) = \begin{cases} 1 - \frac{a-x}{s^L}, & a - s^L \leq x < a \\ 1 - \frac{x-a}{ks^L}, & a \leq x \leq a + ks^L \end{cases} \]

If \( s^L = s^R = s \) then \( \tilde{A} \) is called a symmetric triangular fuzzy number and it will display \( \tilde{A} = (a, s) \).

\[ \hat{A}(x) = \begin{cases} 1 - \frac{a-x}{s}, & a - s \leq x < a \\ 1 - \frac{x-a}{s}, & a \leq x \leq a + s \end{cases} \]

In order to set times of observations to estimate the coefficients of the fuzzy model, criteria and standards should be considered. The first criterion is that the membership function values of \( y_j \) in \( \hat{Y} \) is a large number (Output per \( x_j \)). In this case, we are sure that the fuzzy model is fit to the observations. We are looking forward to the second measure of uncertainty in
predictions based on the minimal model. In other words, we are looking for a model that, first, the \( \bar{Y} \) phase output for all values of \( \bar{Y}_j \), \( j = 1,2,\ldots,m \) has a membership degree is at least as large as \( h \), namely:

\[
\bar{Y}_j(y_j) \geq h, \quad j = 1,2,\ldots,m
\]

Secondly, given the fact that the width of a triangular fuzzy number is greater than the uncertainty that is, to achieve the goal, we need to minimize the total output cuts.

If \( \hat{A}_i \) is \( i = 0,1,\ldots,n \) symmetric triangular fuzzy numbers and real numbers \( x_i \), then \( \bar{Y} \) is a fuzzy number, and if \( \bar{Y} = (f^c(x), f^{sL}(x), f^{sR}(x)) \) is symmetric, where \( f^c(x) \) the middle or front panels and \( S f^{sL}(x) \) and \( f^{sR}(x) \) and \( \bar{Y} \) are as follows:

\[
\begin{align*}
  f^c(x) &= a_0 + a_1 x_1 + \cdots + a_n x_n \\
  f^{sL}(x) &= s_0^L + s_1^L |x_1| + \cdots + s_n^L |x_n| \\
  f^{sR}(x) &= k_0 s_0^R + k_1 s_1^R |x_1| + \cdots + k_n s_n^R |x_n|
\end{align*}
\]

Where \( a_i, i = 0,1,\ldots,n \) view factor \( A_i \) and \( s_i^L \) factor \( A_i \) rather wide right.

Membership function \( \bar{Y} \) is:

\[
\bar{Y}(y) = \begin{cases} 
1 - \frac{f^c(x) - y}{f^{sL}(x)} & f^c(x) - f^{sL}(x) \leq y \leq f^c(x) \\
1 - \frac{y - f^c(x)}{f^{sR}(x)} & f^c(x) \leq y \leq f^c(x) + f^{sR}(x) \\
0 & \text{otherwise}
\end{cases}
\]

Therefore, we will assume that \( \bar{Y}_j(y_j) \geq h \):

\[
1 - \frac{f^c(x_j) - y_j}{f^{sL}(x_j)} \geq h \Rightarrow (1 - h)f^{sL}(x_j) - f^c(x_j) \geq -y_j \quad j = 1,2,\ldots,m
\]

\[
1 - \frac{y_j - f^c(x_j)}{f^{sR}(x_j)} \geq h \Rightarrow (1 - h)f^{sR}(x_j) + f^c(x_j) \geq y_j \quad j = 1,2,\ldots,m
\]

Placing the appropriate link in the above equation, we get:

\[
(1 - h)s_0^L + (1 - h) \sum_{i=1}^n s_i^L |x_{ij}| - a_0 - \sum_{i=1}^n a_i x_{ij} \geq -y_j \quad j = 1,2,\ldots,m
\]

\[
(1 - h)k_0 s_0^R + (1 - h) \sum_{i=1}^n k_i s_i^R |x_{ij}| + a_0 + \sum_{i=1}^n a_i x_{ij} \geq y_j \quad j = 1,2,\ldots,m
\]
Where $x_{ij}$ represents the view of the variable $j$ is $i$.
Total cuts output phase $\hat{y}$ has the form it is called the objective function.

$$z = (1 + k_0)m s_0^L + \sum_{i=1}^{n}((1 + k_i)s_i^L \sum_{j=1}^{m} |x_{ij}|)$$

So in the case of regression analysis to consider an asymmetric triangular fuzzy numbers to obtain the parameters of the following linear programming problem:

$$\text{Min} \quad z = (1 + k_0)m s_0^L + \sum_{i=1}^{n}((1 + k_i)s_i^L \sum_{j=1}^{m} |x_{ij}|)$$

$$\text{s.t.}$$

$$(1 - h)s_0^L + (1 - h) \sum_{i=1}^{n} s_i^L |x_{ij}| - a_0 - \sum_{i=1}^{n} a_i x_{ij} \geq -y_j \quad j = 1, ..., m$$

$$(1 - h)k_0 s_0^L + (1 - h) \sum_{i=1}^{n} k_i s_i^L |x_{ij}| + a_0 + \sum_{i=1}^{n} a_i x_{ij} \geq y_j \quad j = 1, ..., m$$

Where $x_{ij}$ represents the variable $j$ is $i$.
To solve these problems, linear programming, the software used Lingo 9 and Article 10. The coefficients are calculated using the method of defuzzification, the center of gravity coefficients are converted into real numbers. To get the best $h$, to model error (MSE) is calculated and the model that has the least error, and if the minimum number of errors occur among them is the model with the lowest objective function value is selected as the final model. It should be noted, the empirical model used to test the hypotheses is defined as follows:

$$ROS = \alpha + \beta_1 \text{COMPOSE} + \beta_2 \text{DUAL} + \beta_3 \text{NUM} + \beta_4 \text{BCHANGE} + \beta_5 \text{WMEMBER} + \beta_6 \text{IO} + \beta_7 \text{SIZE} + \beta_8 \text{CASH} + \beta_9 \text{LEV} + \epsilon_i$$

5. RESULTS
To test this model in the first stage of the characteristics of the dependent variables, and independent control has been studied using descriptive statistics and then analyzed using inferential statistical results are demonstrated.

5.1. Fuzzy regression results
In order to determine the coefficients of asymmetric triangular and symmetric triangular fuzzy regression methods were used. If we assume that the coefficients of the model are symmetric fuzzy number coefficients for all variables will be as follows:
In the present study, the centers of fuzzy coefficients, the values of \( h \) do not change. This is done to avoid a recurrence. Next, we examined the variables for different values of \( h \) and the width of the phase coefficients are determined. The steps are as follows:

- **Table:** The width of the fuzzy coefficients

<table>
<thead>
<tr>
<th>( h )</th>
<th>( a_{\text{CO}} )</th>
<th>( a_{\text{COMPOG}} )</th>
<th>( a_{BCHARG} )</th>
<th>( a_{\text{NUM}} )</th>
<th>( a_{\text{WMEMBER}} )</th>
<th>( a_{\text{IO}} )</th>
<th>( a_{\text{SIZE}} )</th>
<th>( a_{\text{CASH}} )</th>
<th>( a_{\text{LEV}} )</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.1</td>
<td>0.0066</td>
<td>-0.178</td>
<td>-0.2308</td>
<td>-0.0241</td>
<td>-0.0016</td>
<td>0.0216</td>
<td>0.1986</td>
<td>-0.412</td>
<td></td>
</tr>
<tr>
<td>0.2</td>
<td>0.0001</td>
<td>-0.172</td>
<td>-0.2243</td>
<td>-0.0241</td>
<td>-0.0016</td>
<td>0.0216</td>
<td>0.1986</td>
<td>-0.412</td>
<td></td>
</tr>
</tbody>
</table>

Other values are not listed in the table. According to the results in the table above, in the case of \( h = 0.7 \) we have the lowest error. The optimum phase is shown below:

\[
\hat{\text{RET}} = (0.0001,0) + (-0.1141,1.93844) \cdot \text{COMPOSE} + (-0.172,0) \cdot \text{DUAL}
+ (-0.2243,0) \cdot \text{NUM} + (-0.0241,0.399325) \cdot \text{BCHANGE}
+ (-0.0016,0) \cdot \text{WMEMBER} + (0,0) \cdot \text{IO} + (0.0216,0) \cdot \text{SIZE}
+ (0.1986,1.89109) \cdot \text{CASH} + (-0.413,0) \cdot \text{LEV}
\]

After defuzzification using software center "story" we have the following model:

\[
\text{RET} = 0.0001 - 0.1141 \cdot \text{COMPOSE} - 0.172 \cdot \text{DUAL} - 0.2243 \cdot \text{NUM} - 0.0241 \cdot \text{BCHANGE}
- 0.0016 \cdot \text{WMEMBER} + 0.0216 \cdot \text{SIZE} + 0.1986 \cdot \text{CASH} - 0.4134 \cdot \text{LEV}
\]

**5.2. The results of hypothesis tests**

First hypothesis: the presence of outside directors combination board stock returns, there is a significant relationship. The current study showed an inverse relationship between the presence of other directors and firm performance is required. The achievement of this Grval and nober (1996) gained.
The second hypothesis: the separation of duties of chairman of the board of management and firm performance. There is a factor a significant relationship. The results of the model indicate that the reverse relation between segregation of duties and functions of the company. The third hypothesis: the number of board members and there is a significant relationship between firm performance. The results of the current study suggest the existence of an inverse relationship between the number of board members and company performance. The fourth hypothesis: the change in board members or their representatives in the current year compared to the year before, and there is a significant relationship between firm performance. In the current study, when board members this year are unchanged from the previous year of a dummy variable and Otherwise, the value is zero. Results indicated a positive relationship between the fitted models change over the previous year and the company's board of directors. The fifth hypothesis: the gender diversity on the Board and there is a significant relationship between firm performance. The model suggests the existence of a negative relationship between gender diversity and corporate performance. The sixth hypothesis: There is between institutional ownership and firm performance. The current study showed no association between institutional ownership and firm performance.

5.3. Other results
In the present study, variables, firm size, leverage, operating cash flow is considered as control variables. The fitted model indicate that company size and operating cash flow has a direct relationship with stock return. The results also suggested that there is an inverse relationship between leverage and stock returns.

6. CONCLUSIONS AND RECOMMENDATIONS
This study seeks to find the relationship between board characteristics and stock returns are accepted in Tehran Stock Exchange. To do this, the variables of outside board members, separation of duties, the chairman of the board of management, board members, changes in members' gender diversity And institutional ownership is considered as independent variables.

LITERATURE

BUSINESS PROBLEMS IN A WOMEN'S SMALL
ENTREPRENEURSHIP - THE BOSNIA AND HERZEGOVINA CASE
OF POST CONFLICT AND TRANSITION CONTEXT

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ABSTRACT
Economic empowerment of women can lead to better growth, greater competitiveness and better human development. Economic empowerment of women through entrepreneurship and small business offers a huge space for the introduction real changes in their lives. Entrepreneurship and small business located in the center of events as change agents in the world, regardless of whether it is more or less developed countries. Why? Because it is an important source of job creation and open career opportunities for both men and women. It is an indisputable fact, however, that one is going, extensive presence of asymmetry in the approach to entrepreneurship and small business, which, among other things, also reflected in the trends in the labor market. Men and women were and still are affected by the loss or reduced employment security, or job loss, and women take an increasing share of responsibility cost of living adjustment for the family. But man traditionally "remains" breadwinner of the family as conditional access to employment, and this fact leads to high levels of participation of women on the list of the unemployed. For all that, as a result, self-employment has become for many women this is their only chance for paid work. At the same time, however, women are confronted with fewer opportunities to start their own business due to specific gender barriers in access to information, support networks and collateral. Determining sexually sensitive policies in supporting the development of small and medium business is therefore an important priority of economic policy in countries in transition. The primary goal is that through a descriptive study (first in Bosnia and Herzegovina) to determine whether and to what extent business problems are present in a woman's small entrepreneurship in Bosnia and Herzegovina in post-conflict and transitional reality. In a broader context, the results should show whether and to what extent business problems are related to insufficient economic education, and to indicate the level of readiness of women entrepreneur in small business to further education, and the purpose of acquiring the knowledge necessary for solving business problems. Work will in this regard try to show what the current economic opportunities for additional education for women entrepreneur in Bosnia and Herzegovina. For the realization of the research there will be used all the basic methods of logical and scientific knowledge. Research on this topic was based on primary data collection methods, testing techniques through surveys. To this end, we have interviewed 125 women entrepreneur in small business in Bosnia and Herzegovina. The work will include theoretical analysis of the concept of women's entrepreneurship in general, based on the available literature, scientific articles, professional journals, and other available and relevant information. In connection with the interpretation of the data obtained, the paper will in this regard provide recommendations for measures to ensure the initial conditions (empowerment through
all forms of education and training) that would result in a larger (self) employment of women and their increased participation in economic activities.

**Keywords:** women's empowerment, women's entrepreneurship, self-employment, business problems, post-conflict and transitional context

**JEL Classification:** L -26

### 1. CONCEPT OF WOMEN'S ENTREPRENEURSHIP

The importance of women's entrepreneurship and its contribution to the economic development of the country has been worldwide recognized. The concept of women's entrepreneurship in the economic vocabulary was introduced in the past 30 years, through the development of entrepreneurship in small businesses and as well as by the self-employment of women. Even the eighties of the last century were called "the decade of women's entrepreneurship". This notion "moved" from the United States over the developed countries in all others parts of the world, especially to the transition countries of the Western Balkans, including Bosnia and Herzegovina. The process of transition, the transition from "planned" market system to the "free" market competition, usually is causing overall economic crisis in the country - its consequent presentation is the increase of unemployment. Women are usually the ones (worldwide) first to lose their jobs. For most women, running their own business within the small entrepreneurship enable them to control their own destiny. Therefore for women, self-employment is the main reason for deciding for “entrepreneurial project". This explains why the term "women in entrepreneurship" or so called "female entrepreneurship" became the subject of many seminars, scientific meetings and also the programmes of the governments The answer to this question lies in the essence of entrepreneurship as the most important conditions for the initiation and development of small business. "Entrepreneurship is the process of creating new products or services, including new enterprises and institutions on the basis of original ideas, courage and ability in the present circumstances of the environment". The quotation above summarizes all the essential elements and influencing factors of entrepreneurship. The special value of above conceptual definition of entrepreneurship lies in the emphasis on continuity (the word "process"). This shows us the need for a permanent, continuous adjustment of "the circumstances of the environment" in a given "process." “The combination of various business activities, performed by contractor carrying out their business, is called entrepreneurship”. Although with modest scope, the previous definition of entrepreneurship indicates the interconnectedness and interdependence of business activities, carried out by the subject of entrepreneurship. Emphasis is given to the definition of "interdependence" of business activity and that is its main value. “Entrepreneurship is the process of creating new values by making unique combination of the different resources, for one goal to be achieved – to exploit business opportunity.” Finally, preliminary conceptual definition emphasizes the "exploitation" of business "opportunities" that points us to a particular aspect of entrepreneurship and entrepreneurs: the entity's ability for entrepreneurship in the

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137 Shahbaz Mavdat, Director, Southern Europe and Central Asia, IFC, Foreword for „Voices of Woman Entrepreneurs in Bosnia and Herzegovina", May 2008, Washington, USA.
140 Prof. dr. Milenko Dostic, „Menadzment malih i srednjih preduzeca“, EFSA, Sarajevo, Bosnia and Herzegovina, 2002, pg. 51.
141 Nikola Kuvacic, „Poredzatnicka biblija“, Beretin, Split, Croatia, 2005, pg. 15.
circumstances on the certain business opportunity, and their "use" of available resources (including of course their knowledge). Each of these definitions, or if you want to be more precise conceptual definition, has its own value and each sets its focus on certain elements essential to the understanding of entrepreneurship. In light of these conceptual definitions, women have their special place. Women unquestionably possess the creativity, necessary expertise and skills to start a new business; as well as their fellow entrepreneurs women are highly motivated, prone to taking risks and have developed entrepreneurial spirit - what is then the difference from the male counterparts?

2. DIFFERENCES: WOMEN VS MEN ENTREPRENEURS

What is the difference between "male" and "female" entrepreneurs? As previously mentioned, men and women both have basic characteristics: energy, initiative, perseverance, focus, sense of time and, above all, talent, whose combination determine themselves as entrepreneurs. They have a specific business knowledge and skills and, above all, a certain psychological value or benefits. Opportunists are full of ideas, innovative and creative, independent in forming opinions, hardworking, optimistic, visionary leaders ...... The most common are similar levels of education, beside male colleagues entrepreneurs have similar expectations regarding the profitability and challenges business. They face the same challenges as male colleagues entrepreneurs with respect to the management of small business access to credit, information, training, markets and new technologies. However, it is much more documented differences, which recorded a distinction between the two sexes in relation to their entrepreneurial activities. Here are some of them:

- Women and men differently define the term "entrepreneur" and women are less prone to such call. (Kirkwood, 2004).
- Women and men entrepreneurs have gone through different professional experiences, motivations for starting a business, different business goals and ways to create their own business. (Brush 1992.; Fischer, et. Al., 1993).
- Women entrepreneurs can expect greater social support during start-up businesses. (NFWBO, 2001).
- Women and men have a different management styles and definitions of success. (Bell, 1993).
- The level of optimism and confidence which women have while starting-up their business is lower than their male counterparts. (Singer, 2000).
- Women entrepreneurs are putting a greater emphasis on independence as expected "result" when starting their business (Shane, et. Al., 1991; Ljunggren & Kolvereid, 1996).
- It is more likely for women entrepreneurs that they were working part-time just prior to initiating their own business (Kolvereid & Bullvåg, 1994).
- Women entrepreneur in their business activities "bring" experience of a daughter, wife and mother, recognizing in business activities the importance of personal and human relationships (Reed, 1999).

143 E. Kepler and S. Shane, „Are male and female entrepreneurs really that different?“ Small Business Research Summary, SBA, Office Advocacy.  
Women are usually describing their businesses by using the terms of family nature and their business relationships present as a network, men entrepreneurs thinks hierarchically and seek to establish relations with emphasis on procedures and rules. (Aldrich, et. Al., 1989).

- Women prefer their business activities to be intuitive. This is so called "right side brain" thinking, which emphasize on creativity, sensitivity and core values, while men prefer to entrepreneurs in their business activities on logical "left brain" in thinking, which emphasize analysis, methodical processing of data and develops procedures (West and Zimmerman, 1987).

- Women entrepreneurs are different from men entrepreneurs in how they make their purchasing decisions, although they tend to invest in the use of computers and information technology in the same way as men entrepreneurs (NFWBO, 1994).

- Still, in the world, more men than women run a business and become self-employed. However women in the United States faster than elsewhere in the world starts their businesses (Kourilsky & Walstad, 1998; Kolvereid, et. Al., 1993).

- Women entrepreneurs rely more often on the information and advice provided by their business colleagues than the men entrepreneurs who tend to seek information through online publications, magazines of general interest, through business meetings of various associations and Internet (NFWBO, 2000).

- Women tend to employment in a lesser extent, which is related to the fact that women entrepreneurs are deciding to start smaller businesses (Fischer et al., 1993)

- Women see men as persons who better deputizes, while men admire women because they are perceptive and take care of their business relationships and know how to balance between different tasks and priorities (U.S. Department of Commerce, 1992)

From all of this we can conclude that, although men and women entrepreneurs in business possess important entrepreneurial similarities, they are often different in the way they function in enterprise environment. First of all women in that environment are motivated differently, they seek support differently, they define success differently, they differently displayed responsibilities and relationships, business decisions are made differently, they have a different view of technology and its possibilities, they invest differently and balance the tasks differently. The challenges posed by modern business are changing the role of women once only "traditional" consumers. Although women have made great strides in the business in recent years, gender differences in entrepreneurship in nearly three decades remain relatively unchanged.147

3. VIEW ON WOMEN'S SMALL ENTREPRENEURSHIP WORLDWIDE

Today, in developed and developing countries, small and medium enterprises provide most of the new jobs by expanding the range of products and services and performing on the international market. Businesses that are led by women contribute to that significantly. The number of women in business all over the world is increasing and it is a subject to constant monitoring. In this regard, there is tendency of developing and supporting female entrepreneurship, as well as monitoring and researching. This trend has spread over the developed and underdeveloped countries. For the purposes of monitoring women's entrepreneurship in the statistical framework, generally speaking, women entrepreneurs are "defined" as a woman or group of women who have initiated, organized or running business activities. Individual legal regulations in different countries of the world usually define women's entrepreneurial activity as a business activity owned or controlled by women, assuming that a woman has a minimum of 51% financial interest in the property or capital or it is at least 51% of women employees in the said business enterprise. It is very important herein mentioned the question of control, since control means the actual implementation of the right to make business decisions, which means that women are actively involved in the daily management. Business activity by women is statistically monitored for past several years. The lack of statistical data related to analysis of participation of female entrepreneurship in the national economy, especially the problems the women entrepreneurs are faced, makes any analysis limited. The above is usually a result of lack of national interest in entrepreneurial activities of women, which are usually motivated by thinking that women's entrepreneurial ventures small in size and that they do not even provide the settlement of monthly expenses. It is often considered that women are not asserted to run their own business and that they have the ultimate intention to devote to other activities. This opinion was present until entrepreneurial activities led by women in the United States made economic "boom" creating in eighties, the income of over 1.4 trillion $ and 2/3 of all newly opened jobs. The representations and roles of women in the entrepreneurial world are illustrated by the facts below:

- In the USA, the growth rate of female small business during 2002, has doubled the national average, and almost half of all American companies are owned by women;
- In Canada, between 1981 and 2001, the number of women entrepreneurs is increased by 208% compared with the increase in the number of male entrepreneurs of 38%.
- In the UK, the situation in terms of women's entrepreneurship is worse than in other developed countries according to the available indicators. Only 6.5% of all women of working age were employed in their own businesses. The proportion of women in entrepreneurship is 26%, and this is a figure which does not change since the 90’s of the last century.
- In the EU, 70% of women entrepreneurs founded and later lead companies that employ five of the seven employees.
- In Canada, only 17% of female entrepreneur earns more than the average Canadian income. On the other hand, 42% of male entrepreneurs earn more than the Canadian average income.
- In the transition countries of Central and Eastern Europe, the economic status of women is exacerbated by reductions in the public sector, increased unemployment rates, greater insecurity in employment and the poor state of social protection systems.

148 Prof. dr. Milenko Dostic, „Menadzment malih i srednjih preduzeca“, EFSA, Sarajevo, Bosnia and Herzegovina, 2002. pg. 55.
149 Mr. Sc. Petar Covo, „Odrzivo preduzetnistvo – zensko preduzetnistvo“, Zadar University, Croatia, 2007, pg. 53.
Global Entrepreneurship Monitor (GEM) in 2010\textsuperscript{150}, apropos its special report on women and entrepreneurship is the result of the continuity of the periodic reports composed to ensure a comprehensive and timely research about the importance of women involved in entrepreneurial activity worldwide. GEM research project provides comparable data for the assessment of national entrepreneurial activities in 59 countries around the world whose economies represent more than 52 percent of the world's population and 84 percent of world GDP.\textsuperscript{151} GEM report on women entrepreneur provides an analysis of key features and preview of context of female entrepreneurial activity, and analyze how they are and why they may differ from their male counterparts.

Picture no. 1: \textit{Entrepreneurial Attitudes Of The Adult Population Of Women And Men In 59 Countries According To Their Level Of Economic Development} \textsuperscript{152}

<table>
<thead>
<tr>
<th>Opportunity</th>
<th>Capability</th>
<th>Recognition of ent.</th>
<th>Fear of failure*</th>
</tr>
</thead>
<tbody>
<tr>
<td>W</td>
<td>M</td>
<td>W</td>
<td>M</td>
</tr>
<tr>
<td>Average: Economies based on natural resources</td>
<td>58,9</td>
<td>64,2</td>
<td>64,6</td>
</tr>
<tr>
<td>Average: Economies based on efficiency</td>
<td>41,0</td>
<td>44,9</td>
<td>49,9</td>
</tr>
<tr>
<td>Average: Economies based on innovations</td>
<td>29,5</td>
<td>37,1</td>
<td>35,2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Ent. as good choice</th>
<th>Ent. intentions **</th>
<th>High status of successful ent.</th>
<th>Media attention focused on ent.</th>
</tr>
</thead>
<tbody>
<tr>
<td>W</td>
<td>M</td>
<td>W</td>
<td>M</td>
</tr>
<tr>
<td>Average: Economies based on natural resources</td>
<td>75,8</td>
<td>74,8</td>
<td>39,2</td>
</tr>
<tr>
<td>Average: Economies based on efficiency</td>
<td>73,2</td>
<td>72,5</td>
<td>19,9</td>
</tr>
<tr>
<td>Average: Economies based on innovations</td>
<td>58,1</td>
<td>60,1</td>
<td>6,0</td>
</tr>
</tbody>
</table>

* Population aged 18 to 64 who sees good opportunities for business start – up
** Population aged 18 to 64 who are not involved in entrepreneurial activity

Attitudes of women about entrepreneurial activity is in line with the basis on which the economy resides: women in economies based on natural resources perceived business opportunities and believe in their entrepreneurial abilities. On the other hand, they have less fear of failure than women in the economy with higher level of development. Women from


\textsuperscript{152} GEM 2010 Women’s Report, page 12.
economies based on natural resources have a more positive attitude towards entrepreneurship as a positive and desirable career choice but these positive attitudes decreases with an increase in wealth of the country. Compared with men, fewer women believe that there are many opportunities for entrepreneurship and that they have entrepreneurial skills. In this regard, fewer women than men have the intention to begin with business activities and more of them (compared to men) are discouraged by fear of failure.

The proportion of women in entrepreneurial activities varies around the world, from around 1.5% of the women (adults of working age population: age 18 to 64 years) to 45.4%. For example, in economies that are based on natural resources, about 20% of the women surveyed stated they are starting or already lead the new company; in economies based on effectiveness same is stated by 9.7% of women, while in economies that are based on innovation it is stated by 3.9% of women.

The proportion of women in the total number of entrepreneurs varies greatly, from 16% in Republic of Korea and 55% in Ghana: it actually means that in the Republic of Korea on every 5 men entrepreneur comes only one woman entrepreneur, while in Ghana it is 6.

Out of 59 economies in which GEM conducted research on women's entrepreneurship, only Ghana had more entrepreneur women than men; on the other hand a very small number of countries had roughly equal numbers of men and women entrepreneurs in the total number of entrepreneurial activity. As expected the largest number of economies in the world has registered higher number of male than women entrepreneurs. Over time, it was noted that the gap between women entrepreneurs and men entrepreneurs in some countries decreased, and in some increased.

4. PROSPECTS OF THE DEVELOPMENT ON WOMEN’S SMALL ENTREPRENEURSHIP WORLDWIDE

 Almost all countries of the world acknowledged that although the individual female entrepreneurial ventures are small, their combined impact on the economy of the country is large and these can be significant from several aspects. Almost all countries of the world have different kinds of associations that bring together women active in the business world. The aim of these associations is:

- Promotion of women entrepreneur,
- Assisting the development of women's entrepreneurship,
- An increase in female employment,
- Education of women,
- The creation of business networks and women's lobby networks,
- Encouraging entrepreneurial thinking among women,
- Promoting the women’s private sector,
- And ultimately spreading the idea of the free market.

Women are joining various business associations and unions because they offer a form of leadership that women often need, if they want their entrepreneurial ventures are successful. Women's business associations of different profiles can provide women an unlimited number of direct and indirect benefits. Associations may allow them to easily access financial markets and easier access to remove or reduce the effects of different business barriers, easier access to business information on the domestic and foreign markets and of course allow them to openly and without fear disclose their entrepreneurial attitude.

Associations are also with many indirect effects important for the development of women's entrepreneurship in the world. They have proven to be very effective in increasing the confidence of women in business as well as encouraging and supporting other women to start their own entrepreneurial activities.
Another important problem that women entrepreneurs are faced with is the inability to obtain adequate financial resources necessary for the realization of the idea of the female entrepreneur. The reason most often lies in a fact that the necessary financial organizations most often distrustful the ability of women to be able to repay the funds, and the fact that most women not have a registered property on their own thus making it difficult to provide guarantees for the return of funds.

In the United States and the EU there have been established special cash funds used to provide financial resources in support of women's entrepreneurship. The condition to get the loan from these funds is a good business idea as well as mandatory education in specialized entrepreneurial centers in the area of starting and running entrepreneurial ventures. Strong women's lobbies in developed countries contributed to the fact that most developing countries allocates a substantial portion of funding for women's entrepreneurship from budget every year.

On the other hand, beside financial resources another very important resource for women's entrepreneurship is information. Due to the fact that the entrepreneurial endeavors of female are small in scope, it is very difficult to get to the information they need for expansion of business enterprise.

Women entrepreneurs are getting the information needed for the development of business by contacting people from the business network, attending a variety of themed meetings or through conversations with other people in the business environment. A moderate number of women are using adequately modern means of communications. The use of modern technology becomes a significant advantage for women entrepreneurs who live in countries with developed infrastructure. Incontinent or uneven development of modern technologies of communication can be a significant constraint on business ventures founded and led by women, when they cannot buy the equipment or if there is no infrastructure in the country where they live.

It is of a great importance for women entrepreneurs continuing education in the field of starting and running a business enterprise. Business courses, training programs and business seminars, in addition to opportunities for acquiring knowledge is also the opportunity to meet other entrepreneurs.

Women entrepreneurs need additional training and to acquire additional knowledge in the domain that are essential for the successful conduct of business enterprise: finance, marketing, management, etc..). In addition to courses for women who intend to start their own entrepreneurial venture, courses should be organized for young girls (14-18 years old) in order to stimulate the entrepreneurial spirit of the younger generation. It is very important to act entrepreneurially in these years of building personality and encourage them that they are able to set up and run their own entrepreneurial venture, which would eventually allow them to be economically independent. In education of entrepreneur women entrepreneurial centers and business associations play an important role, which offer the opportunity for additional training.

In such system which cares of and abets active role of woman an ambient for contribution to better life of all members of society is being created.

Primarily, these activities are focused on:
1) facilitating easier communication using the Internet;
2) improving policies related to women's entrepreneurship;
3) development and testing the indicators of women's entrepreneurship policy;
4) facilitate lending through innovative ways of financing;
5) improving the ability of women to develop their business activities.
It should be noted that on the market, which is increasingly driven by innovation and creativity, the participation of women in the business world became essential element in the creation of sustainable competitiveness.

5. WOMEN’S SMALL ENTREPRENEURSHIP WORLDWIDE: PROBLEMS AND CONSIDERATIONS
Unfortunately, like many other unexplored aspects of life in Bosnia and Herzegovina, there are almost no relevant and ongoing research on problems facing women in small entrepreneurship in Bosnia and Herzegovina.

One of the few primary research concerning women's small entrepreneurship in Bosnia and Herzegovina is "Female entrepreneurs in Bosnia and Herzegovina - research findings on status of female entrepreneurs - members of the network."153

It is indicative that a very large number of respondents did not answer or refused to answer the question related to business problems. It only indicates that the focus of the study was different and besides the results presented there was no intention by researchers and examinees to recognize these problems.

Unlike the situation in Bosnia and Herzegovina, the situation in other more or less developed parts of the world is much different. Numerous studies concerning the status and problems of women's entrepreneurship are the product of sustained and focused direct research. Display 3.4. (Picture no. 2) summarizes responses of 56 organizations that is specialized in providing support to women entrepreneurs; they were asked to answer the question about the main problems they face in their business operations.

Women entrepreneurs presented a list of possible business problems, indicating thereby that mentioned problems are problems of high or low importance to women in business, or whether at all represent business problems.

In another dimension of tests, the woman entrepreneur was asked whether the problems mentioned specific for women's entrepreneurial project or generally pose a problem for small entrepreneurship in general.

As specific business problems mentioned, a large number of women entrepreneur in their responses highlighted the increased burden for many women entrepreneur in relation between home and work, which can result in some negative effects (such as the inability to use the law pertaining maternity leave - (Finnish Association of Women Entrepreneurs).

According to display, difficult accesses to the markets are highly positioned as problems that women entrepreneurs are faced with. Even though this is becoming a problem in both cases with female small entrepreneurship and small entrepreneurship in general, there is understanding that they have specific marketing problems.

According to the response of a large number of women entrepreneurs in this research, the lack of marketing knowledge and experience is the biggest barrier to expansion of the entrepreneur.

Picture no. 2: Perceptions Of Specialized Agencies With Regard To The Main Issues Faced By Women Entrepreneur154

153 MI-BOSPO and BHW Foundation - “Female entrepreneurs in Bosnia and Herzegovina - research findings on their position - members of the network” – Tuzla, B&H, November, 2011.
Picture no. 3: Perceptions Of Specialized Agencies With Regard To The Main Problems Faced By Women Entrepreneurs Are In Comparison With The Problems Faced By Small Businesses In General
According to the findings of the organization to support women entrepreneur, lack of sales and marketing skills are the most common problems that have been identified by the respondent, immediately after financial problems. No matter what the problem is recorded in other entrepreneurial ventures, it does not reduce the importance of the female entrepreneur. It can all be viewed from the aspect of general need to "raise" the level of marketing knowledge and skills in female entrepreneurial and other entrepreneurial ventures.
If we take as a relevant example of one of the countries in the world that adequately monitor the problems of women in small entrepreneurship – that would be example of India. India is a country which has conducted numerous studies so far in order to identify the problems that women entrepreneurs are faced with in small entrepreneurship. According to research conducted till 2000 (Bernardshaw 1999 "Rural women entrepreneurs: problems and prospects"; Narayanan and Karunakaran - 1999: Women entrepreneurs - case studies, etc.) the biggest problem women in small entrepreneurship in India are faced with is the lack of adequate business knowledge, resulting in inadequate way female entrepreneurs offers their products or services. According to the results of these studies women in the above situation in small entrepreneurship greatly depend on the intermediaries which market their products and services. Therefore they have so far less favorable market position, because the intermediaries are those who really "takes" most of the profits. Though the majority of the women in a situation of small entrepreneurship research mentioned above could not avoid involvement of intermediaries, it was very difficult for them to do their own market research and independent advertising of products / services.

One of the researches that recently very precisely assessed de facto situation and problems in women's small entrepreneurship in India is a research presented in the study "Women small business owners in India", by Pillai and Amma - 2005, involving 200 women in small entrepreneurship. The study was conducted in order to determine the problems that women in small entrepreneurship are faced with, depending on whether it is a problem at the start of or during the business enterprise. Moreover, the problems are classified by nature to: general, problems based on the (lack of) knowledge, economic, psycho-social and technical.

According to the results of the research marketing problems as problems based on the (lack of) knowledge are positioned as the dominant group over the other mentioned problems. Accurate results are listed in the Table. no. 1.

Table. 1: Problems Based On The (Lack Of) Knowledge Among Women In Small Entrepreneurship In India (N = 200)\textsuperscript{157}

<table>
<thead>
<tr>
<th>Problems</th>
<th># of answers (max to min)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Marketing Issues</td>
<td>1</td>
</tr>
<tr>
<td>The work of government institutions and agencies cooperatig with women in small entrepreneurship</td>
<td>2</td>
</tr>
<tr>
<td>Government assistance to women in a small ent.</td>
<td>3</td>
</tr>
<tr>
<td>Advanced Technology</td>
<td>4</td>
</tr>
<tr>
<td>Analysis and selection of suppliers</td>
<td>5</td>
</tr>
<tr>
<td>The availability of adequate machinery and equipment</td>
<td>6</td>
</tr>
<tr>
<td>Comparison with other bidders in the sector</td>
<td>7</td>
</tr>
</tbody>
</table>

\textsuperscript{155} Sandra L. Fielden, Marylin J. Davidson, „International Handbook of Women and Small Business Entrepreneurship“, EE, MA, USA, 2005, page. 212
\textsuperscript{156} Ibidem, page. 213.
\textsuperscript{157} Ibidem, page. 215.
According to these and other research findings, the problems of women in small entrepreneurship in India based on the (lack of) knowledge are present in a significant extent: mainly related to lack of adequate ways to market products or services. These are the problems of ignorance of the work of different agencies and institutions that are dedicated to working with women in a small entrepreneurship, as well as (non) knowledge of various other forms of support from the government (or non-government) sector.

According to dr. Anshuja Tiwari problems faced by women entrepreneur during his entrepreneurial activities usually result in their inability to expand their business; according to the author the most influential problems met by women entrepreneurs are:

- Socio-cultural barriers,
- Problems of financing and business enterprise,
- Marketing problems,
- Problems regarding the provision of working capital,
- Manufacturing problems and other problems.

Dr. Anil Kumar in her book "Women in Small Entrepreneurship" believes that marketing problems faced by women entrepreneurs are reflected primarily in the fact that women have greater difficulties to access the market and adequate market information; these issues are far bigger and more important than the problem of access to sources of funding. Women entrepreneurs often have major challenge: how to adequately access the market and "keep" their market share. The author says that this problem, however, is not specific to women entrepreneurs who are just starting their entrepreneurial activity. This problem happens even to experienced women entrepreneurs with extensive experience as one ubiquitous and continuous challenge.

According to a survey conducted in Serbia and Bulgaria, female entrepreneurs from the tested sample in Serbia, highlighted almost all knowledge as very important for the conducting of business activities. However, what is special and important for their work has been assessed in the category of very necessary and most necessary, have determined in their responses to marketing presence on the market 66%, the development and expansion of business / products and services with 62%, the skill of business communication and negotiation with 57%, etc.

Respondents in Bulgaria according to the same study, women in business from the tested samples in Bulgaria, are also all the knowledge and skills assessed as necessary for the conduct of entrepreneurial activity. Still, they specifically highlighted, assessed in the categories of need and most needed, development and expansion of business and products / services 82%, marketing performance on the market with 77%, and the opportunity to invest with 68%.

159 Dr. Anil Kumar, „Women in Small business and Entrepreneurship“, International Publishing House PVT, LTD, India, 2008. page. 105
Picture no. 4: Assessment Of Knowledge And Skills Necessary To Conduct Entrepreneurial Activities – Female Entrepreneurs

- Organizations for management human resources: 17 not necessary, 9 a little bit, 29 moderately, 11 very, 34 most
- Managing time: 17 not necessary, 7 a little bit, 29 moderately, 15 very, 31 most
- Skills of business communication and negotiation skills: 19 not necessary, 9 a little bit, 15 moderately, 18 very, 39 most
- Export opportunities: 27 not necessary, 9 a little bit, 25 moderately, 9 very, 30 most
- Legal aspects of business: 9 not necessary, 14 a little bit, 32 moderately, 16 very, 29 most
- Possibility of investing: 11 not necessary, 5 a little bit, 25 moderately, 25 very, 34 most
- Handling of finances: 14 not necessary, 15 a little bit, 20 moderately, 20 very, 31 most
- Knowledge of foreign languages: 19 not necessary, 5 a little bit, 29 moderately, 17 very, 30 most
- Marketing and market promotion: 5 not necessary, 6 a little bit, 23 moderately, 20 very, 46 most
- Knowledge of modern technologies: 8 not necessary, 11 a little bit, 31 moderately, 16 very, 34 most
- Development and expansion of business / products / services: 6 not necessary, 31 a little bit, 15 moderately, 47 very, 47 most

And finally, how big is the importance of determining the presence of a business problems in women's small entrepreneurship, through continuous monitoring and finding ways to overcome it, it is best shown in the document known as the "cradle" of women's entrepreneurship which highlights it. In the United States exists NAWBO - National Association of Women Business Owners - National Association of Women Business Owner with about 9,000 women entrepreneurs members and 80 branches and associations throughout the United States. Of course this is only one, albeit the size of the largest women's entrepreneurial organization in the United States. The organization's activities is mainly based on the organization and implementation of conferences, seminars, and constant lobbying by all levels of government to improve the conditions and methods of operations for the women entrepreneur. From the aspect of this work very important is their success related to tracking marketing problems of women entrepreneurs in their business. Thus, the United States Congress in the document underlined the importance of

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annual monitoring of problems and successes of women's entrepreneurship in the United States, where the National Women's Business Council at least once a year make analysis of the problems facing women entrepreneurs in the United States. The National Women's Business Council also in this document commit itself to provide support for women's business centers and women entrepreneurs throughout the United States, through the provision of:
- Financial assistance,
- Assistance in running the company,
- Marketing support in overcoming marketing problems.
In the sence of providing marketing assistance to overcome the marketing problems, according to this document, the above assistance will include:
- Training and consultation on the subject of marketing with the aim of identifying and segmenting the domestic and international markets, and identifying opportunities to the same,
- Preparation and execution of the marketing plan,
- Development of appropriate pricing strategies,
- Selection of favorable supplier,
- Mastering the technique of negotiating the conclusion of the contract,
- The use of different techniques of public relations and advertising.  

6. THE BOSNIA AND HERZEGOVINA EXPERIENCE WITH A FOCUS ON BUSINESS PROBLEMS IN A WOMEN'S SMALL ENTREPRENEURSHIP

The aim was to perform descriptive research on problems facing women’s entrepreneurs for the first time in Bosnia and Herzegovina. The study was conducted on evaluation - intentional sample of 125 women entrepreneurs in all parts of Bosnia and Herzegovina. The study was conducted in the period August 2011 - February 2012. Primary data collection was done on the basis of short structured questionnaire consisted of 10 questions, most of them closed (questions with multiple choice) to facilitate qualitative analysis of the data collected.

All interviewed women in business, 125 of them, are the owners or part owners of the business. As for representation by sectors, according to the responses of those interviewed we can say that all economic activities are represented in approximately the same level, according to the presented data.

<table>
<thead>
<tr>
<th>Sector</th>
<th># answers</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Production</td>
<td>39</td>
<td>31,20</td>
</tr>
<tr>
<td>Trade</td>
<td>44</td>
<td>35,20</td>
</tr>
<tr>
<td>Services</td>
<td>42</td>
<td>33,60</td>
</tr>
<tr>
<td>Total</td>
<td>125</td>
<td>100</td>
</tr>
</tbody>
</table>

Table. 2: Results Of The Research - The Representation Of Activities By Sector Surveyed Women Entrepreneur

Taking into consideration the data about the time during which women entrepreneurs are engaged in entrepreneurial activities, we can conclude that it is mainly a period of 5 to 15 years. Significantly fewer number of women in entrepreneurial activities is shorter period of time, from 1 to 4 years, or longer period, more than 15 years. This leads us to the conclusion that there is a "tradition" of entrepreneurship for women and that women, especially in the

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post-war years, saw their chance in entrepreneurial activity, and that they used this through the relatively long period of time.

*Picture no. 6: Results Of The Research - The Number Of Years Of Entrepreneurial Activity Of Women Surveyed Entrepreneur*

Analyzing the number of employees in the sample of surveyed entrepreneur women, we can say that it is mainly on microenterprises, with the vast majority of responses recorded fewer than 10 employees. Only in two cases have been recorded more than 10, and in one case more than 15 workers / employees in the business conducted by an entrepreneur woman.

*Picture no. 7: Results Of The Research - The Number Of Employees M/F In The Business Of Female Entrepreneur*

One of the most important issues in the above questionnaire was to ask for a formal education of interviewed woman entrepreneur. Only a third of respondents had a formal economic knowledge (economic school or university), while two-thirds of respondents were no formal economic education.
Table 3: Results Of The Research - Formal Economic Education Entrepreneur Women

<table>
<thead>
<tr>
<th>Formal economic education (High School/Faculty)</th>
<th># of answers</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>YES</td>
<td>41</td>
<td>32.8</td>
</tr>
<tr>
<td>NO</td>
<td>84</td>
<td>67.2</td>
</tr>
<tr>
<td>Total</td>
<td>125</td>
<td>100</td>
</tr>
</tbody>
</table>

Although no formal economic education, the vast majority of respondents have not been able or had no the opportunity to attend relevant seminars or training related to the conduct of entrepreneurial activity. The presented results are even "less favorable" in comparison with the formal economic education.

Table 4: Results Of The Research - Attending Relevant Seminars And Training Woman Entrepreneur

<table>
<thead>
<tr>
<th>Seminars/Trainings</th>
<th># of answers</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>YES</td>
<td>33</td>
<td>26.4</td>
</tr>
<tr>
<td>NO</td>
<td>92</td>
<td>73.6</td>
</tr>
<tr>
<td>Total</td>
<td>125</td>
<td>100</td>
</tr>
</tbody>
</table>

If these figures are compared with the interest in attending seminars on relevant topics, we see that women entrepreneurs are expressed very strong interest in attending them. Very large disparity in the number of women entrepreneur who attended relevant seminars and expressed interest in attending the seminar supports the fact that there is a dire need for creating seminars aimed at women entrepreneurs, regardless of the character of their formal education, which would help them in facilitating the management and overcoming problems in their business activities.

Expressed interest in attending relevant courses, seminars and trainings created for women in business follows the results of the previous questions in the above questionnaire. Answering it most of women positively responded that additional economic education would be helpful in running a small business.

Picture no. 8: Results Of The Research - Interest Entrepreneur Women In Attendance Of Relevant Seminars And Training

![Pie Chart: yes 92%, no 8%]
The high degree of affirmative answers, which might be expected, was linked to the question of how many women in a small entrepreneurship in B&H are aware of the fact that in the developed countries of the world (as opposed to B & H) it is provided special statistical classification that allows the identification of entrepreneur women and based on that special support is provided by government and NGO sector in starting and running a business in different ways.

Women entrepreneurs have shown a distinct willingness to point out the problems in the everyday running of entrepreneurial activity and to them according to their severity and impact on the business, customer. The body of the enclosed response given the following problems:

1. Marketing issues (competition, pricing, product/service, distribution, promotion, etc.)
2. Financial problems (accounting problems, collection, sources of financing, etc.)
3. Problems with the state administration (tax policy and workload, inspections, etc.)
4. Family problems (lack of understanding of the family business obligations, etc.)
5. Unfair competition (gray economy, etc.).

The presented results the foreground financial problems as expected. It is a problem present in the overall economic activities, not only in BiH, but also in the world. However the focus of the research was to determine the existence of business problems in entrepreneurial activities for entrepreneur women in BiH and their perception of the seriousness of these problems.

The presented results of the study on the basis of answers suggest that marketing problems are present in the entrepreneurial activities of female entrepreneurs, and that according to their severity, apropos of perception of these women, are right below financial problems. Other problems inherent to the entrepreneur women, follows the results of marketing problems.

One of the positive results of the research, through interpretation of the answers in the framework of analysis of this question, are the answers to the questions of whether and how women entrepreneurs are having family problems due to his entrepreneurial commitment. Only a small number of respondents (6 of them) answered that serious family problems are present, while the vast majority of women, family problems cited as the least present in the conduct of entrepreneurial activity in relation to others.

Table. 5: Results Of The Research - The Perception Of The Seriousness Of The Problems Facing Women Entrepreneurs In Leading Their Entrepreneurial Activities
### Table 6: Results Of The Research - The Seriousness Of The Problems That Women Entrepreneurs Are Facing In Managing Their Entrepreneurial Activities - Ranking

<table>
<thead>
<tr>
<th>Problems</th>
<th>Average severity of the problem</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Financial problems</td>
<td>3.128</td>
</tr>
<tr>
<td>2 Marketing problems</td>
<td>2.112</td>
</tr>
<tr>
<td>3 Problems with administration</td>
<td>1.960</td>
</tr>
<tr>
<td>4 Unfair competition</td>
<td>1.816</td>
</tr>
<tr>
<td>5 Family problems</td>
<td>1.072</td>
</tr>
</tbody>
</table>

Displayed results shows that women entrepreneurs in BiH are faced with marketing problems in running their business and that they evaluated them as less serious problems. Average score is 2.112. However marketing problems are, in accordance with displayed problems, right below financial problems which are evaluated as the most serious and most present – average score is 3.128.

### 7. CONCLUSION

Female entrepreneurship in Bosnia and Herzegovina in the last few years has gained importance. Particular importance and emphasis was placed on the women’s small entrepreneurship. This is due to the fact that Bosnia and Herzegovina is not isolated from global trends and economic developments in economic theory. In this regard, it is very important the participation of our country in the GEM project that "globaly" at the local level monitors relevant issues related to women's entrepreneurship, which shows that Bosnia and Herzegovina follows with modern trends related to women's entrepreneurship.

Although in many segments shown as a positive example and as a trend in the economic reality of Bosnia and Herzegovina, a women small entrepreneurship is in the "challenge" to respond to the current time of economic recession. In order to gain strength and in turn to help the healing of the whole economy it has to be first of all legally "recognized" (as it is in most countries of the world and neighboring countries), both by statistical or by the legislative institutions. Only with creating basic preconditions for recognizing and evaluating it would be possible to address all problems facing female entrepreneurship in Bosnia and Herzegovina in a systematic and rational way.

Only then it will be possible and direct all the efforts to improve the overall situation for small-existing ventures of female entrepreneurship as well as to encourage new ones who could find space and time for its implementation.

Unfortunately, like many other unexplored aspects of life in Bosnia and Herzegovina, there is almost no relevant and ongoing research on problems facing women in small entrepreneurship in Bosnia and Herzegovina. Unlike the situation in Bosnia and Herzegovina, the situation in
other more or less developed parts of the world is much different. Numerous studies about the status and problems of women's entrepreneurship are the product of sustained and focused direct research.

It is very often said that if you fail to adequately prove the existence of a specific problem, you can only suffer its consequences, but you cannot in an adequate way devote to its resolution. This was exactly the main reason for choosing the topic of inquiry.

The results of this research lead us to number of conclusions:

- In Bosnia and Herzegovina women’s small entrepreneurship is faced with numerous problems where with its seriousness financial and marketing problems are outshined.

- The majority of women owners or co-owners of a women’s small entrepreneurship in Bosnia and Herzegovina have no formal economic education. According to the results presented in research even two thirds of the respondents have no formal economic education, regardless of whether we speak about the Economic High School or Faculty of Economics. This fact only underscores the importance of additional economic education through specially designed seminars and training for obtaining knowledge to adequately identify and solve business problems:

  - In Bosnia and Herzegovina women’s small entrepreneurship is faced with non existence of adequate additional education for women entrepreneur. This is suggested by the fact that very few women had the opportunity to attend appropriate courses (according to research presented only approximately 33% of the respondents have attended relevant courses), which would facilitate overcoming the problems of the business. It is the fact that a very high percentage of respondents showed a willingness to attend relevant seminars (90% of respondents indicated their willingness to do so) that shows awareness of gaining the knowledge necessary to overcome and solving business problems.

  - The special value of this research lies in the fact the women entrepreneur in Bosnia and Herzegovina reported a very high level of readiness to engage in a more organized way to support the work and activities of women entrepreneur.

In this regard, the following recommendations are given as a result of work and research, and are based on the presented results:

- In Bosnia and Herzegovina women's small entrepreneurship, especially in the current conditions of economic recession and crisis, should be offered a series of seminars and adequate training. Women's small entrepreneurship would, through additional economic and marketing education, enable obtaining additional knowledge to overcome present business problems, because the vast majority of women in entrepreneurship is without formal economic education.

- Women in small entrepreneurship in Bosnia and Herzegovina are aware of the problems in business, according to its seriousness allocate financial and marketing in the first place but they are also aware of the need to acquire additional skills that would help them to overcome those problems.

- Only through organizing and incentives to organizations in Bosnia and Herzegovina which are supporting women's entrepreneurship in general and supporting predominantly women's small entrepreneurship should be more insisted on creating economic education system solutions (Academy of female entrepreneurship, etc.). That would adequately and continuously monitor certain problems and respond to them through specially designed programs of support and education.
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WOMAN ENTREPRENEURS IN KOSOVO

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ABSTRACT
The entrepreneurship has no long history of the activity in Kosovo. This activity has started during the second half of last century, mainly with small businesses. During the eighties, the private business got a new strength, more rapid in all sectors. The number of businesswoman during this period of time has been very low. This was due to inability for starting a private business as well as due to the lack of sufficient experience in this sector.
During the nineties, the private entrepreneurship, both for man and woman has been brought to minimum due to a inconvenient situation for developing a business. Even the small number of private businessman or businesswoman who was doing business did not have an appropriate legality from the Serbian regime installed in the economy of Kosovo then. A lot of people became jobless as a consequence of massive violent termination of the employment in the social sector by Serbian regime; therefore they were forced to work “illegally”.
The number of businesswoman registered in the government institutions during the nineties was very low, while after the year 2000, they started to work as entrepreneurs in a regular way, in a full compliance with the legislation of the Republic of Kosovo. This number is rapidly increasing as a result of the aid extended from different international organizations as well as different donors, through financial aid or the professional training provided for them. Despite that the profit of businesswoman is rather low, they have still partiality to create a better life for them and their families, employing an appropriate number of workers, mainly family members and relatives.
Key words: entrepreneur, woman entrepreneur, self-employed, female entrepreneurship
IUSE02: The challenges of Entrepreneurship

1. WOMAN ENTREPRENEURS IN KOSOVO
The entrepreneurship has no long history of the activity in Kosovo. This activity has started during the second half of last century, mainly with small businesses. During the eighties, the private business got a new strength, more rapid in all sectors. The number of businesswoman during this period of time has been very low. This was due to inability for starting a private business as well as due to the lack of sufficient experience in this sector.
During the nineties, the private entrepreneurship, both for man and woman has been brought to minimum due to a inconvenient situation for developing a business. Even the small number of private businessman or businesswoman who were doing business did not have an appropriate legality from the Serbian regime installed in the economy of Kosovo then. A lot of people became jobless as a consequence of massive violent termination of the employment in the social sector by Serbian regime, therefore they were forced to work “illegally”.

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The number of businesswoman registered in the government institutions during the nineties was very low, while after the year 2000, they started to work as entrepreneurs in a regular way, in a full compliance with the legislation of the Republic of Kosovo. This number is rapidly increasing as a result of the aid extended from different international organizations as well as different donors, through financial aid or the professional training provided for them. Despite that the profit of businesswoman is rather low, they have still manage to create a better life for them and their families, employing an appropriate number of workers, mainly family members and relatives.

1.1. The history of the beginning and development of entrepreneurship

It is obvious that a lot of well known names of the world science have dealt with the entrepreneurship. The notion of “Entrepreneur” and “Entrepreneurship” for the first time was mentioned by Richard Cantillon in 1725 (1)

In fact, the real history of the notion of entrepreneurship has been marked in 1950 when people have start to create new ideas for the business activity as individuals. Among a lot of definitions which have mark the history of the entrepreneurship are the following:

Peter Drucker describes the entrepreneurship as a business which is organized in a systematic and effective way.

According to Drucker, the entrepreneur economy is a cultural and psychological phenomenon as much as it is an economic and technological phenomenon. (2)

Richard Cantillon describes the entrepreneurship as an economic activity under the uncertain circumstances, while Jean Baptiste Sey describes the entrepreneurship as a successful combination of production factors in a harmonic system, a system by which the entrepreneur turns and disorganize things (3).

According to Stevenson, the main features which make an enterprise to flourish include the following: the mobility of resources; reinvestment in the community; the happiness in the success of others and the evaluation of change.

Kuratko and Welsch mention four main features of an entrepreneur:

- Knowledge of the market chances
- The readiness to accept the risk
- The ability to provide resources (sources) for investment
- The ability to manage the business

1.2. The basic starting points of the entrepreneurship in Kosovo

It is obvious that the enterprises are very important for the economic system of each country in general and for the economic system of our country in particular, having in mind the fact that we are facing the transition.

According to the data available, the entrepreneurship has start many years ago, while in Kosovo it has occur a lot later, while the significant developments have start in the second half of the nineties of the 20th Century.

According to the data of the period between 1999-2005 comparing with the previous data such as for the years 1985-1999, the entrepreneurship marks a higher percentage which in fact shows that the entrepreneurship in Kosovo is taking the appropriate place in the overall economic development in Kosovo.(4)

1. R.Canillon “The controversy related to the mentality of trade” page 48, 2009
2. Dr. Emeric Solymossy & Dr. Safet Merovci, The Entrepreneurship, page 4
3. The same, page 4
4. A Report for the UN Secretary General, Fostering the entrepreneurship, page 13, NY 2004
1.3. The types of entrepreneurship in Kosovo

All types of the societies in Kosovo are registered with “The Agency for Registering the Businesses in Kosovo-ARBK” (5) Before the year 2012 this was called “The Registering Office” within the Ministry of Trade. (6).

1.4. According to this, the types of businesses in Kosovo are the following:

2. Individual business (A single owner);
3. General partnership (General co ownership);
4. Limited partnership;
5. Limited Liabilities Companies (LLC);
6. Stock Companies (SC);
7. Socially Owned Enterprises (SOE);
8. Publicly Owned Enterprises (POE);
9. Agriculture Cooperatives;

1.4.1. The Individual business: In the individual business, the owner has an unlimited responsibility for all liabilities of the society. The society has an official name, including the legal surname of the owner, adding the abbreviation “I.B”. The status of the individual business is a natural person. The individual entrepreneur is a natural person who performs a certain activity pursuant to law provisions for that enterprise, but in an independent way. According to a recent study, it is estimated that around 72% of enterprises in Kosovo are organized in the form of individual business (single property), 11.3% of the businesses are organized in the form of Limited Liability Company (LLC), 7.0% of the businesses are organized in the form of general partnership and 3.0% of the business companies are organized in the form of limited partnership (7).

1.4.2. General Partnership: In this form of business, all partners have a jointly unlimited responsibility for the liabilities of the company. The joint company has a common name in which the name of one or more partners can be included, putting at the end an abbreviation “GP”.

1.4.3. Limited Partnership: In the Limited Partnership companies, despite the unlimited partners (the partners have unlimited responsibilities for the liabilities of the company), the limited partners also participate or the partners who are responsible for the debts of the company up to the value of their contributions. The Limited partnership has a name in which one or more partners can be included, putting at the end an abbreviation “LP”. This company has no status of the legal person.

1.4.4. Limited Liabilities Company (LLC) A company of limited liabilities are the companies which have been established by one or more founders who are responsible for all liabilities for all assets. The Limited Liabilities Company has a name while after the name, there is an abbreviation LLC. The Agency for Registering the Business in Kosovo (ARBK) can register a company with limited liabilities, without documentary evidence for paying the capital. This company has the status of the legal person.

5. The Parliament of Kosovo, The Law on Trading companies nr. 02/L-123, page 20, 2008
6. The Law amending the Law nr. 02/L-123 for Trading companies, page 34-, 2012
1.4.5. **Stock companies (SC).** Stock companies are the companies whose capital is shared into the shares while the shareholders are responsible for all liabilities and other obligations for all assets and other property. The company can be established with one or more shareholders. The company has the name and the distinction “SC”. The amount of the initial capital is at least 10,000 Euro. This company has the status of a legal entity.

1.4.6. **Foreign company:** The foreign company is a trading company while from the moment it is registered, it is considered to be a subsidiary in Kosovo which is not identified as legal entity. After the registration, it has all rights and obligations prescribed by applicable law. The abbreviation “Subsidiary in Kosovo” is placed after the name.

1.4.7. **Socially Owned Enterprises (SOE):** A Socially Owned Enterprise means a legal entity where the majority of the assets and capital has a social ownership. Such Enterprises until they are privatized are under the jurisdiction the Privatization Agency of Kosovo, pursuant to Law Nr. 02/L-123 designated for the Trading companies. This company has the status of a legal entity.

1.4.8. **Publicly Owned Enterprises (POE):** The Publicly Owned Enterprise is an enterprise dealing for a general interest while it is established by the government. The Publicly Owned Enterprise is monitored by the Government and are organized as Stock Companies, pursuant with the applicable law on trading companies. All ownership interests in a Publicly Owned Enterprise will be represented through shares while all these shares should be registered. This company has the status of a legal entity.

1.4.9. **Agriculture Cooperatives (AC):** The Agriculture Cooperative is a trading company established by natural persons who are mainly farmers who contribute with their private property in the initial capital. The Agriculture Cooperative is established by at least 5 (five) farmers who are the signatories of the obligations. The cooperative can not be registered nor exist without capital.

The capital is shared into the shares value equal to a value of at least 10 Euro. The Director can not be a member of the Cooperative. (8)

1.5. **Categorization of businesses according to their size**

The importance of entrepreneurship in the economic development of a country is often measured through participating of small, medium and large enterprises, employment and participation in the GDP.

In some economies of a few countries which make the group of eight the most developed nations in the world today, the ones with a rapid industrial development, due to its significant development of the extractive industry, due to the expansion capabilities into the large world markets, but also due to their significant capability in the domestic market, large enterprises with more than 500 employees dominate in their structure of classification, such as USA, Germany, Great Britain etc.

In the economies which are ranked into the so called second category, are ranked the countries which have had a historical tradition in entrepreneurship and trade, where the economic development was mainly based in small and medium enterprises such as in Italy, Japan, France etc.

In the most countries of the world and in particular in developed countries, these enterprises were divided into small, medium and large enterprises. The criteria for categorization of businesses vary from one country to another, depending on the economic development of a given country.

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8. Law Nr. 2003/9 on Agriculture Cooperatives & Law Nr. 03/L-004 on Amending the Law on Agriculture Cooperatives Nr. 2003/9.
In Kosovo, based on Law Nr. 04/L-14 on Accounting, Financial Reporting and Auditing, in classifying the Trading companies (9), there are two criteria among three of them which should be fulfilled for each group:

1.5.1. Large trading enterprises are the ones which fulfill two of three criteria as following:
- An overall annual turnover (net): more than four million (€ 4,000,000.00)
- The assets (property) gross in the balance of statement: more than two million (€ 2,000,000.00).
- The average number of employees within a financial year: more than 50

1.5.2. Medium trading enterprises are the ones which fulfill two of three criteria as following:
- An overall annual turnover (net): more than two million (€ 2,000,000.00), but less than four million (€ 4,000,000.00).
- The assets (property) gross in the balance of statement: more than one million (€ 1,000,000.00), but less than two million (€ 2,000,000.00).
- The average number of employees within a financial year: more than 10, but less than 50

1.5.3. Medium trading enterprises are the ones which fulfill two of three criteria as following:
- An overall annual turnover (net): more than fifty thousand (€ 50,000.00), but less than four million (€ 2,000,000.00).
- The assets (property) gross in the balance of statement: more than twenty five thousand (€ 25,000.00), but less than one million (€ 1,000,000.00).
- The average number of employees within a financial year: less than 10

Micro-enterprises: are the businesses as following:
- Annual turnover (net): less than fifty thousand (€ 50,000.00);
- Assets (properties) gross in the day of the balance of statement, less than twenty five thousand (€ 25,000.00).

Average number of employees during the financial year: less than 10

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9. Law nr. 04/L-014, 29 July 2011 published by the President of the Republic of Kosovo under decree Nr. DL-018-2011 on 09.08.2011
It is to be mentioned that such a partition is done for the financial reporting, it is the only official partition and there is no other categorization of businesses with any other law or administrative direction.

Based on the research and sample analysis, in Kosovo over 90% of businesses of woman represent micro-businesses. In Serbia, 80% of woman have micro business while in Bulgaria 75% (10).

Nevertheless, during the recent years, there was a significant increase of the economic contribution that business woman could do and this fact in a way has foster and encourage them to start their own business

The businesses where the owners are business woman are 9% only (11), while such a percentage shows in a way the reality of woman entrepreneurs, having in mind the fact that these woman and the entrepreneurship in general may generate income, making a successful transition, which in a way has a direct impact in economic strengthening of woman in Kosovo.

The aspirations of woman may be low because their aim is to start small local businesses in the field of retailing industries and services which provides them some income, but on the other hand allows them to keep a flexibility in regard to their household activities.

1.6. The position and general status of woman entrepreneurs in Kosovo

The position of woman in general in Kosovo is an issue which has been discussed for a long time from both social and political aspect. For a few decades, certain efforts have been done in order to increase the level of inclusion of woman in the society i.e her emancipation in general.

However, despite various challenge that the woman in Kosovo were faced with, in order to reach a higher level of progress which contains challenges such as family patriarchal behavior to terminate attending the education process for woman until the possibility for opening new jobs for woman, today still there is a situation where, although there are laws which support the woman, the law on equal rights between man and woman, woman in Kosovo is not equal with man.

1.7. The profile of entrepreneurs

Woman entrepreneurs in Kosovo are the individuals who have certain wealth and manage with it, i.e. woman who established kind of workshop within which they perform an independent activity and at the same are registered with the municipal authorities or with the Ministry of Trade (prescribed by law), and registered as an agency (regardless the property) in one of these forms:

11. The SOK The number of registered businesses and tax payers of the business woman, 2006 provided by HysniElshani, statistical office with the SOK September 2007. In a few reports, it is mentioned that the business of woman in Kosovo is in total 5-7%. This means that there are not accurate figures on the % of the businesses of woman in Kosovo.
Company with limited liabilities, Partnership company, Stock company and regardless whether they employ new employees or not, providing that they have a managerial legal position. (12)

In Kosovo, woman entrepreneurs are middle aged, coming from both urban and rural areas, with an elementary and secondary level education, mainly married or widowed, with an average economic situation and who have children. Woman entrepreneurs in Kosovo, in terms of their profile, differ from the other woman in the region. It is obvious that a certain number of woman, in particular from the Dukagjini region, are widowed, with certain number of children without their fathers, as a consequence of the last war in Kosovo, since heir husbands have been killed by Serbian police, paramilitary and military forces such as in the village Meja, Krushe etc. In order to grow up their children and support their families were forced to deal, mainly with small business activities such as processing of milk and producing milk products, handicraft, agriculture products etc.

Woman of younger age are mainly oriented in trading activities, personal services (such as hairdressers, cosmetics, tailors as well as in the field of textiles industry and fashion. Woman entrepreneurs in Kosovo have small enterprises which can employ maximum 5-6 employees, mainly woman. Employed workers are mainly family members or relatives.

Their main motivation is employment in the social sector, but also in the private sector, both having a high unemployment rate in Kosovo where it is very difficult to find a job. They have establish the enterprises, not to have a high profit, but only to survive and in order to gain a certain independence. A certain number of these woman have heritage a kind of property or have made various borrowings, starting the activity in a small workshop, while there are less cases when woman have buy properties or have ask for bank loans. In general, such businesses are mainly family businesses.

While business woman were previously employed, and then they established their own businesses, a great deal of business woman in Kosovo have establish their business and got employed, having a limited experience in this field. In the region for example, woman have establish their businesses, based on their previous activities, i.e. they were employed in a certain sector while they have establish the business in the same sector. (13)

1.8. Woman in the rural areas

Woman of rural areas in Kosovo are a very important part and invisible of the work force, because they do rather heavy jobs in the family farms, heavy jobs in their families, who for the moment have e very poor control of the productive resources, due to the fact that just a few of them have land registered on their name.

The failure in increasing the employment of women in rural areas will keep Kosovo as hostage of a vicious circle of non development and rural poverty (14). The majority of women who have a paid employment in the rural areas are working as teachers, sales persons in the family shops, tailors, hairdressers, livestock development and handicraft, agriculture activities, while all these show lack of movement and high level of dependency.

Another problem of women in rural areas nowadays is because women in such areas have less approach in inputs and the technology of farms, bank borrowings and additional agricultural services. These services are mainly oriented to men, often due to the fact that the communication between man and woman in the rural areas currently are not liked (15).

1.9. The perceptions for woman entrepreneurs

The number of businesses run by women in our region is increasing day by day, despite the difficulties that are present in developing business climate. It is obvious that the overall conditions for doing business in Kosovo are quite difficult, for both men and women, while such problems have an impact to business women in particular. Towards Lisbon, United for Children, UNICEF, page 8, 2011 are a real obstacle, especially in our circumstances of poor economy, high unemployment, and poverty, problems that women face with every day, which means that to be a woman entrepreneur in Kosovo is not that easy. While describing the difficulties and problems faced by our women, a problem which should be mentioned in our region is also the problem of high interest rates, lack of financial means and many other problems, changing the perception on women, intending to show that woman is not capable of running a business, a problem that our women entrepreneurs and those who are willing to enter the business face very often, and this problem continues to be an obstacle towards their success.

Even in developed countries there are wrong prejudices about women in general and in particular for businesswoman. Male entrepreneurs would rather enter into financial agreement between them than with women. (16)

There is a prejudice that it is the man only who should take care of the family, it’s him who can be an entrepreneur because he is able to decide and undertake any risk. The surrounding with such perceptions is of the opinion that woman who is successful in business, aims to take the role of her husband at home. In such cases, women is not honored nor respected.

This problem is not an issue among us only, but it is also present in other countries. Antonia Brookman from Ghana shows that there were many occasions when her work was not appreciated only because she was a woman. Further she prescribes a case when she met with one of the clients and showed her product, while the client was very happy, decided to sign a contract but wanted previously to talk to the owner. As soon as he found out that Antonia is the owner, the client said he does not want to buy anything from women and that business which is managed by women is not a serious business.(17)

15. German Development Institute, Gender issues in Doing Business: An analysis using case studies of Ghanaian women entrepreneurs, page 60, November 2009, Germany
16. German Development Institute, Gender issues in Doing Business: An analysis using case studies of Ghanaian women entrepreneurs, page 52, November 2009, German
2. RESULTS OF THE SURVEY OF WOMEN IN BUSINESS IN KOSOVO

In order to show the current situation of the women in business (businesswomen) in Kosovo, I have conducted a survey where 30 business women were included.

The results are rather interesting and show where business women stand in Kosovo and what is the distinction between them and the businesswomen in the region.

2.1. Age of women entrepreneurs in Kosovo

Young women are involved in the business activities because of the difficulties to find a job, while middle aged women are dealing with business in order to fulfill the family obligations.

The age of women entrepreneurs in Kosovo does not differ very much from the age of women entrepreneurs in other countries. Women entrepreneurs in Kosovo belong to all ages, but most of the age group that participated in this survey and are dominating are aged over 40 years, i.e. women of relatively old age while 40 percent of women entrepreneurs are aged over 40 years while in the other two categories of the age of 20-30 and 31-40 years are at the level of 30%.

In Serbia, the age of employees is different from that in Kosovo and Bulgaria. In Serbia, 21 percent of women entrepreneurs are aged 18-28 years old, 49 percent are aged over 50 years old, while in Bulgaria, at the age of 18-28 years are 30 percent of businesswomen and 50 percent aged over 50 years old (18).

2.2. The marital status of women entrepreneurs

Married women have more family obligations, but at the same time have the support of other family members, in particular of the husband, while unmarried women have less family obligations and also less support by their families. This is the reason why the following question was asked:

The marital status of women entrepreneurs in Kosovo has witnessed that over 76% of them are married while 23% are unmarried. This situation coincides with the age of businesswomen in Kosovo.

2.3. Education of women entrepreneurs

In general, the structure of the education level of the respondents is mixed, being emphasized a little more the one of secondary level education. 7 businessmen or 23.30 percent have completed only the primary school, while 7 of them have completed the faculty.

This percentage is slightly disappointing, due to the fact that education is one of the key factors that affect the economic growth, education also helps women farmers to adopt productivity, according to new technologies, get involved in the counseling centers, get the rural credits and invest in income generating activities and many other elements that are not less important.

It is to be mentioned that educational-professional structure of women entrepreneurs varies: In Serbia, 41 percent of women entrepreneurs have higher level education, 16 percent of them have completed faculty, 41 percent have completed secondary level education while one percent only have elementary level education and master degree.

18. Mr. sc. Almir Pestek, Advancing the life quality of women through entrepreneurship, Sarajevo, page 34, 2009
In Bulgaria, 64 percent of women entrepreneurs have completed the faculty or 90 percent of them have more than high school (19)

2.4. **Number of family members**

The highest percentage of women entrepreneurs in Kosovo have over 4 family members or 56.70 percent, with 2 to 4 family members are 33.30 percent and only 10 percent of them have only 2 family members.

A significant percentage of women entrepreneurs with a great number of family members are from the countryside, i.e from the rural areas while less family members have women entrepreneurs living in urban areas.

This is understood since women entrepreneurs in rural areas deal with different agriculture activities which require more work force, while in the urban areas women entrepreneurs have less workers because the work itself is limited with less work force.

2.5. **Type of entrepreneurship**

The highest percentage of women entrepreneurs in Kosovo are of the type of physical person with 66.70 percent, then limited liability companies with 16.70 percent, while the two other forms of business as partnership companies and DPT are from 6.70 per cent, i.e 10.00 per cent respectively.

Women entrepreneurs in Kosovo, in particular in rural areas, very few are aware of the different types of businesses, they deal more with family businesses, in which businesses, family members are employed. There are rare cases when they are registered as a limited liability companies or as stock companies. So, their higher percentage is a private business or natural persons.

2.6. **Duration of business**

The highest percentage of the businesses are new businesses, i.e. less then 10 years and 10 percent of them have a business for more than 10 years. For less than one year have businesses 20 percent of women, 33.30 percent have business from 1 to 5 years and 36.70 percent of them have 5 to 10 years. These data indicate that women with private business have started to deal in the beginning of this century.

In the countries of the region and beyond, the highest percentage of women entrepreneurs have more than 10 years of experience in business and those businesses are sustainable.

2.7. **The location of business development**

Women who deal with business in Kosovo are mainly from town, because 66.70 percent of them run their business in town, while 33.30 percent in the villages - rural areas.

In rural areas, most of the women are involved in producing of agricultural products, deal with the dairy processing industry, with traditional clothing etc., whereas women in towns deal with business in the sector of textiles, services such as hairdressers, tailors etc.
2.8. Premises where women entrepreneurs run their businesses in Kosovo.

A great percentage of businesswomen in Kosovo rent business premises, i.e. 46.70 percent, while 23.30 percent of them run their businesses in private premises or rent the business premises. 70.00 percent of women run their business out of their properties and 30.00 percent of them run their businesses in their homes or their properties. In the cities, women entrepreneurs rent business premises, while in the villages, the business is run and organized mainly in the properties-private family houses.

2.9. Number of employees in the women enterprises

Women in Kosovo have businesses with a very little capacity, while the number of employees in these businesses is small. 43.30 per cent of businesswomen employ 1 to 5 people, 30 percent of them employ from 5 to 10 people and only 16.70 percent of them have over 10 people employed, while 10 percent of them do not have any person employed, because they do all its business services themselves.

About 92 percent of all European Union enterprises are micro-businesses with an average of about two employees in an enterprise. (20)

2.10. Bank balance of women entrepreneurs

In most of the cases, bank borrowings, with very high interests rates makes a real obstacle for the women entrepreneurs in Kosovo to having positive business. Out of 30 interviewed women, bank borrowings received 13 of them or 43.30 percent, while 17 of them or 56.70 percent of them did not have any borrowing.

At the same time, a specific problem for women entrepreneurs in Kosovo is the issue of credit insurance. Banks in many cases not only do hesitate to approve borrowings for women entrepreneurs, but they also have difficulties in providing mortgage. Another obstacle is the issue of ownership, due to the fact that in Albanian families, the owner of the real estate is the husband, so this is the reason why women can not get a bank borrowing and provide mortgage, because the property is not registered in their names. In this case, women can get small amount bank borrowings with very high interest rate, which means that the women entrepreneurs become dependent from their husbands. If the husbands of the women entrepreneurs give a kind of guarantee or allow their house or other property to be left as mortgage, they will then be able to get a bank borrowing.

2.11. Annual profit

The annual profit of women entrepreneur in Kosovo is very low. During a year, 13.30 of them have a profit of € 1.000 while a higher percentage of them make a profit between € 2.000 and € 4.000 while 30 percent of women entrepreneur interviewed have a profit over € 4.000. These figures show that women entrepreneurs in Kosovo mainly deal with micro businesses. In Serbia, among women entrepreneurs, 80 percent of them are women running micro-enterprises, 18 percent small enterprises and only 2 percent large enterprises, in Bulgaria 75 percent of women businesses running micro-enterprises, 23 percent small enterprises and 2 percent large enterprises (21).

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21. w.w.w.tiranaobserver.al/17.7.2013, Women have no access in business and in bank borrowings.
2.12. Customers of products of women entrepreneurs

Customers of products of women businesses come from all areas, but still the local areas have a slight domination in this field, i.e. 46.70 per cent of them do sell their products in these areas, 33.30 percent of them sell their products in the regional areas while 20 per cent of these products are being consumed in all areas. It would be appropriate if the products of women businesses are sold in a wide range market. This will be enabled through different fairs, which luckily is expanding day by day in Kosovo.

2.13. The motives of women entrepreneurs

There are many motives of women entrepreneurs to run a private business. These motives are classified into five categories.

The motives for establishing a business are very much different where 36.70 percent of women run their businesses because they wish to do so and have certain abilities to run a certain type of business, 16.70 of them run their businesses because of difficulties in finding a job, both in private and public sector, 13.30 per cent run their businesses in order to have higher income and 13.30 per cent run their businesses on voluntary basis. Around 10 per cent of women deal with business because they feel they are prepared professionally to run an appropriate business and 10 percent wish to continue a family tradition in the business.

In Serbia, 70 percent of women run their businesses as a result of economic needs, in order to provide the necessary financial resources for their children and their families in general, while in Bulgaria, 36 per cent of them run their private businesses due to economic needs, while for 41 percent of them, the motive to enter into a private business is the wish for strengthening their professional abilities and at the same time to prove that they are capable to perform such activities. (22)

2.14. Decision making of the women entrepreneurs

Since women have establish their businesses and at the same time they run their small or large businesses, it is inevitable that they take decisions. From 30 women interlocutors, 28 of them or 93.30 per cent have stated that they take decisions while running their business and only 2 of them or 6.70 per cent have stated that they do not take any decision in their business.

2.15. Number of members supported by business women

As a distinction from the countries in the region, the number of family members who are dependent from the income of this type of business is higher, despite a reducing tendency of Albanian families which was marked during recent years. Around 50 percent of members are supported by the income of women businesses having from 2 to 4 members, 26.70 per cent of the income by women businesses support at least 2 members and only 23.30 per cent with the income generated from their business support more than 4 members.

2.16. Supporting women entrepreneurs in establishing their businesses

Based on the data presented in this table, it is obvious that 40 percent of women entrepreneurs have had the support of their families, 23.30 per cent of them are supported by their husbands, 16.70 percent by foreign government and non-governmental institutions, 16.70-per cent of women are self-funded and only 3.30 percent from the foundations dedicated for the development of businesses.

22.w.w. cepor.hr/ The strategy of development of women entrepreneurs in the Republic of Croatia, 2009
2.17. Challenges and problems of women entrepreneurs

It is obvious that women entrepreneurs, while running their business activities face numerous challenges and problems which are serious obstacle to the progress of their business activity. They have problems to provide initial financial means they have problems in finding business premises, family problems (lack of care for their children), do not have information and professional staff etc. Lack of initial financial means to start the business is one of the biggest problems faced by all types of businesses, both men to women. Women face serious difficulties than mean, because if such banks do hesitate to approve credits for women entrepreneurs since there is an opinion among the banks that women can not return the credit. This phenomenon is characteristic for all countries of the region and beyond.

Among the countries where banks hesitate to approve credits for women entrepreneurs are Albania (23), Montenegro, Croatia (24), Macedonia, Serbia, Bosnia (25) but also in other European countries.

Beside financial means and family problems, the husbands do hesitate to invest in women businesses for the fact that women have different dilemmas in functioning of their businesses. In particular, due to this reason, 16.70 percent of women entrepreneurs have problems in providing financial means.

Women in Kosovo have also problems in providing business premises in which they would exercise their business. This is a problem affecting 20 percent of women interlocutors. It is easier to find business premises in the villages because they do the business mainly in their own premises, while in urban areas they permanently face such problems. To find suitable business premises, they need financial means, while due to the fact that they operate with limited capacities, employing just a few employees, mainly 3-4, they are unable to build their own premises in the suburbs nor within the cities.

The efficiency of women entrepreneurs makes more difficult also then on loyal products with which they deal. Women have no abilities for manipulation in the field of trade, therefore they suffer because of non loyal competition. Some of these imported products have no value so to make competition in the Kosovo market, but they have lower prices, therefore this way the businesses of women in Kosovo are damaged.

Women entrepreneurs in Kosovo also face with the problem of lack of sufficient business premises in order to run their businesses. In towns, it is very difficult to provide business premises, while the premises in the suburbs are not suitable to run the business, not only for the reason that they are away from the family, but also they face other technical difficulties such as travelling, physical security of the premises, transport cost etc.

Women entrepreneur also face the problem of a variety of goods in the market example women who produce milk or milk products, cheese, yoghurt etc. of the same quality, despite that these are products produced in Kosovo, while other products come from Serbia, Montenegro, Bosnia and Herzegovina, Slovenia, Macedonia etc. The same situation is noted also in other agriculture products such as strawberries, apples, potatoes etc.

23, 24, 25. w.w.w. cepor.hr/ The strategy of development of women entrepreneurs in the Republic of Croatia, 2009
2.18. How satisfied are women entrepreneurs

If women entrepreneurs would have a chance to get employed in the public sector, 20 per cent of them would not run a private business while 23.30 per cent have dilemmas and 56.70 of women would not change the activity in order to take another duty in public or private sector. Women in Kosovo have establish small enterprises, with a small number of employees. Even the small number of employees belong to family members and relatives. So the structure of employed is mainly built, not by people with certain abilities and professional background, but they are more focused on family relationship.

The same situation is with the women in the region and elsewhere. Based on a survey conducted, for example in Finland, women running the private business, did not establish their businesses to employee people but to employee their family members and relatives. While conducting individual interviews with women entrepreneurs, I have concluded that they have limited knowledge in keeping financial records. Since they run small businesses, they are often surprised with the question who keeps their financial records. So, more time is needed in order for them to become powerful business swomen with a sustainable business.

3. CONCLUSION

By studying the issue of businesses in general and women in business, in particular, we have found the need to make some changes in domestic legislation regarding businesses in Kosovo. Women entrepreneurs, in general, we encounter many difficulties which are not peculiar to men in business, so say as follows:

1. Women in business face difficulties since the first step of starting the business, namely the case of borrowing. Real estate and chattels in most cases are owned by men, so in case of seeking loans can not guarantee real estate, ie they can not put on mortgage joint property without the husband. I should be changed (applied) legislation steadfast (legacy), so that women are equal to men in equal inheritance right opposite gender violence;
2. Banks are reluctant to lend because women have doubts loan return safety. Even in this regard must find a way to establish mutual trust as to men and to women, respectively government to subsidize a loan interest rates to women entrepreneurs
3. A major concern of women enterpreuners is the creation of partnerships with men in business. The men willingly establish business partnerships with men than with women, so in this regard should be that women on equal terms prevail.
4. In traditional Albanian families wife is what should take care of children and care for the household. The woman is what must send their children to kindergarten, to care for clothes, for shuttle from kindergarten or school. This is an overload for women and to be equal with men should share equally affairs.
5. Women Entrepreneurship in Kosovo should be stimulated by the state in various forms either create opportunities or stimulation of loans in other forms such as in mitigating exemption from various taxes (at least for a time), placements fairs for their products, manufactured goods advertisement etc.
6. It should be organized as much training from business experts initial women but also for those women who intend to start business. Practice has shown that a large number of women have started off through the preparation and professional training of local non-governmental associations and abroad. In other countries such as Italy, Germany, USA, etc. Supporting women entrepreneurs become institutionally stimulating women financially but also encouraging mentor shaped by accredited programs with 9 months and mentor for one or two years.
7. With the aim of establishing a climate suitable to deal with the state on business activities should simplify procedures for registration of private businesses, because women are
susceptible to technical and administrative difficulties.

8. Women are afraid of the possibility of bankruptcy of the business, so the state would have to guarantee that their products find the market or in any way guarantee their production.

9. Women entrepreneurs are unable to raise the terms of maternity leave. With prewar laws in the eighties women have one year maternity leave with pay, and now with the laws of war maternity leave lasts 3 months with three months free and others with half newsletters, respectively unpaid. This way of financing does not stimulate women for childbirth, i.e., directly affects the birth rate of the general population. Employees, both women and men, are reluctant to admit women at work, especially those updates because tomorrow they will become mothers and will temporarily halt the work. I think it should be extended maternity leave at least 6 months paid and 6 months free.

10. To be successful women in business, among other things should be done adjustment of children in kindergarten children. Number of kindergarten right now in all municipalities of Kosovo is not sufficient for acceptance of all children, whose parents are employed. We must therefore increase the number of kindergarten children with half or whole day stay. This also applies to small cities of Kosovo, but also in larger rural areas.

11. To organize fairs as much because it says a participant in a fair Pristina: come only with the case of the fairs in order to find some connecting thread between buyers and traders. Then fairs become the exchange of experiences of women of the same overall business and product advertising done.

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CLUSTER DEVELOPMENT AND MAPPING PROCESS IN CROATIA

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ABSTRACT
Clusters present a geographical nearby group of interconnected companies and associated institutions in a particular region that stimulates the creation of the innovations and new knowledge. The research stress main importance of cluster conception and their benefits what is very important for countries characterized by large regional disparities like Croatia. Although some institutions know why clusters are important, there is still no adequate cooperation, coordination and no synergy between actors, nor mutual trust between them in Croatia. This paper provides a review of cluster mapping process initiated by the Croatian Government and EU. The main outcome of the review was the recommendation that three “priority” agglomerations are considered for developing into regional or sub-regional clusters in Croatia - manufacture of furniture and wood processing sector, manufacture of parts and accessories for motor vehicles together with associated general engineering sector and manufacture of food.
Keywords: benefits, cluster, Croatia, development, mapping process,

1. INTRODUCTION
Clusters are mesoeconomic units, which are located between micro unit - companies, and macro level, which means levels of national economies. Porter, defines cluster as a geographical nearby group of interconnected companies and associated institutions in a particular area, linked by similarities and complementarities (Porter, 2008). In present global economy which is continuously changing and causing constant threats and challenges, different forms of networking and connecting companies, as well as flexible form of connecting, are becoming more and more important, compared to separate, independent and unconnected enterprises. In different forms of connecting, which are growing more innovative, new platforms of possible economic successes and growth of competitiveness are being created.

Today, there are enough empirical evidences which point that innovation and competitiveness growth are seriously geographically concentrated. Clusters provide a stimulating environment for innovation and knowledge creation. Regions with strong cluster portfolios are innovative leaders, while regions with no clusters or isolated clusters fall behind. Globalization has increased the benefits of strong clusters and costs in regions that fail to develop a clear specialization profile. Strong clusters emerge in open markets where intense rivalry and cooperation coexist. Clusters emerge in regions where competition encourages companies and financial institutions to choose some location for their future activities based on the attractiveness of a particular region and not on artificially created obstacles for cross border trade and investments. Globalization has increased the need to combine strong internal dynamics within the cluster with linkages between other clusters and markets around the world (Porter, 2003).

Regional specialization represents risks, making regions more vulnerable to specific demand shocks or technological shifts. However, the evidence suggests, that a cluster-based regions generate following advantages (Crescenzi, et al., 2007):

- First, the economic costs of lower productivity often occur due to lack of specialization, especially in terms of globally-linked markets;
• Second, dynamic clusters that are open to outside trends better suite to external shocks, by transferring existing skills into new market areas;
• Third, connections and overlapping companies are making trade-off easier between specialization and diversification;
• Fourth, numerous studies show that the most successful regions have a portfolio of clusters.

Considering that clusters are a flexible form – which is constantly changing – of connecting companies and other related institutions and that, with its development assume strengthening of spillovers on others participants and competitiveness growth, are very important for countries (like Croatia) with large regional disparities and disconnection. Their characteristics and multiple influences on competitiveness are a possible warning for all the participants of economic growth to dedicate a special attention on creating and expanding clusters. Clusters development and their influence on competitiveness growth are the main topic of this paper. The important point is that clusters allow their members to be more productive and more innovative than they would be to operate alone. The special emphasis is on cluster development in Croatia and new performed cluster mapping process.

After introduction, the second part of the paper explains cluster conception and their benefits. Further on, it is elaborated how clusters can influence national competitiveness. The third part of the paper presents cluster development in Croatia and forth part provides a review of the mapping process in Croatia. The conclusion includes some proposals for cluster development in Croatia.

2. CLUSTER DEVELOPMENT
Most enterprises all over the world are trying to create clusters. Clusters present the surrounding that stimulates the creation of the innovations and new knowledge. They are the specific kind of enterprise networking and of other supporting agents in specific industries and they strengthen a huge number of economic and non-economic advantages and even social capital in the regions. Regions with powerful clusters represent the regions - leaders of innovations, and the regions with a few isolated clusters, or even, without them, cannot reach such results (Dragicevic, Obadic, 2014, pp. 183).

2.1. Conception of Clusters
The generally accepted definition of business clusters is first stated by Professor Michael Porter (1998):

"Clusters are geographically close groups of interconnected companies and associated institutions in a particular field, linked by common technologies and skills. They normally exist within a geographic area where ease of communication, logistics and personal interaction is possible. Clusters are normally concentrated in regions and sometimes in a single town".

Clusters can be developed either taking the “top-down” or “bottom-up” approach. In the first instance the initiator is Government – regional or national. While in the second one – business is usually the driving force (Dragicevic, Obadic, 2014, pp. 53-54). In the same time, clusters can be either institutionalised or non-institutionalised and they have a positive influence on: innovation and competitiveness, skill formation, information flows and growth, development and long-term business dynamics. They became the “key term” in new development initiatives, strategies and policies in last few years in Europe and in the globalised world (Dragicevic, Obadic, 2014, pp. 184). As Porter, emphasizes many clusters include governmental and other institutions – such as universities, standards-setting agencies, think
tanks, vocational training providers, and trade associations – that provide specialized training, education, information, research, and technical support (Porter, 1998, pp. 78).

Clusters are complex structures or organisations wherever they are located. There is no common model of a cluster. Each has differing objectives, goals and mixes of members (companies, universities, faculties, Regional Development Agencies, R&D centres, Chambers of Economy, etc.). Many clusters offer differing „soft“ non-profit services (networking, lobbying, market intelligence, joint research, organisation of trade fairs) and „hard“ for-profit services, (provision of professional and consultancy services e.g. new product development, common purchasing and sales activities, etc.). They are at different stages of development (i.e. start up, growth, consolidation or decline) and this influences the legal identity adopted (Maxwell Stamp PLC, 2013a, pp. 1). Clusters are considered as a driver for innovation and regional development worldwide. Being networks of companies, knowledge institutions and other stakeholders in a particular industry field, they are complex and dynamic structures which are subject to continuous change. The success of a cluster depends ultimately on collaboration between its different stakeholders which results in new products and services (Lämmer-Gamp, Kergel, pp. 1).

The cluster approach has a natural tendency to be industry- and demand-oriented, whereas the innovation systems approach is concerned with a spectrum of internal issues which complicate the driving forces underlying innovation. The “Triple Helix” concept/model illustrated in next Figure, provides another concept which is partly overlapping and partly complementary with those of clusters and innovation systems (Andersson et al., 2004, pp. 69). The concept is built upon intensive cooperation between the three partners - industry, academia (science) and the public sector. Government and university interact at the initial stage, i.e. conception of an idea. Thereafter university cooperates with business in technology transfer. Eventually, a final product is commercialized in the market by joint effort of government and business (Etzkowitz, 2012; Etzkowitz and Leydesdorff, 1995).

![Figure 1: Clusters and the Triple Helix Concept (Maxwell Stamp PLC, 2013b, pp. 2)](image)

The “triple-helix” model is the key growth generating wheel – businesses cooperating with R&D, R&D cooperating with the government, government cooperating with businesses, and

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164 The Triple Helix theory was devised in Great Britain and Holland in the early XXI century by professor of Newcastle University Henry Etzkowitz and professor of the University of Amsterdam Loet Leydesdorff. The Triple Helix symbolizes a union between government, business and university, which are the key elements of innovative system in any country. Retrieved 21.01.2015. from http://www.tusur.ru/en/enterprise/triple-helix/
finally most importantly businesses cooperating with other businesses – who are also sometimes competitors, known as “coopetition”. One of the main motors is the synergy which results from the typology of partners it involves. The “triple-helix” model encompasses business sectors, representing core-activity and accompanying support activities, public authorities, potentially representing also different levels of government, and the scientific and research community (Maxwell Stamp PLC, 2013b, pp. 2).

2.2. The Benefits of Clusters Development and Cooperation

Clusters require a new way of thinking on national, regional and local economies. In the European Union the cluster policy becomes the important component of economic policy. This is specially emphasized in the Lisbon strategy and in the European strategy: Europe 2020. In the European Union it is considered that cluster development is correlated with prosperity and the competitiveness growth in some country (European Commission, 2007), and according to this, cluster and cluster policies have a huge importance for further growth (Dragicevic, Obadic, 2013, pp. 106). Cluster benefits come at three levels: individual firm level, sector/regional level and the wider national level.

Clusters are important because they create tangible economic benefits. The benefits of a cluster come in three dimensions (Porter, 1998):

- Firstly, companies can operate with a higher level of efficiency, drawing on more specialised assets and suppliers with shorter reaction times than they would be able to in isolation.
- Secondly, companies and research institutions can achieve higher levels of innovation. Knowledge spillovers and the close interaction with customers and other companies create more new ideas and provide intense pressure to innovate while the cluster environment lowers the cost of experimenting.
- Thirdly, the level of business formations tends to be higher in clusters. Start-ups are more reliant on external suppliers and partners, all of which they find in a cluster. Clusters also reduce the costs of failure, as entrepreneurs can fall back on local employment opportunities in the many other companies in the same field.

In their research Dragicevic and Obadic highlight the essential benefits that cluster bring its members. These are (Dragicevic, Obadic, 2013, pp. 18):

1) Better access to employees and suppliers;
2) Access to specialized information;
3) Complementarity;
4) Access to institutions and public goods;
5) Better motivation.

Furthermore, they emphasize that the benefits of the cluster cooperation include (Dragicevic, Obadic, 2013, pp. 18):

- lower transaction costs what leads to faster decisions, greater innovation, better customer service and more efficient use of resources, and
- more effective public decisions on infrastructure, education and financial sources.

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165 The Lisbon strategy for growth and jobs was launched in 2000 as a response to globalisation. The idea is for the EU and its member countries to cooperate on reforms aimed at generating growth and more and better jobs by investing in people's skills, the greening of the economy and innovation. Retrieved 20.01.2015. from http://ec.europa.eu/archives/growthandjobs_2009/objectives/index_en.htm

The Short Guide to Cluster Formation made by Maxwell Stamp also recognises main benefits from doing business as part of a cluster (Maxwell Stamp PLC, 2013b, pp. 7-8) – market expansion; increase of productivity, better access to credits with better loan conditions (e.g. lower interest rates); access to development funds; joint development of product through joint investments; cost cuts due agglomerated supply; opportunity to appear jointly on third markets, ability to access the third markets due to the possibility of joint promotion and ability to satisfy quality and quantity related request and decrease of cost related to joint introduction of relevant international standards, etc.

2.3. Cluster Development and Competition

Nations and regions are struggling to remain competitive and adapt in the context of globalisation. The public sector response put an increased attention to the importance of linking firms, people and knowledge at a regional level as a way of making regions more innovative and competitive. This new approach is visible across a number of different policy fields. Evolutions in regional policy, science and technology policy and industrial/enterprise policy are converging on the objective of supporting these linkages at the regional level. One of the vehicles commonly used to achieve these goals is to support “clusters” (concentrations of firms and supporting actors) in a particular region (OECD, 2007, pp. 1). Competition in today's economy is far more dynamic. Clusters affect competitiveness within countries as well as across national borders. Therefore, they lead to new agendas for all business executives – not just those who compete globally. More broadly, clusters represent a new way of thinking about location, challenging much of the conventional wisdom about how companies should be configured, how institutions such as universities can contribute to competitive success, and how governments can promote economic development and prosperity (Porter, 1998, pp. 78).

It is important to stress that clusters simultaneously stimulate competition and cooperation. In such way, competition can coexist with cooperation because they occur on different dimensions and among different players. According to Porter, clusters affect competition in three broad ways: first, by increasing the productivity of companies based in the area; second, by driving the direction and pace of innovation, which underpins future productivity growth; and third, by stimulating the formation of new businesses, which expands and strengthens the cluster itself (Porter, 1998, pp. 80).

Clusters are an extremely effective development policy of country’s competitiveness. At first they appear as "islands" of competitiveness and with subsequent development multiply competitiveness in the country (Garelli, 2006). The important point is that clusters allow participants to be more productive and more innovative than they would be to operate alone. In his updated and expanded book On Competition, Porter (2008b) points out that clusters affect competitiveness in three ways:

1. increase the competitiveness of the enterprises located within the cluster;
2. leading and pointing out the path of innovation that support the future growth of productivity;
3. by stimulating the creation of new businesses that expand and deepen cluster itself.

The cluster allows benefit to each member because it has a much greater range of possible business and other activities since it formally partnered with others, without being required to give up its own flexibility. In such way, clusters can contribute to an increase in economy-wide competitiveness by facilitating policy reform, fostering private-public dialogue and becoming a catalyst for wider private sector development initiatives (Maxwell Stamp PLC, 2013c, pp. 10). In countries which are characterized by large regional disparities and disconnection cluster development is very important for economic growth.
3. CLUSTER DEVELOPMENT IN CROATIA

Although an amount of work has been done on clustering in Croatia more work is required to control the power of clusters and clustering as an economic and regional development tool. Croatian enterprises frequently lack critical mass, they suffer from an absence of trust, connections to local “knowledge and talent providers” and confidence especially at the local level. With its cluster policy Croatia wants to strengthen existing regional advantages, and thereby competitiveness and innovation. In general, throughout the Europe it is considered that clusters are largely associated with prosperity and growth competitiveness (European Comission, 2007) so that is the reason why the development of clusters and cluster policy is of great importance for Croatia.

According to some data, there are over eighty clusters in Croatia (Maxwell Stamp PLC, 2013d). Although the time period of their existence is relatively short, it is evident that in most cases these are latent clusters or those who have not created "fertile ground" for development, and they disappeared. Many are called cluster, but are substantially shallowly connected horizontally or vertically. The full content of the cluster means a horizontal and vertical, and/or diagonal connection.

This means that there have to be a team with scientific and research organizations, and not only with the same type of companies. The idea in the cluster concept is in the cluster heterogeneity and connectivity from which occur innovation, knowledge spillovers and information and encourages the growth of competitiveness. If this is achieved, then this is a cluster, in his essential meaning. On the Croatian language word cluster is commonly translated as a cluster or a group of identical items. If we take it just like that, we can really conclude that it has a multiple connections (Dragicevic, Obadic, 2014).

Greater cluster’s development in Croatia came just after 2006, while the beginnings of the development date back to the year 2001. Different initiatives from many governmental institutions for cluster development in Croatia were carried out between 2004 and 2011 (Dragicevic, Obadic, 2013, pp. 145). The most important document which defines cluster policy in Croatia, Cluster Development Strategy in the Republic of Croatia 2011-2020, was adopted in April 2011167. The Strategy encompass the strategic plan and implementation process for building and maximising the benefits of clusters as major contributors to national innovation and growth in Croatia. Its sets out six main areas for future strategic development of Croatian clusters (Vlada Republike Hrvatske, 2011, pp. 12):

- improving the management of Croatian cluster development policy
- strengthening of clusters and cluster members
- promoting innovation and transfer of new technologies
- strengthening of export potential and internationalisation of clusters
- strengthening the knowledge and skills for cluster development
- effective use of EU funds and EU Community Programmes.

Unfortunately, in our earlier research we found out that the level of coordination and networking among all the government bodies both at national and regional level does not exist. At the same time, a small number of existing clusters has no real support for its further development. A huge disparity in competitiveness level among counties and regions in Croatia still exists (Dragicevic, Obadic, 2014).

According to current policy, a wide range of new and existing clusters in various sectors were promoted and encouraged in recent years in Croatia. Substantial financial support was provided to these clusters. In the seven years (2007-2013) Croatia supported 46 clusters involving 604 companies with 35 million Kuna. Some clusters are active only in the region or

167 The Strategy was developed by the former Ministry of Economy, Labour and Entrepreneurship at the 125th Government meeting held on 28th April 2011 (Vlada Republike Hrvatske, 2011).
local area where they are located and some work nationally and internationally. Next table shows the most common examples in Croatia.

Table 1: Examples of Clusters in Croatia (Maxwell Stamp PLC, 2013d, p. 7)

<table>
<thead>
<tr>
<th>Food</th>
<th>Apple</th>
<th>Plum</th>
<th>Honey</th>
<th>Wine</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tourism</td>
<td>Medical</td>
<td>Small Hotels</td>
<td>Leather/Textiles</td>
<td>Wood</td>
</tr>
<tr>
<td>ICT</td>
<td>Automotive</td>
<td>Metal processing</td>
<td>Agri Machinery</td>
<td>Bio-energy</td>
</tr>
<tr>
<td>Transport/Logistics</td>
<td>Ship Building</td>
<td>Construction</td>
<td>Interior Design</td>
<td>Semi-conductors</td>
</tr>
</tbody>
</table>

The primary focus of recent policy has been to encourage all types of clusters without setting criteria to distinguish their capacity to contribute to growth and be sustainable organisations over the long term. Although the development of clusters in Croatia has its ups and downs, clusters certainly have their future as a part of the Croatian economy. This was recognized by the Croatian Government and EU which have jointly funded the “Support for Cluster Development Project”, and part of which was also benchmarking process (Maxwell Stamp PLC, 2013a, pp. 14).

At the beginning the Ministry of Economy, Labour and Entrepreneurship and Crafts was responsible for cluster development and from 2012 that is the Ministry of Entrepreneurship and Crafts. Currently, the Ministry of Entrepreneurship and Crafts is the responsible ministry for national cluster development strategy and will therefore seek to ensure distribution of information on strategy implementation to all other relevant and participating ministries, clusters and agencies as well as the wider public (Maxwell Stamp PLC, 2013d, pp. 5). The Project “Support for Cluster Development Project” was financed by IPA (Instrument for Pre-Accession assistance) IIIC project for a 2007 – 2013. period.

This project identified the sectors in the regions of Croatia, made the guidelines of national development cluster, established three pilot regional clusters of competitiveness in the agro-food, automotive and wood processing sector, training of cluster managers was conducted, local/regional stakeholders and other interested parties in order providing support and dissemination of knowledge. Also, an analysis of existing cluster initiatives has been made and guidelines for the development of potential areas for business development in Croatia have been provided\(^\text{168}\). As part of these project eighteen different documents in the form of analysis and reports have been made. Until than cluster mapping\(^\text{169}\) was still not carried out. Developing the “Cluster Mapping Report” in Croatia is a pioneering work, because it identifies and recommends clusters which hold the greatest potential for development. Therefore, next section provides a review of the mapping process in Croatia which is a precondition for successful implementation of Croatia’s Cluster Development Strategy (2013-2020).

4. CLUSTER MAPPING PROCESS IN CROATIA

The Report on Cluster Mapping took two approaches for identification and recommendation of clusters which hold the greatest potential for development. In first part, three-star mapping

[^168]: Retrieved 27.01.2015, from the web site of Ministry of Entrepreneurship and Crafts: \[http://www.minpo.hr/default.aspx?id=423\]

[^169]: The aim of mapping is to provide an overview of existing clusters and their relationships, which will serve as a basis for defining the appropriate future activities within the Cluster Development Strategy (Dragicevic, Obadic, 2013, pp. 151).
is used to identify those clusters which hold most importance for the Croatian economy. The second part provided an analysis of the over 80 clusters which Ministry of Economy, Labour and Entrepreneurship (MELE) and other organisations have funded across Croatia since 2008. As part of the cluster mapping process, this project sought to analyse the current situation of these clusters, in order to assess whether they were still active and if they were growing or decline, so as to ascertain whether any of them could be developed into more dynamic clusters, particularly alongside the agglomerations identified under the three-star mapping exercise (Maxwell Stamp PLC, 2011, pp. 5-6).

The three star agglomeration mapping process found a total of 138 (28 three-star, 21 two-star and 89 one-star) agglomerations cross the 21 Croatian NUTS III regions/counties (Maxwell Stamp PLC, 2011, pp. 11-13). The next maps show the overall distribution of three and two star agglomerations at the three NUTS II Region in Croatia.

![Figure 2: Map of Three and Two Star Agglomerations Pannonian NUTS II Region (Maxwell Stamp PLC, 2011, pp. 12)](image)

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170 The mapping of „agglomerations“ is based on the „three stars“ methodology developed and utilised by the European Cluster Observatory for mapping and assessing clusters.

171 Those sectors at the regional level reaching 10% of the total sectoral employment at the national level received one star. If a NACE sector in a particular NUTS II or III region represents more than 3% of a region’s total employment then a two star rating is awarded for that sector. If a sector satisfies both criteria: dominance and size, it is awarded three stars (Maxwell Stamp PLC, 2011, pp. 7-8).
Previous agglomeration maps show a mix distribution of economic sectors across the country. However, the NUTS II regional distribution of three and two stars is dominated by two sectors, construction and tourism. Construction of residential buildings (F41.2) is a dominant sector with ten two star and one three star agglomerations spread across the three NUTS II regions, showing high sectoral specialisation in most counties. A second dominant sector for both three star and two star agglomerations is Hotels and similar accommodation (I55.1) with four three-star and two-star agglomerations, all located in the NUTS II Adriatic region. Of the remaining three and two star agglomerations in the Adriatic region the most significant is building of ships and boats (C30.1) with three-star agglomerations in the Adriatic NUTS II region. Northwest is “home” to a series of traditional sectors, notably C10 manufacture of food products (C10) with 2 agglomerations, with a specialisation in meat products. The sector shows high sectoral specialisation and records increases in both the employment and export index (Maxwell Stamp PLC, 2011, pp. 13-14).
The outcome of the review of the Cluster Mapping Report, was the recommendation that three “priority” agglomerations are considered for developing into regional or sub-regional clusters (see Table 2).

**Table 2: Recommendation for developing into regional or sub-regional clusters**

(prepared according to Maxwell Stamp PLC, 2011, p. 55)

<table>
<thead>
<tr>
<th>Agglomerations</th>
<th>Argumentation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Manufacture of furniture (C31) and wood processing sector (C16) for North West Croatia</td>
<td>- given the strengths of both sectors in the region’s economy and the existence of a “top ten” cluster that could be utilised to act as the lead organisation in the development of the cluster</td>
</tr>
<tr>
<td>2. Manufacture of parts and accessories for motor vehicles (C29) together with associated general engineering sector in Adriatic Croatia</td>
<td>- based on the existing motor parts and components agglomerations identified in Istria, as well as the presence of engineering related agglomerations in neighbouring combination ○ there is potential for collaboration among 3 existing automotive clusters (ADKlaster, ACH autocluster and Auto Cluster Croatia) who could act as lead organisations for the development of the cluster</td>
</tr>
<tr>
<td>3. Manufacture of food in eastern counties of Pannonian Croatia</td>
<td>- given the high concentration of crop and animal production (A1) agglomerations together with manufacture of food (C10) agglomerations, especially in Osijek-Baranja County</td>
</tr>
</tbody>
</table>

Other potential agglomerations identified during the review for possible development into clusters was the combination of the two pharmaceutical agglomerations in Zagreb county and in Koprivnica-Križevci County into a single cluster. Similarly, the alternative energy sector has been identified as a sector with high potential. It is felt that Croatia has the right combination of natural resources (e.g. sun, sea, wind, etc.) alongside a range of existing sectors such as ICT, advanced engineering and electronics which could be linked effectively to the alternative energy sector. Finally, the importance of ICT for all sectors was acknowledge by Cluster Mapping Report and it was decided that this economic sector should be incorporated into all recommended clusters rather than supporting it as one of the pilot clusters (Maxwell Stamp PLC, 2011, pp. 55).

5. **CONCLUSION**

The paper carries many empirical evidences which stress that clusters stimulates the creation of innovations and new knowledge. They create tangible economic benefits – higher level of efficiency, knowledge spillovers, better access to employees and suppliers, synergy, complementarity, access to institutions and public goods etc. That is very important for countries with large regional disparities and disconnection, like Croatia.

During the last decade, there were significant efforts of different ministries, associations and some regional development agencies for some initiatives on cluster development in Croatia. Although some institutions know why clusters are important, there is still no adequate co-operation, coordination and no synergy between actors, nor mutual trust between them.

This paper elaborates and emphasizes the importance of “Support for Cluster Development Project” (SCDP) finally initiated by the Croatian Government and EU. Within the framework of this project “Cluster Mapping Report” in Croatia was designed. This paper provides a review of this process. The main outcome of the review was the recommendation that three “priority” agglomerations are considered for developing into regional or sub-regional clusters in Croatia - manufacture of furniture and wood processing sector, manufacture of parts and
accessories for motor vehicles together with associated general engineering sector and manufacture of food.

**LITERATURE**


Section 3
Entrepreneurship Caught Between Creativity and Bureaucracy
HOW TO INTEGRATE ENTREPRENEURSHIP EDUCATION AND CREATIVITY INTO A BUREAUCRATIC ENVIRONMENT (CASE STUDY)

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ABSTRACT
Research has revealed that there is a positive correlation between entrepreneurship and economic growth. As a consequence, the European Commission is taking action on enhancing entrepreneurship and recommends appropriate entrepreneurship training in schools and higher education. Besides other factors, entrepreneurship education is often characterised by creativity, problem solving, interdisciplinarity and practice orientation. With respect to these aspects, universities might not be the right environment to launch an education for entrepreneurship and creativity. They are often inflexible institutions characterised by bureaucratic structures, laborious decision processes, and highly regulated procedures. Although they should teach entrepreneurship and creativity, they are caught up in bureaucracy and stagnancy themselves. Nevertheless, universities are obliged by government to contribute essentially to entrepreneurship education.

In this case study, we examined the integration of entrepreneurship education under the challenging circumstances mentioned above. The university in this case study is home to more than 32,000 students and 4,000 employees, 6 faculties, 76 departments, and about 120 study programs. Due to cooperation with other institutions, about 60,000 students are allowed to participate. The program in this study provides basics in management, entrepreneurship and intrapreneurship to increase general employability and to promote creativity, interdisciplinary thinking and entrepreneurial acting. The findings of our study indicate the importance of a setting that allows students to participate irrespective of their discipline or the progress in their studies. Moreover, it seems advantageous that students can customise the program according to their specific needs. The importance of flexible integration into regular academic studies has to be emphasised. In this study, we provide an adequate solution to master this challenge in a bureaucratic environment.

Keywords: bureaucracy, entrepreneurship education, integration, university

1. INTRODUCTION
Europe's new companies alone, particularly small businesses, generate more than four million new jobs every year (European Commission, 2013). In response to the growing importance of these companies, the European Commission is taking action on enhancing entrepreneurship in Europe. According to the European Commission, "entrepreneurship refers to an individual's ability to turn ideas into action. It includes creativity, innovation and risk taking, as well as
the ability to plan and manage projects in order to achieve objectives.” (European Commission, 2005, p. 17, 2006, p. 4). Education should therefore develop awareness of entrepreneurship from primary school to university. Introducing young people to entrepreneurship triggers their initiative and helps them to be more creative and self-confident (European Commission, 2006).

When considering the requirements of modern entrepreneurship education the question remains whether universities are the best choice for implementation. They are often inflexible institutions characterised by bureaucratic structures, laborious decision processes and highly regulated procedures. In other words, although these institutions should teach entrepreneurship and creativity, they are often caught up in bureaucracy and stagnancy themselves.

The aim of this paper is twofold. Firstly, we examine the main characteristics of entrepreneurship education at universities. For this purpose, we present a short overview of relevant literature and structure the findings to elaborate the main aspects. Secondly, we analyse the situation at the investigated university and show how entrepreneurship education and teaching for creativity was implemented in a bureaucratic environment. In this section, we examine the most important factors regarding structure, integration and content.

2. ENTREPRENEURSHIP EDUCATION AND CREATIVITY

The relevance of entrepreneurship education has been growing ever since the first entrepreneurship class was held in 1947 in the USA, and especially from the 1980s on, when Drucker’s *Innovation and Entrepreneurship* was published (Drucker, 1985; Katz, 2003). In literature, there is a consensus that entrepreneurship can be taught and there is evidence that entrepreneurial attributes can be positively influenced by entrepreneurship education (Gorman, Hanlon, and King, 1997). It impacts students’ awareness of entrepreneurship as an alternative career path to employment and provides them with skills needed to start and successfully run their businesses (Gorman et al., 1997; Slavtchev, Laspita, and Patzelt, 2012). In contrast, there is also some research indicating that entrepreneurship education does not have the intended effects. For example, Oosterbeek, van Praag, and Ijsselstein (2010) discovered that the intention to become an entrepreneur could even be negative. They argue that this could be due to the more realistic self-perception of students and the following decrease in optimism that they can start a successful business on their own.

Bae, Qian, Miao, and Fiet (2014) define entrepreneurship education as education for entrepreneurial attitudes and skills and entrepreneurial intentions as a desire to own or start a business. In accordance, Jones and English (2004) describe entrepreneurial education as the “process of providing individuals with the ability to recognise commercial opportunities and the insight, self-esteem, knowledge and skills to act on them” (p. 416). Literature emphasises different key aspects in entrepreneurship education. Based on our literature review, entrepreneurship education should imply the following four parts:

**Professional skills.** Entrepreneurship education should provide (theoretical) management and entrepreneurship knowledge. Students should be able to manage a company, therefore it is necessary to teach them basic skills in traditional business disciplines, e.g. management, marketing, controlling, finance and accounting (Jones and English, 2004). At best, they also learn the basics about business environments and get some insights in macroeconomic correlations. A proper theoretical education will enable them to assess opportunities and threats as well as strengths and weaknesses of their business ideas. Many authors propose a mixture of professional competences and soft skills. For instance, Vesper and McMullan (1988) demand knowledge-based courses about entrepreneurship and functional core areas as
well as skill-building courses and practice. Similarly, Plaschka and Welsch (1990) postulate that entrepreneurship education should include theory-based practical applications on the one hand, and creativity, multi-disciplinary and process-oriented approaches on the other.

**Behavioural and attitudinal competencies.** This leads us to the second part of proper entrepreneurship education, which refers to skill-building courses. This category covers all aspects of soft skills such as personality traits, communication, language, personal habits, and social manners. But it also includes competences that are more entrepreneurship-specific, like opportunity recognition, opportunity assessment, negotiation, leadership, risk management, conveying a compelling vision, commercialising a concept, value creation with new business models, marshalling resources, resource leveraging, guerrilla skills, focussing, tenacity resilience, self-efficacy, and building and using networks (e.g. Jones and English, 2004; Morris, Webb, Fu, and Singhal, 2013).

Many authors advocate courses in creativity, creative thinking, and creative problem solving (Morris et al., 2013; Plaschka and Welsch, 1990; Solomon, Yar Hamidi, Wennberg, and Berglund, 2008; Vesper and McMullan, 1988). Amabile (1997) defines creativity as the “production of novel and appropriate solutions to open-ended problems in any domain of human activity” (p. 18) and entrepreneurship as the “successful implementation of creative ideas to produce a new business, or a new initiative within an existing business” (p. 18) and therefore entrepreneurial creativity as “the generation and implementation of novel, appropriate ideas to establish a new venture” (p. 20). In that context, Solomon et al. (2008) found that exercises in creativity can be used to raise the entrepreneurial intentions of students in entrepreneurship education.

**Practice.** Another very important point is practice. Literature suggests a vast field of practice-orientated activities, like working in start-ups, writing business plans, meeting entrepreneurs, simulations, videos of new venture start-ups, role play, and business games (e.g. Clouse, 1990; Vesper and McMullan, 1988). Neck and Greene (2011) suggest starting businesses as coursework, serious games and simulations, design-based thinking, and reflective practice as new methods in entrepreneurship education. Rasmussen and Sørheim (2006) also state the relevance of learning-by-doing activities in a group setting and a network context. Jones and English (2004) demand a teaching style that is action-oriented, encourages experiential learning, problem solving as well as project-based learning, and is supportive of peer evaluation.

**Awareness and self-assessment.** The last part of entrepreneurship education is about awareness and self-assessment. This part is for some reasons crucial, as it allows students to discover their specific abilities, informs them about career options, and teaches them to assess which career – entrepreneur or manager – is most suitable for them (Graevenitz, Harhoff, and Weber, 2010). Research is ambiguous regarding the effects in this matter. On the one hand, some results suggest that initially undecided students are most likely to change their beliefs when attending an entrepreneurship class (Graevenitz et al., 2010). On the other hand, Slavtchev et al. (2012) show a positive effect of entrepreneurship education on students’ intentions to become entrepreneurs in the long term (after some time in paid employment), but a negative effect on their intentions in the short term (immediately after graduation). This could be due to the fact that entrepreneurship education provides more realistic perspectives on what it takes to be an entrepreneur (Oosterbeek et al., 2010; Slavtchev et al., 2012).
3. BUREAUCRATIC ENVIRONMENT

In this section, we take a short look at universities, which are often obliged by government to contribute essentially to entrepreneurship education. The European Commission (2006) has also recommended fostering entrepreneurship in higher education and including entrepreneurship as an objective of education into curricula. Entrepreneurship should be embedded into curricula across all levels of education before the end of 2015 (European Commission, 2013).

But with respect to the above mentioned characteristics of entrepreneurship education, universities might not be the right environment to launch education for entrepreneurship and creativity. There are some obstacles that could interfere with these efforts:

- **Bureaucracy**: Universities are often bureaucratic institutions. They have standardised rules related to curricula, courses, lecturers, and content as well as the kind of teaching. These rules are defined in numerous laws and can restrict the options for a modern and unconventional education for entrepreneurship or creativity.

- **Decision-making**: Complicated and lengthy procedures often stop novel approaches even before they get started. Strong support from opinion makers is required to overcome laborious decision processes and bureaucratic barriers.

- **Structures**: Universities are characterised by inflexible structures. This problem is twofold. On the one hand, there are long-established departments and staff members who fear to lose their vested rights. On the other hand, there are strict rules for curricula that complicate the establishment of entrepreneurship education within these programs. For both reasons it is hard to implement interdisciplinarity that is strongly needed in entrepreneurship education.

- **Financing**: The unpleasant nature of budgets is that they are restricted. If somebody gets more money, another one will get less. This “mechanism” interferes with new disciplines and, due to distribution battles, limits them in their development.

- **Academia**: The scientific world is characterised by objectivity, accurateness, prudence, standardised methods, projectable procedures, and theoretical issues. Entrepreneurship focuses on practical issues, a high factor of unpredictability, exceptional methods, emotions, creativity, and courage. This should not be misunderstood: creativity, for example, is just as important for academia as accuracy for entrepreneurship. They are not opposite poles, but often choose opposite approaches.

These issues have to be considered when implementing entrepreneurship education and appropriate actions have to be taken subsequently. Problems that affect the quality of entrepreneurship education and influence the entrepreneurial mindset have to be prevented.

4. CASE STUDY

In this section we analyse the situation at the investigated university and elaborate the most important factors regarding structure, integration and content of entrepreneurship education at an institution that meets the above mentioned aspects.

**Preconditions and objective of the program**

The location in this case study has more than 275,000 residents and about 60,000 students at eight universities or colleges of higher education. The investigated university itself is home to about 32,000 students and 4,000 employees, 6 faculties and 76 departments, offering more than 120 study programs.

The situation is characterised by a low affinity to entrepreneurship as a possible way to create one’s own future. Only a very small number of students considers becoming an entrepreneur.
Entrepreneurship education in the region faces challenges such as complex study law rules, a conservative mindset with regard to a “traditional” career, and fear of failure. Furthermore, the universities and disciplines have different cultures and socialisations. To counteract these problems, the universities at the site and a local academic incubator established an inter-university program called TIMEGATE. The project name TIMEGATE stands for Transfer Initiative for Management and Entrepreneurship Basics, Awareness, Training and Employability. TIMEGATE provides essential basics about entrepreneurship and intrapreneurship to increase general employability and promote interdisciplinary thinking and acting. It is the answer to the challenge of creating a regional entrepreneurship ecosystem.

Specific objectives are:
- to position entrepreneurship as a bridge and crosscutting issue for students of all disciplines and to break down bureaucratic structures between universities,
- to integrate entrepreneurship into relevant networks at the site and to use regional advantages (young, well-educated environment, comprehensive industry spectrum),
- to develop an independent and formative mindset and to ensure entrepreneurial thinking and acting within the organisation,
- to provide practically oriented content through external experts and enable students to learn from managers and entrepreneurs.

The whole program, which is free of charge for students, is funded by the involved universities and the Ministry. The latter provides extra funding for this cooperation between universities. This additional budget is very important for acceptance within the universities because it highlights the relevance of entrepreneurship education for the Ministry while avoiding distribution battles involving traditional programs and departments at the same time. For this reason, decision processes could be accelerated, enabling rapid compilation of the fundamental structure of the program with the support of university administration.

**Structure of the program**
In the program’s development phase, it was necessary to decide how profoundly the program should be integrated into existing study curricula. Due to the fact that many legal and administrative regulations would have limited the program, it was decided to integrate it by means of elective courses, which are available and open to all students of the participating universities. Since all curricula require elective courses amounting to nine or more ECTS, it is possible for students to integrate entrepreneurship education into their regular studies and to attend courses without “losing” time. Furthermore, students can participate irrespective of their studies and academic progress. Students can acquire certificates to formally confirm qualifications for the labour market. Those certificates still have numerous options to choose from, but also require the completion of certain obligatory courses.

**Content of the program**
The program consists of two certificates (Figure 1). The Basic Entrepreneurship Certificate includes three courses with one ECTS each. Building on the Basic Entrepreneurship Certificate, it is possible to earn an Advanced Certificate in which students can deepen content and can set individual priorities according to their own needs. For the Advanced Certificate it is mandatory to finish the Basic Certificate first. Furthermore, it is necessary to choose between the School of Creativity and the Garage. The former is designed for students without a concrete business idea to learn creativity techniques. In the latter, the students can refine their business concepts or work on their start-up. Additionally, students have to
complete three more elective courses based on their needs (Figure 1: Individual courses). Over 30 courses are available in three major fields. Firstly, there are core business courses such as accounting, financing, marketing, leadership and management, and secondly, courses for e.g. soft skills, personality, psychology and creativity. Thirdly, the final part focuses on practical insights in specific branches of industry, for example pharmacy, health, and manufacturing. The lecturers are mostly experts with practical experience. They provide relevant knowledge in their areas and ensure practical relevance in teaching.

According to the literature review, entrepreneurship education should target professional competences as well as behavioural and attitudinal competencies, practice, awareness and self-assessment. The program focuses on the following aspects:

- **Professional skills:** The Business Administration Basics and Entrepreneurship Basics courses, in particular, provide fundamental knowledge. Furthermore, students can attend core business lectures when they have to select their individual courses in the Advanced Certificate. The aim is to give interested students useful tools for an upcoming start-up phase.

- **Behavioural and attitudinal competencies:** The School of Creativity course enables students wishing to start a company to independently learn application-oriented techniques and methods for a structured development of start-up and business ideas. Students should get insights into creativity techniques and learn which concepts and methods are primarily used in economy and practice. More courses focusing on soft skills and personal competences are available in the context of the individual courses they have to choose.

- **Practice:** The whole program provides a high level of practice orientation. One special course is the Garage. Students apply preliminarily suggesting their ideas and providing an executive summary. After their successful admission to the Garage, students are accompanied by experienced mentors. They work in interdisciplinary teams for one semester to develop their
own business models. Workshops on storytelling, legal basics, design thinking and e-business are currently available. The course defines basic aspects related to starting a venture. The 18 mentors form a key part of the course. They can be booked within the semester for coaching sessions and advise on issues such as marketing, sales, design or even financing and software development. Through individual and personal coaching, open questions are handled competently and quickly.

- **Awareness and self-assessment**: This program leads to a better view of entrepreneurship as a very important topic. The main point is that it is not limited to business students. Because of the collaboration of local universities, it ensures that students of all disciplines become aware of entrepreneurship as a possible career option. The program will enable them to better assess themselves and their business ideas. Students learn about their strengths and weaknesses and find out whether they are qualified as an entrepreneur or not. Events such as panel discussions with entrepreneurs or start-up cafes lead to a higher awareness and complete the program.

### Specifics of the program

This case study provides some important insights for the implementation of an entrepreneurship program at university. The following issues characterise the project:

- Collaboration between universities on the site enables entrepreneurship education for all disciplines and not just for the obvious ones. That not only provides an interdisciplinary approach, but ensures that all students become aware of this career option.
- Integration into curricula through elective courses allows students to attend the program without losing time doing their regular studies, irrespective of their academic progress. Furthermore, this approach avoids bureaucratic obstacles, opens up flexibility in implementation, and also allows for creative solutions, as it is not necessary to adapt curricula with regard to their content or extent.
- The program can be tailored to the personal needs of the students, as it offers a high number of optional courses. Hence, students can focus on their business ideas.
- Universities position themselves as partners and support the students before, during and after the founding. Network effects and synergies are used by integrating non-university partners.
- A high level of practice within the program ensures relevance for the economy.
- Entrepreneurship education is a pillar of university policy.

### 5. CONCLUSION

The economic relevance of entrepreneurship has increased constantly, and as a result, political decision makers in Europe and the United States have started to make increased efforts to foster entrepreneurship at schools and universities. Literature reveals that proper entrepreneurship education should include professional skills (basic knowledge in core areas of management and entrepreneurship), behavioural and attitudinal competencies (e.g. soft skills, creativity, opportunity recognition, negotiation), practice (hands-on activities, e.g. business planning, starting an own business, interaction with start-ups), and courses for awareness building and self-assessment. The latter point is not only important for drawing attention to an entrepreneurial career, but also for identifying and filtering those students with the highest potentials. In that sense, it can protect students from choosing the “wrong” career. Accordingly, there is evidence that entrepreneurship education does not necessarily have a positive effect on students’ intentions to become an entrepreneur in the short run, for it provides them with a more realistic perspective on what it takes to be an entrepreneur (Slavtchev et al., 2012).

In this case study, we examined the implementation of entrepreneurship education and creativity at a university. Universities are characterised by bureaucracy, laborious decision processes, inflexible structures and lengthy processes, restricted budgets and an ambiguous relationship between “theoretical” academia and “practical” entrepreneurship. For this reason,
university might not be the right environment to launch education courses for entrepreneurship and creativity. Our findings indicate the importance of a setting that allows students to participate irrespective of their discipline or study progress. Moreover, it seems advantageous that students can tailor the program to meet their specific needs. The importance of flexible integration into regular academic studies has to be emphasised. Although at present universities may sometimes be stagnant and cumbersome institutions, they are crucial for creating new ideas and finding novel solutions. Therefore, universities and start-ups are more similar than expected.

LITERATURE

WHICH SMES PERCEIVE ACCESS TO FINANCE AS AN OBSTACLE TO THEIR OPERATIONS? EVIDENCE FROM TURKEY

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ABSTRACT
Small and medium-sized enterprises (SMEs) have a fundamental role in the economic growth and job creation in almost all economies in the world. Access to finance is fundamental for the survival and growth of SMEs. However, financial constraints are considered to be one of the most important factors that impede the growth of these firms. To contribute to the understanding of the financial constraints faced by SMEs, this paper sets out to find the firm level determinants of perception of access to finance as an obstacle to the operations of Turkish SMEs. We find that size, age, percentage of sales exported and business group affiliation do not have an effect on the tendency to see access to finance as an obstacle. Audited firms are less inclined to see access to finance as an obstacle. This inclination decreases with an increase in the percentage of sales exported. Firms that have made a recent credit application have a lower tendency to see access to finance as an obstacle. This tendency is strengthened with an increase in the percentage of sales exported. Keywords: Bank loans, Financial Constraints, SMEs

1. INTRODUCTION
SMEs are a central part of the economic fabric in almost all economies in the world. A thriving SME sector contributes to economic growth, entrepreneurial activity, job creation and innovation. Access to finance is fundamental for SMEs to grow and prosper. However, barriers to bank finance are ranked as one of most important constraints faced by SMEs (Hughes, 2009; Mason and Kwok, 2010; Shen, Shen, Xu and Bai, 2009). SME literature suggests that these firms face higher barriers to bank financing than large firms (Beck, Demirgüc-Kunt, Laeven and Maksimovic, 2006; Beck, Demirgüc-Kunt and Maksimovic, 2008; Pissarides, 1999). SMEs encounter greater difficulties in accessing bank financing because they are informationally opaque and it is difficult for banks to evaluate their corporate capabilities (Ang 1992; Berger and Udell, 1998; Gregory, Rutherford, Oswald and Gardiner, 2005).

Emerging market SMEs encounter more challenges in accessing bank financing (Hanedar, Broccardo and Bazzana, 2014; Menkhoff, Neuberger and Rungruxsirivorn, 2012; Menkhoff, Neuberger and Suwanaporn, 2006). The additional challenges are related to the preference of firms to operate outside the formal system. (OECD, 2006).

Diamond (1991) suggests that because young and small firms do not have a long term relationships with banks so that they can establish reputational capital, the probability that they can receive credit is lower. Levenson and Willard (2000) contend that banks do not prefer to lend to smaller firms because the high fixed costs of granting loans to them lower profit margins. The authors find that smaller and younger firms have lower success rates in their loan applications. Chakravarty and Yılmazer (2009) also show that size of a firm has a positive relationship with the probability of being approved for a loan.

To contribute to the SME financing literature on emerging markets, this paper analyzes the firm level determinants of perception of access to finance as an obstacle to the operations of
Turkish SMEs. The analysis uses the cross-sectional data set of 1,139 SMEs for the year 2013. We find that size, age, percentage of sales exported and business group affiliation do not affect the inclination to see access to finance as an obstacle. SMEs whose annual financial statements are checked and certified by external auditors have a lower inclination to see access to finance as an obstacle to their operations. However, this inclination decreases with an increase in the export intensity of the firms. We also find that SMEs that made a credit application in the last fiscal year have a lower tendency to perceive access to finance as an obstacle. This tendency is strengthened with an increase in the percentage of sales exported.

The remainder of the study is organized as follows: Section 2 discusses the research methodology. Section 3 depicts the sample and presents the summary statistics. Section 4 gives the results of the empirical study and section 5 concludes.

2. RESEARCH METHODOLOGY

The perception of access to finance as an obstacle to the operations can be described with the following multiple regression model:

\[
\text{Obstacle}_i = \beta_0 + \beta_1 \text{Size} + \beta_2 \text{Age} + \beta_3 \text{Export} + \beta_4 \text{Growth} + \beta_5 \text{Group} + \beta_6 \text{Audit} + \beta_7 \text{Experience} + \epsilon_i
\]

Obstacle represents the dependent variable. We form our dependent variable from responses to the subsequent question: “To what degree is access to finance an obstacle to the current operations of this establishment?”. The responses vary between 1 (no obstacle), 2 (minor obstacle), 3 (moderate obstacle), 4 (major obstacle) and 5 (very severe obstacle). Size represents firm size which is proxied by the number of full time employees. Age stands for firm age. Age and size are expected to have a negative relationship with the perceived degree of accessibility of finance as an obstacle to the operations because younger and smaller firms may not have adequate reputational capital to have easy access to financing.

Export represents percentage of sales exported by the firm. Access to finance is expected to be positively affected by exposure to foreign trade. Competitive pressure exerted on exporting firms may positively affect access to finance through its effect on efficiency and quality of output (Ganesh-Kumar, Sen and Vaidya, 2001).

Growth stands for firm growth. Firm growth also may also affect perception of accessibility of finance as an obstacle to the operations. Firms with high growth may not perceive accessibility of finance as an obstacle because of their increasing cash flows. However, the requirement of a large amount of funds as a result of growth may make firms think that not having adequate access to finance adversely affect the operations (Canton, Grilo, Monteagudo, and Van der Zwan, 2010). We measure firm growth with the change in sales revenue in the last three years.

Group stands for the dummy variable for business-group affiliation. Perception of accessibility of finance as an obstacle may be influenced by group affiliation because group affiliated firms may use internal capital markets within groups as a source of finance.

Audit represents the dummy variable for whether the firm has its annual financial statements checked and certified by external auditors. We expect that firms that have audited financial
statements are expected to encounter lower financing constraints and have better perceptions about the accessibility of finance as an obstacle the operations.

**Experience** represents the dummy variable for having a recent loan application experience. The variable is formed from the responses to the following question: “Did this establishment apply for any loans or lines of credit in 2012?”. Recent experiences on bank loan applications may affect perception of accessibility of finance as an obstacle (Canton et al., 2010).

We also repeat the regression analysis by adding interaction terms between the audit and experience dummy variables and the export variable. Exposure to foreign trade is expected to affect the strength of the relationship between the given independent variables and the perception of access to finance as an obstacle to the operations. Our regression model with interaction effects is as follows:

\[
\text{Obstacle}_i = \beta_0 + \beta_1 \text{Size}_i + \beta_2 \text{Age}_i + \beta_3 \text{Export}_i + \beta_4 \text{Growth}_i + \beta_5 \text{Group}_i + \beta_6 \text{Audit}_i + \beta_7 \text{Audit}_i \times \text{Export}_i + \beta_8 \text{Experience}_i + \beta_9 \text{Experience}_i \times \text{Export}_i + \epsilon_i
\]

Multicollinearity is not a problem in our model because the VIF values of the independent variables are below the cutoff value of 4. Description of the variables used in the regression model is presented in Table 1.

**Table 1: Description of the variables used in the regression model**

<table>
<thead>
<tr>
<th>Dependent Variable</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Obstacle</td>
<td>On a scale from 1 (no obstacle) to 5 (very severe obstacle), respondent gives an answer to the following question: ‘To what degree is access to finance an obstacle to the current operations of this establishment?’</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size</td>
<td>Number of full time employees</td>
</tr>
<tr>
<td>Age</td>
<td>Firm age</td>
</tr>
<tr>
<td>Export</td>
<td>Percentage of sales that was exported in 2012</td>
</tr>
<tr>
<td>Growth</td>
<td>Percentage change in sales revenue in the last three years</td>
</tr>
<tr>
<td>Group</td>
<td>Dummy=1 if the firm is part of a larger firm</td>
</tr>
<tr>
<td>Audit</td>
<td>Dummy=1 if the firm has its annual financial statements checked and certified by an external auditor</td>
</tr>
<tr>
<td>Experience</td>
<td>Dummy=1 if the firm applied for any loans or lines of credit in 2012</td>
</tr>
</tbody>
</table>

**3. DATA**

The cross-sectional data set comes from World Bank Enterprise Survey which was carried out in year 2013. 1,139 firms whose number of employees is less than or equal to 250 make up our sample. Firms in the sample operate in nine industry categories (food, textiles, garments, non-metallic mineral products, fabricated metal products, other manufacturing, retail and other services). For further information about World Bank Enterprise Surveys, you can visit the web site www.enterprisesurveys.org.
Table 2 gives the summary statistics of the variables.

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Standard Deviation</th>
<th>Median</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Dependent Variable</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Obstacle</td>
<td>0.714</td>
<td>1.095</td>
<td>0</td>
</tr>
<tr>
<td><strong>Independent Variables</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Size</td>
<td>43.667</td>
<td>51.637</td>
<td>21</td>
</tr>
<tr>
<td>Age</td>
<td>16.547</td>
<td>12.542</td>
<td>14</td>
</tr>
<tr>
<td>Export</td>
<td>28.685</td>
<td>38.219</td>
<td>0</td>
</tr>
<tr>
<td>Growth</td>
<td>0.385</td>
<td>0.514</td>
<td>0.273</td>
</tr>
<tr>
<td>Group (Dummy)</td>
<td></td>
<td>Percentage Frequency of 1= 85%</td>
<td></td>
</tr>
<tr>
<td>Audit (Dummy)</td>
<td></td>
<td>Percentage Frequency of 1=48%</td>
<td></td>
</tr>
<tr>
<td>Experience (Dummy)</td>
<td></td>
<td>Percentage Frequency of 1=60%</td>
<td></td>
</tr>
</tbody>
</table>

We see that obstacle variable has a mean of 0.714. This shows that firms on average indicate that access to finance is roughly a minor obstacle to the current operations of the establishment. The mean age of firms is 16.54 years. Average percentage of sales that is exported by the sample firms is approximately 29%. Total sales revenue of firms grew by 38.5% on average in the last three years. 85% of the firms are part of a larger firm. 48% of the firms have their annual financial statements checked and certified by external auditors. 60% of the establishments applied for a loan or a line of credit in year 2012.

4. EMPIRICAL FINDINGS

The estimation results of the regression models are given in Table 3. Column 1 presents the results of the model without the interaction effects given by equation (1). We see that size, age, growth, and business group affiliation do not have a statistically significant relationship with the perception of access to finance as an obstacle to the current operations of the establishments. Audit dummy variable has a statistically significant negative relationship with the dependent variable at the 0.01 level. The coefficient indicates that firms whose financial statements are checked and certified by external auditors are less inclined to see access to finance as an obstacle to their operations. Experience dummy variable also has a statistically significant negative relationship with the dependent variable at the 0.01 level. The coefficient shows that firms that applied for a loan or line of credit in the last fiscal year have a lower tendency to see access to finance as an obstacle.

Column 2 presents the results of the model given by equation (2) which includes the interaction effects. The statistically significant coefficient of the interaction effect of audit dummy variable and export variable shows that the effect of having audited financial statements on the inclination to see access to finance as an obstacle changes with the export intensity of the firm. The positive coefficient shows that audited firms with a higher percentage of sales that is exported have a higher tendency to see access to finance as an
Table 3: Regression estimation results

<table>
<thead>
<tr>
<th>Dependent Variable: Obstacle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent Variables</td>
</tr>
<tr>
<td>Size</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Age</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Export</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Growth</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Group (Dummy)</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Audit (Dummy)</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Audit (Dummy) × Export</td>
</tr>
<tr>
<td>Experience (Dummy)</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Experience (Dummy) × Export</td>
</tr>
</tbody>
</table>

R²: 0.1 0.12
F-Statistic: 7.77 7.19
Prob (F-Statistic): 0 0

The null hypothesis that each coefficient is equal to zero is tested. P-values in brackets.

*** Significant at 1% level.
**  Significant at 5% level.
*   Significant at 10% level.

obstacle than firms with a lower percentage of sales that is exported. This finding can be the result of the uncertainty and failure risk that exporting carries (Amiti and Weinstein, 2011). The interaction effect of experience dummy variable and export variable which is also statistically significant indicates that export intensity have an effect on the relationship between having applied for a loan or a line of credit in the previous year and the inclination to see access to finance as an obstacle. The negative coefficient shows that among the SMEs that made a recent credit application, those with a higher percentage of sales that is exported have a lower tendency to see access to finance as an obstacle than the ones with a lower percentage of sales exported. Eventually, we can say that being an export intensive firm strengthens the negative effect of the experience of a recent credit application on the inclination to see access to finance as an obstacle to the operations.
5. CONCLUSION
This paper examines the determinants of the perception of access to finance as an obstacle to the operations of Turkish SMEs. Determining these determinants for an emerging market is an important contribution to the literature because of the importance of SMEs for the economic prosperity of emerging markets. The results of the World Bank Enterprise Survey which was conducted in Turkey in year 2013 are used to compose the cross-sectional data set. The sample is composed of firms whose number of full time employees is less than or equal to 250.

The estimation results show that firm size, age, percentage of sales exported and business group affiliation do not have a relationship with the inclination to see access to finance as an obstacle. In line with our expectation, we find that firms that have audited financial statements have a lower tendency to see access to finance as an obstacle to their operations. However, this tendency decreases with an increase in the percentage of sales exported. This finding can be attributed to the credit-constraints faced by exporting SMEs created by their exposure to uncertainty and failure risk.

We also find that SMEs that made a recent credit application have a lower inclination to perceive access to finance as an obstacle. An increase in the percentage of sales exported strengthens this inclination. As a result, export intensive firms that made a credit application in the last fiscal year are less inclined to see access to finance as an obstacle than non-export intensive firms that made a credit application.

LITERATURE


THE ANALYSIS OF GENDER CHARACTERISTICS OF COMMUNICATION IN THE CASE OF INTERVIEWS WITH CROATIAN AND GERMAN ENTREPRENEURS

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ABSTRACT
This paper analyzes the features of gender-marked language of communication and examines its relationship with the leadership styles of female and male entrepreneurs. The theoretical part of the work provides a solid foundation that is used for the verification of empirical research. It takes into account the characteristics of female entrepreneurship as underrepresented, but also the shape of a growing business in the Republic of Croatia, the characteristics of male and female leadership styles and the differences between them not only in Croatia but also in Germany, as well as the linguistic expression of the characteristic features for both women and men, focusing on their differences as well.

The empirical part of the work is based on the testing corpus, which consists of 20 written interviews with entrepreneurs, collected from magazines, newspapers and downloaded from the Internet. At each interview, a total of 27 variables related to linguistic behavior were questioned. The study evaluates the types of arguments used by entrepreneurs of Croatian and German national identity. Also, a great attention is paid to the structure of the argumentation processes. The results showed that only certain parts of the linguistic behavior mentioned in the theoretical part can actually be attributed to women or men, thus the style of leadership which they belong, and whether the results are identical according to the national identity of respondents.

Keywords: gender-marked language of communication; leadership styles of female and male entrepreneurs

1. INTRODUCTION
The main emphasis of the paper is the contrastive analysis of newspaper interviews in the press with regard to specific implementation of a gender perspective. The communication is a key factor in the success of any organization. The analysis of the implementation of a gender perspective in the communication style was chosen because of the popularity of topics related to women's rights and specific discrimination against women in business life.

The theoretical part of the paper gives an overview of the basic guidelines related to female entrepreneurship, communication, gender marked by communication and characteristics of women's and men's ways of leading. Feminist linguistics laid the foundations of the theory of linguistic behavior of women and men.
Empirical research is based on a random sample comprising 20 interviews with Croatian and German male and female entrepreneur. Interviews surveyed for this study were taken from daily newspapers and magazines from online archives and also represent a way of achieving mass communication through print media as well as the mass media. The aim of the research is to link leadership style enterprise segment and communication style in relation to the gender of a person and the country of origin.

2. ARGUMENTATION AND GENDER FEATURES OF LANGUAGE AND COMMUNICATION

In this paper the characteristics of gendered communication are linked with the way of the company management through the prism of argumentation. According to Skaric (2011: 13) an argument or reasoning is the process within which the audience and/or the other party accept the rational attitude or the claim of a speaker, especially based on quality argumentation. This paper will show the characteristics of gender-based modes of communication which can be analyzed in a written discourse, and which indicate male and/or female leadership style, as described by Poloski (2003, cf. Eagly and Johnson, 1990), and can be examined through parts of argumentation. According to Trömel-Plötz (1978), Spender (1980) Klann-Delius (2005), Lakoff (2004) Samel (2000) and Borcic (2009, 2012) the method of female communication is characterized by civility and refinement, but also by uncertainty, which can be associated with implicit expression of their attitude, the inclusion of a interlocutor into the discussion and the presentation of team thinking. At the language level that part is examined based on speaking through I or we perspective.

Women's communication style is further considered more indirect and more subjective and male style more direct and objective (Cf. Barada, 2004, Klann-Delius, 2005, Lakoff, 2004, Samel, 2000, etc.). Contrary to the stated, men are more likely to show their dominance with different linguistic means emphasizing their position or importance. According to German female linguists (cf.. Samel, 2000, Klann-Delius, 2005) by using I/my-perspective of speaking in specific thematic contexts it is possible to further highlight their importance. Accordingly, directly expressing their opinions, speaking through the I-perspective, the use of counter-arguments and clear reasoning in the response is considered in this paper as a possible male linguistic behavior, as well as the support to the fundamental thought through additional arguments, examples and evidences, speaking through we-perspective, the use of argumentum ad populum. Argumentum ad populum is described by Skaric (2011: 89-97) as the use of stereotypes for evidence in order to act more convincingly.

It is important to emphasize that the paper does not consider that there is a "female" language in terms of speaking a special language that men do not understand, and vice versa. The paper explores the possibility of the existence of differences in the way of communication of male and female entrepreneurs, and the possibility of connecting these characteristics of the communication style and the management characteristics.

3. MALE AND FEMALE ENTREPRENEURSHIP

Leadership is described as a process of social influence in which one person affects the participation and support of others in the pursuit of the common task (Chemers, 1997). Coric (2002, cf. FFAGENSON, 1993) explains female entrepreneurship as a company and/or economic subject "which has a minimum of 51 percent female ownership", but in a today's society, men have more power and authority than women, so the female entrepreneurship is in the process of development since women sometimes do not have equal access to loans,
training, information, support, and all which enables successful conduct of work such as public support in the form of adjustment of working hours of kindergartens and others.  

There are different types of the company leadership and are therefore different leadership styles represented in today's business environment. Various researchers conduct the analyses and descriptions of gender-based leadership style (cf.. Bass et al., 1996, Eagly et al., 2003, Eagly and Karau, 2002, etc.). Poloski (2003) also analyzes and describes the male and female management style and states that female leadership style is democratic, participatory, collegial, friendly, "emotional", interactive. One might call it a collaborative style, or a supportive style. It is obvious that the characteristics of female leadership are in line with the characteristics of female methods of communication (cf. Barada, 2004, Klann-Delius, 2005, Lakoff, 2004, Samel, 2000, etc.). Women further prefer cooperation over competition, problems are solved by adapting, negotiation, consultation and compromise. According to Poloski (Ibid.) a typical male leadership style is best described by words such as determination, courage, power, security, aggression, objectivity, logic, self-confidence, vigor, etc., again synergetic with the characteristics of the male methods of communication (cf. Barada, 2004, Klann-Delius, 2005, Lakoff, 2004, Samel, 2000, etc.).

Eagly and Johnson (1990) studied the connection between gender of a person and characteristics of the leadership. Their researches have shown that men are more focused on solving tasks, while women are more focused on interpersonal relationships. They further showed that women are more prone to democratic or participative style, while men are more inclined to autocratic or directive style, which is in full compliance with the conclusions related to communication. The examination of the communication styles supports the efficient internal communication. The internal communication, leadership and problem solving with the employees are three aspects of key importance in the potential success of any organization. Organizations can not expect to be successful if they have ineffective internal communication and employees frustrated by the environment in which they feel ignored and lead without a clear direction.

4. RESEARCH

The aim of the research is to link leadership styles attributed to female or male entrepreneurs with the characteristics of their linguistic behavior. It is chosen to investigate whether there are different ways of argumentation in the language of male or female entrepreneurs in relation to the country of their origin. The status of independent variables is given to the gender of a person, and the status of the dependent variable is given to a term of communication style.

The following hypotheses were set prior to the implementation of the empirical research:
H1: In interviews with male entrepreneurs prevalent are features typical of male language and behavior.
H2: In interviews with female entrepreneurs prevalent are features typical of female linguistic behavior.

4.1. Corpus and methodology

The research is based on newspaper interviews with female and male entrepreneurs. The corpus includes interviews with Croatian and German female and male entrepreneurs, and was collected by searching the web and business magazine portals as well as searching

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business newspapers and magazines. Overall there is a total of 30 interviews, 17 of which with male entrepreneurs and 13 with female entrepreneurs. All 30 of them were firstly numbered 1-30, and then using the algorithm of random numbers 10 were selected with male entrepreneurs and 10 with female entrepreneurs divided into five female and male Croatian entrepreneurs and 5 female and male entrepreneurs of German national identity, which constitutes the final corpus of 20 interviews.

For the research purpose, a quantitative and qualitative methods were used. The analysis is carried out according to the analytical matrix that is made for the purposes of this paper, and is located at the end of this paper, as Appendix 1. The analytical matrix consists of variables, which along with some general information about the interview and the interviewee question the features of a particular linguistic behavior in their written forms.

4.2. The overview of collected information and discussion

This chapter presents the results obtained by empirical analysis. Each interview was analyzed for all the variables mentioned above. The research unit is a theme statement or an answer to a question. The results are given in percentages. The percentages represent the ratio of the testimony and identified sentence characteristics by variables in Analytical matrix (Appendix 1). The variables 1-5 relate to general information about the interview and the interviewee, the results are listed in the table at the end of the paper, as Appendix 2.

Variables that examined the types of arguments (6-13), a reference to the author (6:07), personal opinion (8:09), team opinion (10:11), argumentum ad populum (12:13) gave results listed in table 1. It is important to note that in most responses it was possible to identify, for example, both I and we perspective, so for these variable in both cases, the response was positive.

<table>
<thead>
<tr>
<th>Variable</th>
<th>a reference to the author (variable 6 and 7)</th>
<th>I-perspective / stating personal opinion (variable 8 and 9)</th>
<th>WE perspective / stating team opinion (variable 10 and 11)</th>
<th>The use of argumentum ad populum (variable 12 and 13)</th>
</tr>
</thead>
<tbody>
<tr>
<td>INTERVIEWS FROM CROATIAN NEWSPAPER</td>
<td>2%</td>
<td>8%</td>
<td>68%</td>
<td>77%</td>
</tr>
<tr>
<td>INTERVIEWS FROM GERMAN NEWSPAPER</td>
<td>6%</td>
<td>26%</td>
<td>59%</td>
<td>81%</td>
</tr>
</tbody>
</table>

Table 1. Results for variables 6 - 13

173 It is important to emphasize that the results of studies conducted on the written discourse have their shortcomings. Here we refer to the fact that the text of the interview has very likely been subjected to editing / proofreading by journalists and publishers and that is simply a factor that can not be influenced, but it is necessary to accept and adapt research to it.
Variables 6-7 examine how many times in an interview the male or female entrepreneur includes the author of the interview. The answers of Croatian female entrepreneurs in 8% of testimonies were identified in which women are referring to an external authority (the person who interviewed them), while the statements of men identified 2% of such statements. In the German discourse the ratio is 26% in the female discourse versus 6% in male.

Variables 8-9 are used to check if male entrepreneurs really use more personal ("I") opinion while variables 10-11 check whether truly female entrepreneurs use more team opinion ("we") and whether it is determined by the national identity. Given that some previous studies have shown that women are more likely than men to use first person plural, based on these variables it is possible to see if that is really true. Does the female leadership style truly express a desire for cooperation, the sharing of power and the developing and maintenance of good interpersonal relationships? The Croatian entrepreneurs use rhetorical discourse perspective I in 77% of testimonies, men in 68%. The German discourse has a similar ratio, male entrepreneurs use rhetorical perspective I in 59%, and we in 53% of testimonies.

Variables 12-13 examine who uses more often argumentum ad populum. In the answers of Croatian female entrepreneurs 17% of expressed opinions were in the form of argumentum ad populum, and in interviews with German entrepreneurs identified were in 6%, while such testimonies cannot be found in interviews with Croatian or German male entrepreneurs.

Variables 14, 15, 16, 17, 18, 19, 20, 21 check how male and female entrepreneurs support their relevant claims and enrich them with the examples and evidence of the correctness of their allegations. The results are listed in Table 2.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Direct opinion stating (variable 14 and 15)</th>
<th>Public stating of basic claim (variable 16 and 17)</th>
<th>The support to claims in form of additional claims (variable 18 and 19)</th>
<th>The confirmation of claims in form of examples and proofs (variable 20 and 21)</th>
</tr>
</thead>
<tbody>
<tr>
<td>M</td>
<td>F</td>
<td>M</td>
<td>F</td>
<td>M</td>
</tr>
<tr>
<td>INTERVIEWS FROM CROATIAN NEWSPAPER</td>
<td>10% 6%</td>
<td>100% 100%</td>
<td>100% 97%</td>
<td>47% 54%</td>
</tr>
<tr>
<td>INTERVIEWS FROM GERMAN NEWSPAPER</td>
<td>23% 28%</td>
<td>100% 100%</td>
<td>100% 100%</td>
<td>70% 88%</td>
</tr>
</tbody>
</table>

Table 2: Results for variables 14-21

Variables 14 and 15 give us the insight into whether women or men are more inclined to direct declaration of their attitude and can it be linked with the national identity to which they belong. The results in Table 2 show that in the analyzed interviews Croatian male entrepreneurs more often state directly their opinion as well as German female entrepreneurs, therefore the results cannot be linked to the gender of a person.
Variables 16, 17, 18, 19, 20, 21 are used to check how male and female entrepreneurs support their claims with relevant statements, and enrich them with the examples and evidences of the correctness of their allegations. The results (Table 2) show that most analyzed testimonies identify clearly expressed opinion in the form of a claim and that the differences in terms of gender are minimal, they can be even reduced to a statistical error of researchers. The difference in the analyzed discourse is evident with variable 20 and 21, because the results indicate that the German male and female entrepreneurs state more evidences and examples in their answers to the claim, whereas female entrepreneurs more often (88%) compared to male entrepreneurs (70%).

Does the interviewee use counter-arguments in the argumentative process, or refutes them to confirm their original theory is examined with the variables undernumber 22, 23, 24 and 25. An affirmative answer can be associated with an increase importance of the original thesis. The variables 26 and 27 examine how male and female entrepreneurs offer a conclusion or a closure of the conversation. This can be associated with the statement about language and communication between the genders, which is located under the "gender perspective in language and communication", that women in conversations have more fully completed sentences. All the results are listed in Table 3.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Stating counterarguments (variable 22 and 23)</th>
<th>Additional refuting as the enhancement to original claim (variable 24 and 25)</th>
<th>Stating a clear conclusion (the closure is not identified) (variable 26 and 27)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entrepreneurs (M)</td>
<td>Entrepreneurs (F)</td>
<td>Entrepreneurs (M)</td>
<td>Entrepreneurs (F)</td>
</tr>
<tr>
<td>INTERVIEWS FROM CROATIAN NEWSPAPER</td>
<td>21%</td>
<td>9%</td>
<td>15%</td>
</tr>
<tr>
<td>INTERVIEWS FROM GERMAN NEWSPAPER</td>
<td>36%</td>
<td>35%</td>
<td>27%</td>
</tr>
</tbody>
</table>

Table 3: The results for the variables 22-27

As for the use of counter-arguments and the refute of counter-arguments by enhancing the initial claim German male and female entrepreneurs are almost equal. German female entrepreneurs in the structure of argumentative processes use counter-arguments in 35% of the time, and refute it in 24%. With male entrepreneurs the results are almost identical with 36% of counter-arguments and 27% refutings of counterarguments. Again, the differences in the results are not significant among the male and female entrepreneurs of the same national identity, but the differences are visible among entrepreneurs of different national identity. German male and female entrepreneurs compared to Croatian ones are more inclined to use counter-arguments in order to give greater importance to their theses and statements. Finally, variables 26 and 27 examine how much in the structure of argumentative processes male entrepreneurs offer a conclusion to their thesis. Table 3 shows that German male and female
entrepreneurs often offer almost identical conclusion to their thesis. Male entrepreneurs in 61% of cases and female in 60% of cases. There is a greater difference with Croatian male and female entrepreneurs. It is evident that with female entrepreneurs there is no difference depending on the national identity, while there is with male entrepreneurs.

5.  CONCLUSION

The gender marked linguistic behavior is a topic that increasingly more intrigues not only Croatian linguists, but also the general public, because of interesting views which it offers about eternally polemized male-female relationships. Despite not yet being sufficiently explored, its settings are easily applicable to all aspects of the interactions between women and men, including business. In recent years, female entrepreneurship has started to develop in the Republic of Croatia in significant numbers. This resulted in a number of theoretical representations of women as entrepreneurs, which are attributed with a democratic leadership style. Men on the other hand, cherish the autocratic leadership style.

The theoretical overview of gender characteristics of a language gave interesting facts, i.e. the difference between "male" and "female" way of communicating based on which variables are set in the Analytical matrix. The variables examine the characteristics of gender-based behavior which can be tested on a written corpus and which can be connected with the leadership styles. Generally the female speaking style is considered more indirect, and therefore more subjective, while the male is more direct and objective.

The conducted empirical research has shown that certain linguistic indicators, which according to the literature women more frequently use, is more typical for men and vice versa. Regardless of the results, it is important to say that the results in this study are symptomatic and are only valid for the analyzed interviews. Finally, it is difficult to say for sure to whom a certain style of leadership belongs to. One thing is certain and that is that both women and men are able to take over the features of the other. Likewise, the fact that there are gender differences in communication is not at all surprising, but it is also not surprising that they may disappear when men and women begin to take their business "roles". However, the fundamental value of this work is to encourage as many male and female researchers to engage in some aspect of this topic.

LITERATURE


APPENDICES

APPENDIX 1 : ANALITICAL MATRIX

THE ANALYSIS OF GENDER CHARACTERISTICS OF COMMUNICATION IN THE CASE OF INTERVIEWS WITH CROATIAN AND GERMAN ENTREPRENEURS

Variable 1: The identification number of the interview (from 1 to 20)
Variable 2: The name of the newspaper/weekly/internet portal
Variable 3: Interviewee
Variable 4: The title of the interview
Variable 5: The length of the interview (without the journalist’s questions) in sentences:
Variable 6: the Interviewee refers to the author:
YES
Variable 7: If the answer under 6. is YES, how many times does the interview refer to the author?

Variable 8: The interviewee states his or her personal opinion

YES

NO

Variable 9: If the answer under 8. is YES, how many times?

Variable 10: The interviewee states team opinion:

YES

NO

Variable 11: If the answer under 10. is YES, how many times?

Variable 12: The interviewee uses argumentum ad populum:

YES

NO

Variable 13: If the answer under 12. is YES, how many times?

Variable 14: The interviewee shows direct opinion:

YES

NO

Variable 15: If the answer under 14. is YES, how many times?

Variable 16: The interviewee says basic claim:

YES

NO

Variable 17: If the answer under 16. is YES, how many times?

Variable 18: The interviewee uses the argument to support the basic claim:

YES

NO

Variable 19: If the answer under 18. is YES, how many times?

Variable 20: The interviewee supports her or his claims with examples and evidences:

YES

NO

Variable 21: If the answer under 20. is YES, how many times?

Variable 22: The interviewee uses counterarguments:

YES

NO

Variable 23: If the answer under 22 is YES, how many such sentences?

Variable 24: The interviewee uses counter-arguments which emphasize the basic claim:

YES

NO

Variable 25: If the answer under 24. is YES, how many times?

Variable 26: The interviewee offers the closure instead of the conclusion in the conversation:

YES

NO

Variable 27: If the answer under 26. is YES, how many times?
# APPENDIX 2
## THE OVERVIEW OF GENERAL INFORMATION ABOUT THE INTERVIEWED PERSONS

<table>
<thead>
<tr>
<th>Number of interview</th>
<th>Female entrepreneurs /title of the interview/source</th>
<th>Male entrepreneurs /title of the interview/source</th>
<th>Number of words</th>
</tr>
</thead>
<tbody>
<tr>
<td>9</td>
<td>Sandra Mihelčić: „Moja firma – to sam ja“, Web portal 100.Ljudi.net</td>
<td>Luka Rajic: „Nisam zainteresiran za Podravku, a ne zanima me ni politika“, 880 <a href="http://www.vecernji.hr">http://www.vecernji.hr</a></td>
<td>1372</td>
</tr>
</tbody>
</table>
INTERDEPENDENCE OF INTERNAL AND EXTERNAL INTEGRATION ON THE CASE OF TRAVEL AGENCIES

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ABSTRACT
Internal and external integration in managing supply chains are important factors for achieving success of individual companies and wider, for success of all companies cooperating in a supply chain. The interdependence of internal and external integration can be defined with an interactive mode, which points to a positive influence on company performance. The higher the level of internal integration is, the higher the influence of external integration is on company success, in particular from the logistics point of view. In the frame of awareness of importance of both levels of integration, we will research the connection between and the influence of internal integration on external integration on the case of travel agencies. The level of internal integration in this research is generally dealt with on the level of an individual agency, while the level of external integration is composed of the integration of travel agencies with tour operators and other travel agencies, transport services (air, rail, bus and water), accommodation providers and insurance companies. The results of research, performed with statistical analysis of questionnaires and structural equation modelling, point to a positive correlation and positive influences of internal integration with external integration.

Keywords: External integration, Internal integration, Interdependence of integration, Travel agencies

1. INTRODUCTION
A large portion of the gross domestic product in many countries around the world is represented by the service sector, out of which, an important part is presented by the tourist industry. According to Walker (2009, p.15), this industry is becoming the world’s most important activity that has doubled in scope in the last 30 years.

Tourism service supply chains are therefore an important element of the national economy, but the research on the field of these chains is at a much lower level than research focusing on “classical”, manufacturing supply chains. Studies conducted in recent times, namely, can be traced to an increased focus on the field of tourism supply chains, but also a lot of unexplored areas can be observed, including the internal and external integration and the importance of their relationship. Members of the tourism supply chains are becoming increasingly aware that the multi-dimensionality and diversity of packages is dependent upon collaboration between the various members of a particular tourism supply chain and the collaboration with competitors, suppliers, customers and / or companies in the chain. Cooperative relations between these members of each tourism supply chain may also promote informal links between them (Huybers, Bennett, 2003, p. 573).
Tourism supply chain can be defined as a network of tourism enterprises which carry out different activities related to tourism, it includes a wide range of participants in both the private and the public sector (Zhang, Song, Huang, 2009, p. 351). The tourism supply chain is comparable to the production supply chain, but with the basic difference that mainly the «production» part of these chains are the tourists traveling with a product bearing a particularly high service component (Tapper, Font, 2004, p.120). Tourism supply chains are also based on business relations between members of the chain, and their management can contribute towards sustainable performance improvements (Tapper, Font, 2004, p. 124).

All these relationships are important for firm performance. If internal relations are observed, internal integration is the focus, and when relations between the members of the chain are observed, this is research into external integration. If supply chain management is understood as the integration of key business processes from end consumer through original suppliers (Lambert, Cooper, Pagh, 1998, p. 5) it can be seen that supply chain management is the coordination and collaboration between organizations and across the entire supply chain.

Contingency theory is based on the effective performance or efficiency of the company and is achieved only when excellent adaptation between the structural organization of the company and the conditions of its environment is ensured (Burns, Stalker, 1961, p. 57-62; Thompson, 1967, p. 37). The success of the company can be measured by hard (financial: e.g. assessment of profitability, growth, market share) and soft (non-financial: e.g. assessment of consumer satisfaction, perceived effectiveness of relations) factors. The success of the company is generally understood as the sum of the performance of teams, departments and individuals, which represents internal integration, which is also linked to external integration.

Consequently, internal and external integration are necessary for success of the company. The interdependence of internal and external integration or dependence of external integration to internal integration and vice versa is a topic where it is necessary to provide basic knowledge, as it can also show the importance of internal integration for the success of the company. In a literature review, three different theoretical approaches were found, giving rise to the fourth approach that was identified by Germain and Iyer (2006, p. 34), which also defines the interdependence of the interaction of internal and external integration and its impact on the performance of the company. Their study showed that the higher the level of internal integration, the stronger the influence of external integration on the performance of the company is - this is primarily a logistical point of view. Conversely, they found that a low level of internal integration consequently represents a low level of external integration and the resulting poor performance or competitiveness of companies. External integration has a positive impact on the performance of the company only in the event that the level of internal integration is high enough (Germain, Iyer, 2006, p. 36).

Flynn, Hou and Zhao (2010, p. 61) recognize three dimensions of supply chain integration: customer, supplier and internal integration. Stank, Keller and Daugherty (2001, p. 34) define customer and supplier integration as external integration, which is the degree to which a manufacturer partners with their external partners to structure interorganizational strategies, practices and processes into collaborative, synchronized processes. In the present paper, the case of external integration of travel agencies with other members of the tourism supply chain will be examined. In the context of this research, internal integration will be addressed as a process of interaction and collaboration in which employees within the company cooperate with each other to achieve mutually acceptable results for the company. Activities that form
the basis of determining the current level of internal integration of the analysed companies consist of interactive and collaborative perspectives or from their compositions. In the context of this study, the external integration will be understood as a form of interaction, communication or collaboration beyond the margins of the main organization (Stock, Greis, Kasarda, 1999, p. 229; Rinehart, Cooper, Wagenhaim, 1989, p. 67; Griffin, Houser, 1996, p. 198).

In the field of external integration of tourist agencies with individual members of the tourism supply chain, some specific research has already been carried (see Bastakis, Buhalis, Butler, 2004; Fadeeva, 2004; Jemal, Getz, 1995; Kernel, 2005; Medina-Muñoz, García-Falcon, 2000; Morrison, Lynch, Johns, 2004; Topolsek, Mrnjavac, Kovacic, 2014; Tsaur, Yung, Lin, 2006; Ye, Song, Li, 2012; Wong, Mistilis, Dwyer, 2011), but none specified a connection of internal and external integration.

According to the given characteristics and importance of internal and external integration, the main objective of this research is to study the interdependence of internal and external integration in the case of tourism supply chains and to study the key elements of internal and external integration. For this purpose, a questionnaire was prepared and circulated among travel agencies and with the help of which a link between the observed variables will be observed. The results of the questionnaire were analysed in different stages and were subjected to exploratory factor analysis (EFA), confirmatory factor analysis (CFA) and the structural equation model (SEM model).

2. RESEARCH CONCEPTUAL FRAMEWORK

Figure 1 provides a conceptual framework, which is associated with the hypothesized model. The figure shows the used indicators, namely 14 for the internal integration (INT_Ii, i = 1, ..., 14) and 11 for external integration (EXT_Ii, i = 1, ..., 11). It is believed that they can make an appropriate model that includes only two latent factors, each associated with the corresponding arguments in the questionnaire (INT_I and EXT_I). The first factor is called INT_I, which is linked to the level of internal integration and represents collaboration among employees within the tourism agency. Here it should be noted that most of the respondents were smaller travel agencies, which do not have specific functional silos. The second factor, called EXT_I, is connected to the external integration, in which the average travel agency cooperation with other travel agencies or tour operators, with transport providers, hotels, accommodation providers, restaurants and insurance companies are included.

The model consists only of two factors since the only interest of this research is the link between internal and external integration. This also applies to the given hypothesis, which assumes a positive link between them and the direct positive impact of internal integration (INT_I) to the external integration (EXT_I).
3. MATERIALS AND METHODS

3.1. Participants
To determine the anticipated positive correlation between internal and external integration in the case of travel agencies, a survey was carried out among Slovenian and Croatian travel agencies. Each interviewed travel agency responded to arguments related to the level of internal and external integration, in both cases they assessed their agreement with an argument or a mean of cooperation on a 5-point Likert scale (1 - not at all involved in this way, 5 - fully cooperate in this way). After completion of the survey process, 158 fully completed questionnaires were received and were used in this study.

3.2. Measures
The first part of the questionnaire was related to internal integration, where respondents marked their agreement with 14 arguments on the aforementioned 5 point Likert scale. In Table 1, the mean and standard deviation for each argument are presented.

Table 1: Mean and standard deviation (SD) of the INT_I indicators

<table>
<thead>
<tr>
<th>Item</th>
<th>Content of the INT_I item</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>INT_I1</td>
<td>Phone call</td>
<td>4.35</td>
<td>1.088</td>
</tr>
<tr>
<td>INT_I2</td>
<td>E-mail</td>
<td>4.61</td>
<td>.923</td>
</tr>
<tr>
<td>INT_I3</td>
<td>Achieving the overall aim of the company</td>
<td>4.27</td>
<td>1.181</td>
</tr>
<tr>
<td>INT_I4</td>
<td>The collective achievement of the objectives</td>
<td>4.37</td>
<td>1.067</td>
</tr>
<tr>
<td>INT_I5</td>
<td>Sharing of information and other resources</td>
<td>4.30</td>
<td>1.068</td>
</tr>
<tr>
<td>INT_I6</td>
<td>Achieving a common understanding</td>
<td>4.15</td>
<td>1.168</td>
</tr>
<tr>
<td>INT_I7</td>
<td>The joint decisions</td>
<td>4.11</td>
<td>1.234</td>
</tr>
<tr>
<td>INT_I8</td>
<td>Exchange of forms</td>
<td>3.97</td>
<td>1.269</td>
</tr>
<tr>
<td>INT_I9</td>
<td>Exchange of reports</td>
<td>3.77</td>
<td>1.311</td>
</tr>
<tr>
<td>INT_I10</td>
<td>Informal team work</td>
<td>3.69</td>
<td>1.386</td>
</tr>
<tr>
<td>INT_I11</td>
<td>Guided joint planning</td>
<td>3.91</td>
<td>1.269</td>
</tr>
<tr>
<td>INT_I12</td>
<td>Formal meeting</td>
<td>3.68</td>
<td>1.292</td>
</tr>
<tr>
<td>INT_I13</td>
<td>Sharing ideas</td>
<td>4.10</td>
<td>1.158</td>
</tr>
<tr>
<td>INT_I14</td>
<td>Exchange fax. material</td>
<td>3.15</td>
<td>1.593</td>
</tr>
</tbody>
</table>
As was already mentioned, an 11-item questionnaire connected to external integration was also used in the study. Travel agencies assessed individual arguments related to their methods of external integration, answers were given on a 5-point Likert scale (1 - not at all involved in this way, 5 - fully cooperate in this way). Mean values and standard deviations of individual variables are given in Table 2.

### Table 2: Mean and standard deviation (SD) of the EXT_I indicators

<table>
<thead>
<tr>
<th>Item</th>
<th>Content of the EXT_I item</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>EXT_I1</td>
<td>Informal team work</td>
<td>2.49</td>
<td>1.257</td>
</tr>
<tr>
<td>EXT_I2</td>
<td>Exchange of information on sales forecasts, sales and spare capacities</td>
<td>2.53</td>
<td>0.842</td>
</tr>
<tr>
<td>EXT_I3</td>
<td>Joint process development</td>
<td>2.23</td>
<td>0.844</td>
</tr>
<tr>
<td>EXT_I4</td>
<td>Joint planning for anticipating and solving operational problems</td>
<td>2.26</td>
<td>0.834</td>
</tr>
<tr>
<td>EXT_I5</td>
<td>Joint setting of goals</td>
<td>2.24</td>
<td>0.840</td>
</tr>
<tr>
<td>EXT_I6</td>
<td>Joint development and understanding of responsibility</td>
<td>2.36</td>
<td>0.895</td>
</tr>
<tr>
<td>EXT_I7</td>
<td>Aligned decisions on how to improve cost efficiency</td>
<td>2.25</td>
<td>0.861</td>
</tr>
<tr>
<td>EXT_I8</td>
<td>Formal meeting</td>
<td>2.62</td>
<td>0.839</td>
</tr>
<tr>
<td>EXT_I9</td>
<td>Phone call</td>
<td>3.53</td>
<td>0.819</td>
</tr>
<tr>
<td>EXT_I10</td>
<td>E-mail</td>
<td>3.61</td>
<td>0.763</td>
</tr>
<tr>
<td>EXT_I11</td>
<td>Exchange of forms and reports</td>
<td>2.79</td>
<td>0.925</td>
</tr>
</tbody>
</table>

### 3.3. Analysis methods

The entire process of analysis of collected data consists of three basic parts, as recommended by various authors (eg. Hair, Black, Babin, Anderson, 2010). Consequently, the first step was an exploratory factor analysis (EFA) with SPSS, which represents a preliminary statistical technique to identify latent factors and determine their indicator loadings. The next stage was carried out by confirmatory factor analysis that was conducted using AMOS, which explores how well the presumed theoretical structure of the factor model fits the real data (Hair, Black, Babin, Anderson, 2010). The last step was the structural part of SEM (Structural equation modelling), which allows for the determination of links between factors.

### 4. RESULTS

#### 4.1. Exploratory factor analysis

Before conduction of the exploratory factor analysis (EFA), the normality test was performed. Various authors, such as Ullman, 2006; Weston and Gore, 2006; Zhai, Liu, Fellows, 2013 etc. have given normality areas, connected to skewness (+/- 3) and kurtosis (+/- 7). In the given sample, no overruns of borders of normality were detected, because both skewness (between -1.962 and 2.962) and kurtosis (between -1.596 and 6.239) were in normality limits.

As already mentioned, the main objective of the EFA was to extract only two factors, one for internal integration and one for external integration. Due to the normal distribution of data, the extraction method used was Maximum likelihood with Promax rotation (with Kaiser Normalization). To determine reliability, the Bartlett's test of sphericity (BTS) and the Kaiser-Meyer-Olkin (KMO) test were carried out. The BTS value was highly significant (approx.
Chi-Square = 2787.070; df = 171), while the value of KMO was 0.885. Based on recommendations from Sahin, Todiras, Nijkamp, Neuts, Behrens (2013) (and others) the factor analysis can be argued as reliable. On the basis of the EFA, those items not significantly loading to any factor were excluded. Thus, for the INT_I factor, the excluded factors were INT_I1, INT_I2 and INT_I9, and for EXT_I factor, the excluded factors were EXT_I1, EXT_I9 and EXT_I10.

All item loadings on factors were significant, since they reached the value 0.45 or more (Hair, Black, Babin, Anderson, 2010). Cumulative (%) for EFA was 65.120, and total variance (%) was 23.388. The results of the rotated factor pattern matrix (loadings and Cronbach’s alphas) are presented in Table 3.

Table 3: The results of the rotated factor pattern matrix in EFA

<table>
<thead>
<tr>
<th>Pattern Matrix</th>
<th>Factor</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cronbach Alpha</td>
<td>INT_I</td>
<td>0.910</td>
<td></td>
</tr>
<tr>
<td>INT_I5</td>
<td>.804</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I4</td>
<td>.790</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I6</td>
<td>.766</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I3</td>
<td>.760</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I13</td>
<td>.738</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I8</td>
<td>.709</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I11</td>
<td>.703</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I7</td>
<td>.676</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I12</td>
<td>.661</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I10</td>
<td>.657</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT_I14</td>
<td>.458</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I4</td>
<td>.979</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I5</td>
<td>.969</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I3</td>
<td>.963</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I7</td>
<td>.956</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I6</td>
<td>.924</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I2</td>
<td>.837</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I8</td>
<td>.664</td>
<td></td>
<td></td>
</tr>
<tr>
<td>EXT_I11</td>
<td>.539</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Extraction Method: Maximum Likelihood.
Rotation Method: Promax with Kaiser Normalization.

From the EFA results it is evident that the variables related to the internal integration are significantly loaded on the corresponding factor INT_I and the variables related to the external integration are significantly loaded on the corresponding factor EXT_I.
4.2. Confirmatory factor analysis

The resulting loading factors from EFA were assigned to confirmatory factor analysis. Due to the normality of the data, the maximum likelihood (ML) estimation method was selected in the CFA as it carries with it the assumption of multivariate normality. In the data set used in the CFA, there are no missing data issues. Based on different research, modal fit was also evaluated. Here, the following different model fit indices were checked, most notably and often used were: Goodness of Fit Index (GFI), Adjusted Goodness of Fit Index (AGFI), the Comparative Fit Index (CFI), the Root Mean Square Error of Approximation (RMSEA), Standardized Root Mean Residual (Standardized RMR). All of those model fit indicators were above the recommended value. Additionally, the Composite (construct) Reliability (CR) values and Average Variance Extracted (AVE) were calculated for both factors. All CR were greater than the threshold of 0.7 (from 0.731 to 0.889), while the AVE values were greater than the threshold of 0.5 (from 0.524 to 0.678).

4.3. Structural equation model

Based on the conceptual model, shown in figure 1, the structural part of the model was performed. The model consist of the measurement part of the CFA model. In the structural equation model (SEM), the ML estimation method was used when estimating all the necessary parameters of the model. After the completed estimation, the calculation of the GOF indices was also needed. All observed model fit indices were inside the preferred value areas (Chi-Square = 179.171; p = 0.003; GFI = 0.912; AGFI = 0.953; CFI = 0.982; RMSEA = 0.048; PCLOSE = 0.545; Standardized RMR = 0.0599), which shows that the developed structural equation model ensures a good fit to the data.

Figure 2 shows the standardized estimated SEM model, whose estimations are significant at the p ≤0.05 level. The results of the SEM model, based on the given conceptual model, show that on the case of travel agencies, internal integration has a positive effect on external integration. Due to the fact that the causal path from factor INT_I to factor EXT_I is statistically significant with a regression weight of 0.30, we can confirm our research hypothesis.

Figure 2: The standardised estimated SEM model for INT_I (internal integration) and EXT_I (external integration)
5. CONCLUSION
Internal and external integration of companies have a proven impact on the performance of manufacturing supply chains. Since the service supply chains, which include the tourism supply chain, are an essential element of every developed country’s GDP, the importance of internal and external integration in tourism supply chains is very important because it affects not only the performance of all members in this chain, but consequently also to the country's GDP. In the context of this paper, the basic goal was set to research whether there is a positive correlation between internal and external integration and to analyse the expected positive impact of internal integration on external integration. The central focus was on travel agencies, which generally must work together both internally and externally. External cooperation of travel agencies refers to the following members of the chain: with other travel agencies or tour operators, with transport providers, hotels, accommodation providers, restaurants and insurance companies. Based on the determination of the total level of external integration and elements of internal integration, it is therefore possible to prove a link between these two constructs, which supports certain conceptual models of previous research, such as the model from Germain and Iyer (2006). In the future, research should be directed towards other members of the tourism supply chain, since it is not necessarily that their aspect of cooperation with travel agencies is comparable to those that arose in this paper.

LITERATURE


SMEs IN BOSNIA & HERZEGOVINA AND CROATIA: IS THERE A FUTURE FOR PARTNERSHIP FORMS?

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ABSTRACT
In most of the European jurisdictions, small and medium-sized enterprises (SMEs) incur significant costs in carrying out their regular business activities due to the legal requirements imposed on them, which are traditionally tailored to satisfy the needs of large public companies. As a result, the need for providing business organization forms which will meet the needs of smaller businesses has been recognized recently. This paper examines legal characteristics and usage of different forms of partnerships and certain hybrid legal forms as types of business organizations in several European countries with the aim of establishing the advantages and disadvantages of their use. The results are then compared with the existing legislation in Bosnia and Herzegovina and Croatia. There has not been much use of partnership forms in these countries, mainly due to the unlimited liability imposed on partnerships members. Following recent trends of some jurisdictions allowing limited liability partnerships, the aim of this paper is to examine the attractiveness of partnership form features and to discuss the possibility of creating new hybrid business forms which will suit the needs of SMEs in these countries.

Keywords: organization form, partnership, small and medium-sized enterprises

1. INTRODUCTION
In most of the European jurisdictions, small and medium-sized enterprises (SMEs) incur significant costs in carrying out their regular business activities due to the legal requirements imposed on them, which are traditionally tailored to satisfy the needs of large public companies. McCahery and Vermeulen (2000, p. 2) point out on disproportionate and over-regulatory imposition of many of the EU's harmonized company law provisions on smaller firms. As the result, the need for providing business organization forms which will meet the needs of smaller businesses has been recognized recently, and some of the states have responded to these needs.

Business organization forms available to SMEs generally include: a sole proprietorship, different forms of partnerships available depending on the legal system, and a limited liability company. There are many considerations that need to be taken into account when choosing a form of organization. Aprill and Holo (2009, pp. 2-34) classify them into tax and non-tax considerations, and as the primary one they identify the number of levels of income taxation applicable to the entity and its owners. With respect to the non-tax considerations, limited
liability is considered to be the key one. Other non-tax considerations include: formation requirements, management and control over the business operations, transferability of interests, fiduciary duties owed by owners and managers to the entity or to other owners, the risks and consequences of an entity dissolving upon certain events, applicability of securities laws, and possibility of changing form of organization. These considerations will therefore be taken into account in analysing different forms of partnerships.

This paper examines legal characteristics and usage of different forms of partnerships and certain hybrid legal forms as types of business organizations in several European countries with the aim of establishing the advantages and disadvantages of their use. According to Andenas and Wooldridge (2009), the partnership form is still used by many businesses in the European Union, and is of considerable economic importance despite its disadvantages.

Up to this moment, partnerships have not been made subject to much of the European Union directives, and there are no indications that they will be in the near future. This means that they mostly remain governed by national laws. The only exceptions to this are certain hybrid forms. Only the Council Directive 90/605/EEC extended the scope of the Fourth and Seventh Directive to partnerships in which general partners are public companies, private companies or limited partnerships with shares (Art. 1-2).

2. PARTNERSHIP FORMS IN EUROPEAN COUNTRIES

The unlimited liability of partners for the debts of a partnership is considered the most serious disadvantage of this form. It is generally assumed that precisely due to the unlimited liability of partners, partnerships require much less regulation than limited liability forms: limited liability companies or even limited liability partnerships (LC, 2003, p. 1). However, Blair (2003, p. 9) argues that unlimited liability was not the main reason why markets chose the corporate form, but the power over the other partners in a partnership. It is being shown that corporate form is not necessarily used to raise new capital nor to avoid unlimited liability, but it can also be used to lock in the existing capital so the future of the business would not depend on the personal affairs of one of the partners (Blair, 2003, p. 19).

Bubb (2015, pp. 343-345) recognizes the following practical problems with the partnership form, which made it difficult for partnerships to attract outside equity: (1) transferability of interests depending on consent of all partners and transaction costs in subsequent reorganizing of the firm; (2) unlimited liability of partners; (3) possibility of partial liquidation forced by partners' personal creditors; (4) difficulty of establishing centralized governance structure in case of many partners; and (5) inability to litigate in its own name which raised the costs of litigation for creditors. However, entrepreneurs during the Industrial Revolution in England were choosing partnership form for certain advantages it provided.

The advantages of this form are shown in its flexibility which is illustrated by the great differences in the size and nature of partnerships, and its informality. There is a large degree of privacy in financial matters that partnerships enjoy (LC, 2003, p. 1). The flexibility of the form is increased if contracting around the default rules is allowed, but that involves expenses and uncertainties with respect to interpretation of clauses in partnership agreements by courts (Bradley, 2001, pp. 332-333). According to Bradley (2001, p. 336), the Law Commissions in the UK adopt a contractual model of partnership law. During the Industrial Revolution in England entrepreneurs opted for partnership form because, due to the unlimited liability of partners, it minimized the costs of debt financing, and may have minimized the agency costs
too (Bubb, 2015, p. 352). In some of the countries, distinction is made between civil and commercial partnerships. Civil partnerships are partnerships which don't have commercial objectives, as defined by the national laws, and which are not considered commercial by reason of their form. Civil partnerships exist in Belgium, France, Germany and Spain. Apart from that, there are silent partnerships, which exist in Belgium, France and Germany. Those are entities which don’t have to be registered and the relationship doesn’t have to be disclosed to the third parties. This paper focuses on commercial partnerships. There are two main types of these partnerships: general partnerships and limited partnerships.

Partnerships still play an important role in the United Kingdom economy, even though the number of partnerships and the turnover which they achieve declined since 1998 (LC, 2003). The latest data available show that there were 457,000 ordinary partnerships (LLPs are counted as companies) in the UK at the beginning of 2014 (BIS, 2014), compared to 684,645 partnerships in 1998 (LC, 2003). Partnerships in the UK vary in size and formality. They are used for running small family businesses and for short-term profit making ventures as informal associations between two persons, but also for major business enterprises as professional or business partnerships, in which case they have many members, elaborate partnership agreements and management structures (LC, 2003; Andenas and Wooldridge, 2009). Partnerships in the United Kingdom are used for conducting a wide range of business activities, starting with many professionals carrying on their businesses in this form. They also often appear in the retail trade, construction, manufacturing, agriculture and tourism (LC, 2003). The partnership form in some of the European countries is used because of the given tax advantages. In some countries (e.g. Germany) partnerships were used for the purpose of avoiding mandatory disclosure of annual accounts (Andenas and Wooldridge, 2009).

General partnerships are used for conducting a wide range of business activities. All members of a general partnership (general partners) manage the business and have unlimited liability, i.e. joint and several liability, for all the partnership’s obligations. In a limited partnership, there are two kinds of members: general partners who manage the business and have unlimited liability for the partnership’s obligations; and limited partners who are not involved in management and have limited liability, meaning they are liable only to the extent of their contributions to the partnership. Therefore, limited partnerships are much more specialized in nature, and can present a useful vehicle for investors who are not willing to take an active role in management.

In many countries commercial partnerships have legal personality (Belgium, France, Scotland and Spain). The stability of partnerships is increased by that fact, because legal personality allows them to continue its existence after changes in its membership (Bradley, 2001, p. 333). In order to insure continuity of business irrespective of changes in ownership, so that the partnership would not automatically dissolve on change of partners, and to insure possibility of entering contracts and holding property, the Report of the Law Commission and the Scottish Law Commission on Partnership Law in the UK (2003) recommended the introduction of separate legal personality for both general and limited partnerships in England and Wales. However, a partnership there still doesn’t have legal personality (Ministry of
Justice, 2013). In 2006 the UK Government rejected the Commissions' recommendations on general partnerships, but accepted to carry out in stages the reform to limited partnerships.\(^{174}\)

Also, *offene Handelsgesellschaft* (general partnership), *Kommanditgesellschaft* (limited partnership) and *Partnerschaftsgesellschaft* in Germany do not have legal personality. However, they can sue or be sued, enter into contracts and acquire rights and duties. Legal personality also lack Dutch commercial and private partnerships (*maatschap*). In these cases (where partnerships lack legal personality), their members have legal treatment of co-owners of the partnership's property. In other European countries commercial partnerships mainly have legal personality.

Partnerships are characterized by the importance of the personal element. That means that a partner has agreed to associate with his co-partners exclusively (LC, 2003, p. 6). For that reason, consent of all the other members is usually required for transferring a share in a partnership, and in case of death or bankruptcy of a member, partnership can be dissolved. Partners generally enjoy freedom in deciding on the internal construction of a partnership. The personal element is also manifested in the joint and several liability of all or certain members of a partnership for all its obligations (Andenas and Wooldridge, 2009).

General partnerships in the UK are regulated by the Partnership Act 1890, which forms the basis of partnership law in the UK and defines a partnership as "the relation which subsists between persons carrying on a business in common with a view of profit" (s. 1(1)). The section 2 of the Act contains rules for determining existence of partnership, under which the mere sharing of the profits or co-ownership of land do not necessarily mean that a partnership exists (Andenas and Wooldridge, 2009). A partnership relationship results from a contract, and therefore can arise only by mutual consent, express or inferred from the conduct of partners (LC, 2003, p. 6). However, partnership is not only governed by the rules of contract law, as it is „more than a simple contract“ (LC, 2003, p. 6).

A partnership in England and Wales lacks legal personality. This means that it is not an entity separate from its members; it cannot enter into contracts, i.e. acquire rights or obligations, and own property. The rights and obligations of a partnership are treated as a collection of individual rights and obligations of its members. On the contrary, a partnership in Scotland is a legal person distinct from its partners, and therefore it can enter into contracts and acquire rights and obligations, it can own property, sue and be sued. It can also be a partner in another partnership (LC, 2003, p. 6-7).

A partnership is automatically dissolved on any change of a partner, but the remaining partners can agree to continue in partnership (Ministry of Justice, 2013). For introducing a new partner consent of all the existing partners is required (LC, 2003, p. 6). Regarding the retirement from a partnership at will, and in case that duration of the partnership is not fixed, the Act provides that any partner can determine the partnership at any time on giving notice of his intention to do so to all the other partners (s. 26).

Limited partnerships in the UK were introduced by the Limited Partnerships Act 1907. They are widely used for venture capital funds (Ministry of Justice, 2013), and present one of the most important vehicles for venture capital investment across Europe. In 2003 there were

about 3000-4000 limited partnerships that functioning in England and Wales and about 3000 in Scotland (LC, 2003, p. 2). Recently came into force The Legislative Reform (Limited Partnerships) Order 2009 which implements two of the Law Commission’s (2003) recommendations: making a certificate of registration conclusive evidence that a limited partnership has been formed at the date shown on the certificate; and requiring all new limited partnerships to include “Limited Partnership”, “LP” or equivalent at the end of their names.

Expanding the number of available business forms is essential for meeting the complex needs of different kinds of closely held firms (McCahery et al., 2013, p. 2). Today, traditional partnership laws are considered inappropriate in the current business climate which has led to the introduction of more suitable uncorporate business forms, first in the US, and later in some other countries. The term uncorporation is introduced to name the business forms which combine the best features of partnerships and corporations (Ribstein, 2010, referenced by McCahery et al., 2013, p. 1). These forms are usually considered as a kind of hybrid legal forms, and have attracted a lot of attention during the last two decades. McCahery and Vermeulen (2000, p. 14) argue that introduction of an efficient hybrid closely held form can reduce the costs and at the same time minimize the risk of opportunistic behaviour, which is important in stimulating development of a legal environment favorable to SMEs.

Beside the traditional limited partnership, there is also a relatively new form - limited liability partnership (LLP) in the United Kingdom, introduced by the Limited Liability Partnerships Act 2000 (LLPA 2000), which is designed for professional or trading partnerships. It has no parallel in the rest of the observed countries, but is somewhat similar to the US limited liability partnership (Andenas and Wooldridge, 2009, p. 102) and more to the US limited liability company (Bradley, 2001, p. 339). This new form has legal personality and a qualified form of limited liability. Thus, partners actively involved in the business are enabled to limit their liability for partnership’s obligations (LC, 2003, p. 2). The new limited liability forms in the US which preceded the introduction of the LLP in the UK have reduced the importance of the general partnership (Bradley, 2001, p. 330), causing claims on the “death of partnership” (Ribstein, 1992, referenced by Bradley, 2001, p. 330) and the “death of liability” (Lopucki, 1996, referenced by Bradley, 2001, p. 330). The use of the new form in the UK also raises questions of competition between the EU member states (Bradley, 2001, p. 341).

The introduction of this form of partnership in the UK (and previously the US) is the result of the pressure from professional partnerships and their concerns for the increase in liability claims, especially for professional negligence. The reasoning goes that partners in a large partnership are not really capable of supervising or controlling the other partners’ activities, so they should not be held liable for their actions. Of course, there are the opposite claims warning about the position of an injured third party. However, some argue based on the 1998 judgment in Williams and Another v. Natural Life Health Foods Limited and Mistlin case that the new form of limited liability partnership in the UK cannot effectively limit the liability of its members (Andenas and Wooldridge, 2009, p. 102).

Bradley (2001, p. 339) points out that the LLPA 2000 does not specify if there are any circumstances in which members of an LLP will be personally liable, and they should be only concerned about the potential tort liability. The Law Commissions take the viewpoint that if a partner commits a negligent act in the course of the partnership’s business, he cannot enjoy the benefit of limited liability with respect to that act (LC, 2003, p. 2). As a consequence, negligent members are liable to injured third parties to the full extent of their assets (Andenas
and Wooldridge, 2009). Also, in case of wounding up, members can be required to contribute to the partnership’s assets (s. 1(4) of the LLPA 2000).

Unlike the other partnership forms, the British LLP is considerably regulated due to the limited liability. It is also very different from its US counterpart, because it shares many characteristics with corporations and therefore the applicable rules are adaptations of the rules which apply to limited liability companies, rather than general partnerships. That is even the case with the creditor protection mechanisms (Bradley, 2001, pp. 338-340). So, provisions of the Companies Act 1985 relating to disclosure of financial information, the Company Directors Disqualification Act 1986 and of the Insolvency Act 1986 apply to it (LC, 2003, p. 2; Andenas and Wooldridge, 2009, p. 102).

Even though they have partnership governance structure (McCahery and Vermeulen, 2000, p. 36), LLPs don’t enjoy the privacy in financial matters as other partnerships do, and they incur costs of preparing, filing and auditing of financial statements. However, they are taxed as partnerships (Bradley, 2001, pp. 339-340). For these reasons limited liability in the UK involves greater costs than in the US (Bradley, 2001, pp. 331). The need for creditor protection on one side and the commitment to supply legal rules which will enable owners to maximize wealth on the other side is exactly the tradeoff explaining the debate on regulation of closely held firms (McCahery and Vermeulen, 2000, p. 2). McCahery and Vermeulen (2000, pp. 37-39) argue that the UK LLP therefore does not represent a successful low cost solution for SMEs, but only a response to the demands of a particular class of firms.

In the US the costs of forming and maintaining an LLP are higher than the same costs required for a general partnership. According to Bradley (2001, pp. 331, 337-338), forming a general partnership in the US in many cases now would be irrational, as these costs are relatively small in comparison to the benefits of reduced liability. Because of the above mentioned costs, situation is different in the UK. In 2003 the number of incorporated LLPs was 5420 in England and Wales and approximately 250-260 in Scotland (LC, 2003, p. 3). It is assumed that the vast majority of partnerships in the UK will remain general partnerships, while limited partnerships and LLPs will be used only as useful vehicles for particular businesses (LC, 2003, p. 3). There are criticisms questioning the effectiveness of both the US LLC and the UK LLP for small businesses (McCahery and Vermeulen, 2000, p. 7-8).

Limited partnership with shares is a compound of the limited partnership and the public company. They were popular during the earlier part of the nineteenth century due to the fact that formation of a public limited liability company required a state permission. On the contrary, no such permission was required to form a limited partnership with shares. Today, limited partnerships with shares are in restricted use in Belgium, France (where allegedly they have been undergoing a certain revival), Germany, Italy and Spain. This form is unknown in the United Kingdom, and it ceased to exist in the Netherlands after the company law reform in 1971 (Andenas and Wooldridge, 2009).

Similar to the limited partnership, a limited partnership with shares has two kinds of members. One of them are general or unlimited partners, which have unlimited liability, i.e. they are jointly and severally liable for the debts of the partnership without limitations. Most often, general partners are the managers or directors of the partnership. The other kind of members is limited partners, which are holders of transferable shares in the partnership and enjoy limited liability, i.e. they are only liable for the debts of the partnership to the extent of
their contributions. Therefore, limited partnerships with shares can be quoted on stock exchanges, and, as a rule, they have legal personality. They are considered a sort of a combination between public limited liability company and limited partnership, and are governed by a mixed legal regime that applies to these forms in different countries. Some of the specific characteristics of this form in France and Germany are outlined below.

French *société en commandite par actions* (SCA) is considered a kind of a corporation, and is governed by provisions of the French Commercial Code of 1999 along with the *société anonyme* (SA). General partners (commandités) in the SCA, unlike the limited ones (commanditaires) who hold transferable shares identical to the shares in a SA, need a consent of all the other members in order to transfer their shares. Directors of the SCA can be general partners or outsiders, but not limited partners in it. The above mentioned recent revival of this form in France is partly explained by the possibility of raising a considerable amount of capital by using this form, while at the same time, the management of the SCA remains with a small number of members (general partners), whose shares represent only a small fraction of the capital. Also, the management structure of the SCA is more flexible than of the SA (Andenas and Wooldridge, 2009).

Despite the flexibility described, it seems that limited partnership with shares is even less used in Germany than in France. Similarly, it is defined and regulated by the provisions of the German Stock Corporations Act (*Aktiengesetz* - AktG). At the same time, the relationships between partners, and between partners and third parties are regulated by the provisions of the German Commercial Code (HGB) which regulates limited partnerships. General partners have the power to manage and represent limited partnership with shares. A general partner in German *Kommanditgesellschaft auf Aktien* (KGaA) can be a GmbH or a *GmbH & Co KG*.

One of the hybrid legal forms available that include a partnership is *GmbH & Co. KG* which was considerably used in past to avoid double taxation under German law. Even though those reasons after the year 1976 no longer exist, this form remains popular in Germany for other reasons. Similarly, in France exists *société en commandite simple à responsabilité limitée*. Both of these entities consist of a limited partnership in which the general (unlimited) partner is usually a private limited liability company, while directors of that private company are limited partners (Andenas and Wooldridge, 2009).

New hybrid legal forms have been in use in France and Germany recently, namely *société en commandite par actions* (SCA) à responsabilité limitée and *GmbH & Co. KGaA*. Both of these forms consist of a limited partnership with shares whose shareholders have limited liability, and of a private limited liability company (SARL or GmbH) which is the general partner in this entity and therefore has unlimited liability. It is usually the case that directors of that private company are directors of the hybrid entity at the same time, and often they are family members or close friends. This way these persons avoid unlimited liability, which would be imposed on them if they were members of a SCA in France or a KGaA in Germany. For this reason the legality of these forms has been questioned in France, but upheld by some German courts. Those hybrid formes proved to be useful for a number of purposes, e.g. for fighting takeover bids *SCA à responsabilité limitée* in France (Andenas and Wooldridge, 2009). In France also exists *groupement d’intérêt économique* (GIE), a form that was introduced in 1967 and which has characteristics of both a company and a partnership (Andenas and Wooldridge, 2009).
3. PARTNERSHIP FORMS IN BOSNIA & HERZEGOVINA AND CROATIA

Croatian company law is developed based on the German legal experiences and law of the European union (Barbic, 2007, p. 344-345). In accordance with that, Croatian law recognizes almost all kinds of partnerships that exist in German law, except for the limited partnership with shares which has not been introduced due to the constant reduce of its significance, and the Partnerschaftsgesellschaft (Barbic, 2007, p. 353). Autonomy in regulating internal relations is very high in case of partnerships, and considerably narrowed in case of corporations (Barbic, 2007, p. 352). Unlike the German law, Croatian law recognizes legal personality of partnership forms for practical reasons, following the approach of the French law in this respect. Only civil and secret partnership lack legal personality (Barbic, 2007, p. 353).

Company laws in both entities of Bosnia and Herzegovina recognize only two partnership forms: general and limited partnerships. Both forms have legal personality. There is a possibility of transforming a limited partnership into a limited partnership with shares under the Law on companies of the Federation of B&H, but without any further provisions in respect of that form. There are not many law provisions dealing with partnership forms in the Federation of B&H, which therefore leaves many legal uncertainties and could be one of the reasons of avoiding these forms.

There has not been much use of partnership forms in both B&H and Croatia, mainly due to the unlimited liability imposed on partnerships’ members. There were only 307 general partnerships active in Croatia in September 2014. There is no precise data on the number of limited partnerships in Croatia, but there are currently more than 100 registered limited partnerships mainly in dealing with protection services in the Croatian court registry. According to the electronic court registries of business entities in B&H, there are only two general partnerships currently registered in the Federation of B&H and one limited partnership which is registered in the District of Brcko. No special tax provisions apply to these partnership forms in both B&H and Croatia (CEPOR, 2013, p. 38).

The most widely used form of organising business (if sole proprietorship excluded) is the form of the limited liability company in both of these countries. Beside the regular limited liability company, and following the German legal reforms, in Croatia was in 2012. introduced a simple limited liability company (jednostavno društvo s ograničenom odgovornoscu) as a transition form to the regular one, which is gaining on its significance in terms of the number of active businesses using this form. One of the goals of introducing this form was making it easier to start up a business by allowing up to three founders to found a company basically without taking in capital, while at the same time they can enjoy the limited liability (Brnabic and Ivancev, 2014, p. 450). The concerns about the risk of opportunism towards company's creditors have proven true in the German court practice, and the form didn't provide the flexibility nor proved as competitive as it was expected (Brnabic and Ivancev, 2014, p. 452). There is no such counterpart in the legal system of B&H.

4. CONCLUSION

Increasing the competitiveness of SMEs in Bosnia and Herzegovina and Croatia is considered to be of great importance and a key priority in the way of future economic development. Possibly, introducing new business forms which will satisfy more the needs of SMEs can help in accomplishing that goal and increasing the number of start-ups. Introduction of an efficient hybrid closely held form can reduce the costs and at the same time minimize the risk of opportunistic behaviour, which is important in stimulating development of a legal

175 http://www.hok.hr/statistika/trgovacka_drustva_i_obrtni
176 http://www.hok.hr/statistika/trgovacka_drustva_i_obrtni
environment favorable to SMEs (McCahery and Vermeulen, 2000, p. 14). Also, introducing new business forms can be considered in terms of regulatory competition among jurisdictions, especially Croatia as a member of the EU, but that is out of the scope of this paper.

According to the previous research, European company law requirements imposed on the closely held businesses using limited liability company forms, such as minimum capital requirements, disclosure and other mandatory rules, do not suit the needs of SMEs and act on their disadvantage (McCahery and Vermeulen, 2000, p. 13). These requirements are mostly transposed into the legal systems of both B&H and Croatia, where the most widely used form of organising business (if sole proprietorship excluded) is exactly the form of the limited liability company. Even though the simple form of the limited liability company recently introduced in Croatia is gaining on its significance, there are some indications that this form also does not completely suit the needs of SMEs. Instead of minimizing, it increases the risk of opportunistic behaviour. As for the B&H, where there is not even this option, this issue is of primary importance as this country ranks 174 on starting a business (DB, 2014, p. 180).

Recent trends and available research point out that potential answers lie in introducing hybrid legal forms which will combine the most suitable features of partnership and corporate forms. Specifically, as also argued by McCahery and Vermeulen (2000, p. 56) SMEs should be granted access to the limited liability, high degree of flexibility, and preferential tax treatment. Having in mind the UK experiences with the introduction of LLP, the development of a potential new form of business organization should be made in response to the specific needs of SMEs in these countries. Different ranks on enforcing contracts (115 for B&H and 49 Croatia) and resolving insolvency (77 for B&H and 98 Croatia) point to the one specific need to be taken into consideration specifically in case of B&H and that is creditor protection (DB, 2014, pp. 180, 187).

Blair (2003, p. 16) argues that the reason behind the opting for the corporate form in past was mainly the legal separateness as the „singular accomplishment of corporate law“ in terms of separating ownership from control and providing the ability to lock in the existing capital, and not the limited liability. According to Bubb (2015, p. 356), the partnership form was optimal for a debt-financed business due to the unlimited liability in particular, which also reduced partners' incentives to act opportunistically towards the creditors. Exactly the opportunism is what scholars are concerned about when it comes to the newly introduced forms combining characteristics of partnerships and corporations (McCahery and Vermeulen, 2000, p. 8). Therefore, even though businesses so far opted almost exclusively for company forms with limited liability, the unlimited liability option should not be completely abandoned.

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18. The Limited Liability Partnerships Act 2000, United Kingdom

19. The Partnership Act 1890, United Kingdom

ROLE OF SMEs IN THE ECONOMIC DEVELOPMENT

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ABSTRACT
The aim of this paper is the analysis of data regarding the SME sector in Kosovo, the presentation of current positive and negative development trends within this sector as well as offering recommendations towards the intensification of government incentives towards creating a sustainable environment for SME development, focused on the economic development of Kosovo.

This paper analyzes (i) data regarding SME development in Kosovo such as: size, activity, legal status, business age, strategic orientation of SMEs, their financing sources, SME contribution in GDP, their international activities, their impact in the labor market and other relevant data, (ii) data regarding existing barriers, opportunities and challenges towards SME development in Kosovo as well as (iii) data regarding developmental support for the private sector through government policies and SME development strategic aims.

Aiming on creating the environment for supporting sustainable business development and employability optimization, emphasis should be given to: reduction of administrative and regulatory obstacles towards establishing new businesses as well as developing existing ones; improvement of businesses’ access to funding opportunities especially for startups; reporting from SMEs in compliance with established standards; integration of prevalent informal economies into the formal economy; promotion of entrepreneurial culture and other alternative solutions for promoting SME growth as a catalyst for economic growth and unemployment reduction.

Keywords: Economic development, SMEs, Kosovo, policy support, employability.

1. INTRODUCTION
Throughout all countries, regardless of their development level, SMEs exert an important role in economic development, noting that SMEs are a source of employment, competitiveness, economical dynamism and innovativeness.

Due to the importance of SMEs in job creation, economic development and innovativeness, the government should take responsibility into stimulating further growth of SMEs in Kosovo.

In such context, self-employment and entrepreneurship become a priority for citizens, local authorities and decision makers alike as means of income generation and new job creation. Since a considerable amount of new jobs are created through establishing new SMEs and developing existing ones, the successful implementation of the Strategy for SMEs will become the main contributor of economic growth in Kosovo.
Policies design for the creation of a sustainable environment for business development facilitates on the development of core personnel, thus ensuring SME success.

2. DATA REGARDING SME DEVELOPMENT IN KOSOVO

The business analysis regarding size, legal form of organization, economic activities, age, their participation in foreign trade, strategic orientation and funding methods comprise some of the data that offer a more detailed overview of the operation and development of businesses in Kosovo, and as such will be duly analyzed. Because in various institutional reports, often the number of registered businesses include non-active ones, this paper will use data published by the Kosovo SME Promotion Programme (KOSME)\(^{177}\), as they are based on the data from Kosovo Tax Administration (ATK).

**Enterprises according to size and employee number.** Size of SMEs in Kosovo is defined by the Law no. 2005/02-L5 and the Law no. 03/L-031 on Supporting the Small and Medium Enterprises. The employee number is the sole criterion used to classify enterprises according to size in Kosovo; in comparison to EU countries – where except employee number, annual turnover is taken into consideration as well.

<table>
<thead>
<tr>
<th>Classification</th>
<th>Enterprises</th>
<th>Persons employed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number</td>
<td>Share (%)</td>
</tr>
<tr>
<td>1 person employed</td>
<td>25,938</td>
<td>56.3</td>
</tr>
<tr>
<td>2-9 persons employed</td>
<td>17,797</td>
<td>38.7</td>
</tr>
<tr>
<td>10-49 persons employed</td>
<td>1,940</td>
<td>4.2</td>
</tr>
<tr>
<td>50-249 persons employed</td>
<td>310</td>
<td>0.7</td>
</tr>
<tr>
<td>250+ persons employed</td>
<td>47</td>
<td>0.1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>46,032</strong></td>
<td><strong>100.0</strong></td>
</tr>
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*Table.1. Number of enterprises in the private sector according to size and employee number (KOSME, Report on SMEs in Kosovo 2014, p.4)*

From the data above, it is seen that from a total of 46,032 enterprises, a majority of them (56.3%) are single-employee enterprises, 38.7% are microenterprises which are the biggest employers in the private sector at 31.9%, medium enterprises at 0.7% which encompasses 16.4% of the private sector employment as well as large enterprises at 0.1% share accumulating 19.3 of private sector employees. Thus, SME sector participates with more than 80% of employees, whereas large firms retain less than 20% share of private sector workforce.

\(^{177}\) ECIKS and KMU Forschung, Kosovo SME Promotion Programme (KOSME), Report on SMEs in Kosovo 2014. A report on the state of the private sector in Kosovo, published by KOSME on behalf of the Kosovo Investment Enterprise Support Agency (KIESA). KOSME provides capacity development to the Ministry of Trade and Industry with financial support from Austrian Development Cooperation and Swiss Development Cooperation and is implemented by ECIKS and KMU Forschung.
When compared to the trend of the amount of registered enterprises in the region and the BE27, it can be clearly observed that the ratio of SMEs to the overall number of enterprises is dominant in both of these two regions (Figure 1).178

According to the legal form of organization, individual businesses are dominant, including sole proprietorships (92%) and micro-businesses (77%). It is also observed that medium enterprises are more often organized as limited liability companies; where even up to 10% of surveyed individual businesses plan to switch their legal form of organization into a LLC.179

Based on the data of the Kosovo Agency of Statistics for the fourth trimesters (T4), in 2012 only 16.6% of businesses were organized as limited liability companies, in 2014 this ratio amounted to 22.9% meaning that there is a positive trend of adopting the limited liability model of firms’ legal organization.180 Except LLCs, firms are also organized as joint stock corporations which in the fourth trimester of 2014 participate at 0.4%, general partnerships at 0.8% and foreign firms at 0.9%.181

According to economic activities, retail and wholesale trade are dominant at 43% as compared to other activities along with accumulating 33% of workforce. Second by share is the manufacturing sector with 10.5% of overall business count and approximately 16% of the workforce. Of a similar importance are also business services at 10.2% of businesses and 13% share of the workforce, whereas other activities have a more modest participation.

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178 European Commission, the European Bank for Reconstruction and Development (EBRD), the European Training Foundation (ETF) and the Organisation for Economic Co-operation and Development (OECD), Report of SME POLICY INDEX 2012-Western Balkans and Turkey-July, Brussel, 2012
179 ECIKS and KMU Forschung, KOSME, Report on SMEs in Kosovo 2014, pg. 16.
Table. 2. Number of private enterprises and persons employed, by sector, in 2013 (Kosovo SME Promotion Programme, Report on SMEs in Kosovo 2014, pg. 6)

Analyzed from the perspective of business sustainability, the following table depicts data that provide insight that new entrants are more prevalent in the construction and business services sectors at 19%, sectors that also record a lower ratio of business closures.

Table. 3. Number of start-ups (entries) and closures (exits) of businesses in 2013, by sector (Kosovo SME Promotion Programme, Report on SMEs in Kosovo 2014, p.12.)

According to numerous studies, the main reasons of business closures in Kosovo are attributed to the lack of funding mechanisms in businesses, insufficient research and planning, lack of timely identification of business problems, lack of preliminary experience in business, unfair competition, etc.

Business Age - There is an advantage regarding the age of business owners because a considerable part of them are young, namely half of them are less than 40 years old. Based on the results from the survey conducted by Kosovo SME Promotion Programme, business owners at the time of founding their business were in average less than 30 years old.

Female Entrepreneurs are quite active, yet there is a rather acute number of women as business owners. Thus, according to the KOSME survey, 13% of SMEs are owned by women whereas in 3% of them women are co-owners. Their largest participation is in business services where 23% enterprises respectively are owned/managed by women, whereas in other sectors women participation is low. Women-led firms are also younger in average than those led by male counterparts.
Policies attributed to SMEs should be targeted to such entrepreneur groups, with an objective to improve the diversity of entrepreneurs in Kosovo and consequently raise the overall potential for economic development. Through improving competences of women towards SME development, such a measure should be thoroughly planned and implemented, because women amass an important share of activities in the private sector and thus contribute considerably in poverty reduction. Equal participation of both genders needs more actualization in strategies and programs regarding SME development, using specific, targeted solutions for existing obstacles.\footnote{OECD Conference of ministers responsible for small and medium-sized enterprises, Promoting SMEs for development, Istanbul, Turkey 3-5 June 2004, pg.5,6.}

**Strategic orientation of SMEs** – Businesses in overall, aimed at profit maximization and consolidation of their competitive advantages are led by differing strategic orientations. They tend to use the low cost and pricing strategy as well as focused strategy of offering premier quality products and services. As observed in the following table, ambitions toward the latter discussed strategy are more prevalent (40\%) whereas 26\% of businesses give priority to low cost and pricing strategy. However, noticeable differences exist between the sectors.

<table>
<thead>
<tr>
<th>Sector</th>
<th>Businesses focussing on low costs (%)</th>
<th>Businesses focussing on improving quality (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>21%</td>
<td>35%</td>
</tr>
<tr>
<td>Construction</td>
<td>42%</td>
<td>43%</td>
</tr>
<tr>
<td>Wholesale and retail trade</td>
<td>33%</td>
<td>40%</td>
</tr>
<tr>
<td>Transporting and storage</td>
<td>35%</td>
<td>41%</td>
</tr>
<tr>
<td>Accommodation &amp; food service</td>
<td>17%</td>
<td>43%</td>
</tr>
<tr>
<td>Business services</td>
<td>6%</td>
<td>51%</td>
</tr>
<tr>
<td>Personal services</td>
<td>13%</td>
<td>43%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>26%</td>
<td>41%</td>
</tr>
</tbody>
</table>

*Tab.4. Strategic orientation of SMEs, by sectors (ECIKS and KMU Forschung- KOSME, Report on SMEs in Kosovo 2014, p.25.)*

**Funding Sources** - Access to funding remains problematic for many businesses in Kosovo according to surveys SMAPN.\footnote{SMAPN- Sondazhi për Mjedisin Afarist dhe Performancën e Ndërmarrjeve, Banka Evropiane per Rindertitim dhe Zhvillim, Strategji per Kosoven, 2013.} In this survey, approximately 60\% of the SMEs have stressed that they had to apply for loans during the recent years. For example, in the business services sector, bank loans were utilized only by 24\% of enterprises, whereas the manufacturing, construction, and transport sectors have utilized bank loans by 50\% of businesses. This is related to higher amounts of funding required and also to investments often being made in long-term fixed assets. Thus, one of the problems faced by businesses regarding bank funding are unfavorable crediting conditions and high interest rates. Businesses need financial support, especially
small firms and startups, which can be achieved through micro-financial instruments entailing more favorable loan conditions as an imperative for the creation and development of already established businesses.

**International business activities of SMEs** – As per WB reports, economic progress in Kosovo is attributed to donor aid and remittances in the recent years, which is not a solid base for a sustainable economic strategy. Researchers support the idea that an outward export strategy and a subsequently coherent trade strategy are necessary steps for small economies to reach sustainable growth.\(^\text{184}\)

Taking into consideration the challenges that SMEs face in Kosovo, their contribution in the economic performance and especially in the trade balance is relatively insignificant.\(^\text{185}\)

The share of SME exports is relatively small. Based on survey data, \(^\text{186}\) 5% of businesses claim to have direct sales channels abroad whereas another 1% export indirectly through an agent or another intermediary in Kosovo. The prevalence of exports is more attributable for small and medium-sized businesses than micro-enterprises.

Countries that are considered as influential exporting partners for Kosovo as per the SME sector include Albania, Macedonia, Montenegro, Germany, Switzerland, Austria, Italy, and the US.

The same survey also depicts that SMEs that are engaged in exports have fared better than those SMEs that have not done so, in terms of growth in revenue. More than 50% of SMEs engaged in exports have achieved a growth rate of more than 5%; a figure matched by only 25% of non-exporting SMEs. On the other hand, only 12% of exporting SMEs faced a decline of turnover in contrast to more than 30% decline of non-exporting SMEs. The main issues faced by firms is attributed to finding clients or agents abroad. Travelling restrictions follow as second in rank as obstacles that caused problems to 50% of exporting SMEs.

Among SMEs in Kosovo, import has a more significant presence than export: 15% of firms are engaged in direct purchase of goods or services from abroad whereas another 15% are conducting such purchase using an intermediary in Kosovo. The importing incidence increases with firm size. Half of small and medium-sized businesses are direct importers.\(^\text{187}\)

Thus, increasing exports among SMEs should be considered as another focus of the SME policy.

### 3. BUSINESS ENVIRONMENT FOR SME DEVELOPMENT IN KOSOVO

The country ranking from the World Bank report on Doing Business has instilled competition between countries aimed at improving their doing business status, having specifically affected policymaking in these countries.

In Kosovo, the Ministry of Trade and Industry is the institution with the core competences to address the business climate.

According to the World Bank report on “Doing Business 2015”,\(^\text{188}\) Kosovo has progressed to the 75\(^{\text{th}}\) place, witnessing a steady increase from previous years. In the World Bank report “Doing Business 2013” Kosovo was ranked 98\(^{\text{th}}\) from a pool of 187 countries.

Implementation of reforms aimed at facilitating business registration procedures that have contributed to such progress have included: removal of work permits, reduction of required documentation for import and export, elimination of business registration fees, elimination or

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\(^{185}\) UNDP, Vleresin baze i rajonit ekonomik jug, 2014, pg.7.

\(^{186}\) Kosovo SME Promotion Programme, Report on SMEs in Kosovo 2014

\(^{187}\) Burimi I njejte, p.29.

\(^{188}\) The rankings are benchmarked to June 2014 and based on the average of each economy’s distance to frontier (DTF) scores for the 10 topics included in this year’s aggregate ranking
reduction of capital requirements, as well as there has been an improvement towards protection of foreign investors. Additionally, aimed at improving transparency, and offering “one-stop-shop” services, most municipalities have functionalized “Centers for Business Services”. Such centers provide all services related to business registration, industrial property services as well as informative materials regarding Doing Business reforms and an array of other services\(^\text{189}\).


Competitive enterprises should implement international standards. Council for Standardization in Kosovo will be more oriented towards SMEs so they can be encouraged to understand that quality should be a measure of their competitiveness\(^\text{190}\).

**SMEs and the informal economy** – Regarding the size of the informal economy in Kosovo only estimations can be encountered, as objective data do not exist. The informal economy as a ratio of the entire economy in Kosovo is estimated to be at similar level to other countries of the Western Balkans. In the National Strategy for the Prevention of Informal Economy it is presented that according to regional estimations covering the 2006-2012 timeframe, the informal economy ratio in Kosovo’s neighboring countries varies between 23-38.8% of GDP\(^\text{191}\). The informal economy is an obstruction of fair competition and increases the relative costs of businesses working in the formal sector. Informality diminishes the trust between SMEs and the financial institutions, reduces SMEs’ access to funds as well as their ability to


\(^{191}\) Qeveria e Republikes se Kosoves, Strategjia kombetare per prandalimin e ekonomise joformale.
utilize formal mechanisms of conflict resolutions. The presence of informal economy also discourages foreign investments. There is a need for the analysis and figuring up modalities for the integration of the informal economy within the formal economy, along with the elimination of factors that have a discouraging impact on SMEs regarding formally registering employees, firm’s turnover and profit at relevant institutions.

4. STRATEGIC OBJECTIVES FOR SME DEVELOPMENT
The Government of the Republic of Kosovo, in July 2011, has adopted the Strategy for SME Development for the 2012 – 2016 period. Ministry of Trade and Industry (MTI) is responsible for strategy design through the Agency for SME Support. Strategy for SMEs is a sub-sectorial component of the Strategy for National Development of Kosovo and includes a number of Government Agencies which are responsible for parts of their implementation.

The Strategy contains seven strategic aims as follows:

**Strengthening the legislative and regulative framework for the creation and development of SMEs** based on the “Think Small First” principle that aims to streamline the existing legal and regulative framework, to improve inter-ministerial support for the implementation of the Strategy for SMEs, to improve the facilitation of starting and closing businesses, to increase the number of SMEs entering the formal sector. It is important to exert efforts for improving the annual report regarding SME statistics because as much is proven to be required.

**Improvement of SMEs access to finance** that could be achieved from the materialization of objectives such as: development, expansion and promotion of financing instruments spectrum for SMEs, attracting and directing diaspora funds towards SMEs, implementation of training programs for the understanding of funding options and applying for financing as well as other forms of support aimed at improving access to finances.

**Promotion and Development of Entrepreneurial Culture** through the promotion and increase of cooperation between universities, vocational schools and businesses, stimulation of creativity and innovativeness, increase of cooperation with SME relevant international institutions. An important best practice to be used are experiences regarding “virtual firms” or “practical firms” implemented in Austria and Germany –as business models based on actual firms to stimulate entrepreneurship learning for students; “Supervisors’ Network” in Ireland–where businesses profit from advices of experienced entrepreneurs; “Business Information Systems” in Finland –where entrepreneurs register their business with a single registration application procured through a single contact as well as other successful experiences.

**Strengthening of local and international SME competitiveness** which could be carried on through strategic aims as follows: Development of technical, innovative and managerial skills of SMEs in accordance to the EU Program for policy support regarding Information and Communication Technologies. Implementation of international standards and Quality Management Systems for SMEs, Development of a plan for import substitution to support SMEs to remain competitive in the internal market, facilitation of SME access in regional and other foreign markets as well.

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193 Ibid. pg. 17.
194 Ibid. pg.4.
195 MTI, SME Development Strategy for Kosovo 2012-2016, with vision 2020, July 2011
Improvement of the dialogue between the private sector, public sector and civil society through raising awareness of the role of SMEs in Kosovo’s economic development, and systematically increasing responsibilities of institutions regarding SMEs.

**Strengthening SME Supporting Institutions** (economic zones, business parks, business incubators, Municipal Business Centers and other forms of SME support)

**Improvement of the position of female entrepreneurs (and other entrepreneurial groups)** by implementing: design of facilities for investment by female entrepreneurs, promotion and development of support programs to encourage female entrepreneurs, establishment and development of new firms, design of specialized training programs, development of funding opportunities, development of business incubators for female entrepreneurs.

The successful implementation of the Strategy for SMEs will support the facilitation of numerous obstacles regarding economic growth, would increase private sector activities, will increase foreign and domestic investment and consequently will become the biggest contributor for new job creation. Also, governments are able to create environments in support of the long run development such as promoting education, training programs as well as the development of SME clusters. As such, the Strategy for SME development should be integrated in the context of a broader strategy for national development, poverty reduction and transitional/developing countries’ growth strategy. Embedded strategies aimed at SMEs and the private sector tend to strengthen SME capacities and improve their competitiveness domestically, regionally and globally.

5. CONCLUSIONS

Businesses play a critical role in Kosovo’s economic development and new job creation, thus there is a need for comprehensive support policies for the stimulation of startups as well as development of already established enterprises. This infers creating a positive entrepreneurial climate through which business would benefit, allowing them to invest in sustainable businesses.

Aiming on creating suitable conditions for the development of businesses and the maximization of employability, there is continuous requirement for the reduction of administrative and regulative obstacles regarding new business creation as well as the development of existing ones; development of advisory services for startups along with the support of SMEs towards human resources management and financial risk, improvement regarding access to funds especially for startups and existing businesses, stimulation of an entrepreneurial culture, etc.

Development of new businesses, expansion of existing ones, stimulation of self-employment should be focal for governmental and policymakers efforts in Kosovo, in order to reduce the unemployment and create profits in the long term.

This would also contribute towards the creation of favorable conditions for the integration of the informal economy as a part of the formal economy, a much discussed concept that has not yet been addressed sufficiently. The more stable an economy is, the less space remains for the informal economy, taking also into account that this might also contribute towards expanding horizons for successful firms in the formal economy.

Of critical importance is the provision of entrepreneurs with appropriate skills to be able to successfully compete in the market.

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Competitiveness and business dynamism are directly dependent from the regulatory environment regarding investment, innovation and entrepreneurship.

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LOW BUDGET HOME BASED BUSINESS: A PROPOSAL FOR SUSTAINABLE ENTREPRENEURSHIP FOR BRAZILIAN MEGACITIES (SAO PAULO)

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ABSTRACT
This study aims to analyze the contribution of the creation of daycare centers for seniors (typically non-medical services) and children to promote sustainable development as well as social support in urban centers of megacities in emerging economies of developing countries, like São Paulo/ Brazil. The current scenario presents: longer life expectancy and increasing numbers of older people; the growing presence of women in the market and the hierarchy of companies making more and more difficult for them to take care for small children and elderly as well as the failure of public care structure to respond adequately to citizens’ demands. In addition, families are getting smaller which removes potential caregivers within them. Large arrangements for caring can be useful in some contexts, but generally, require commuting from home to the support structure and new public and private investments. The potential reduction of human daily dislocations could improve the environment and life quality in megacities: decreasing CO2 emissions, pollution and the volume of traffic; giving practicality to everyday life of families with dependent members of care and generating new opportunities of small business. In addition, this new residential structures employment might reduce the need to shift the caregivers themselves to their work place, strengthen community bounds and not require immobilization of new properties of the exclusive use for Care centers in highly urbanized areas. The methodology used in this paper is based in the exploratory-descriptive and bibliographical-documentary method.

Keywords: daycare centers, low budget, megacities, developing countries, Sustainable entrepreneurship

1. INTRODUCTION
Several studies and proposals have been presented in the last decades, intended to protect and enhance the well-being of both present and future generations, by promoting sustained, inclusive and equitable economic growth, creating greater opportunities for all, reducing inequalities, raising basic standards of living, fostering equitable social development and inclusion, and promoting integrated and sustainable management of natural resources and ecosystems in urban areas. The challenge is to find ways to make change in the way of thinking and acting to meet the principles of sustainability, especially in megacities, like reconfiguration of productive spaces, change in the habits of the urban population and new public policy development for municipalities (MARIUZZO, 2012). Additionally to this list,
innovative business models that encompass sustainable point of view should be design. For the acquisition of sustainable city status, it is necessary, among other objectives, to achieve the reduction of emissions of CO$_2$ and other greenhouse gases and the increase in quality of life for residents through strategies that reduce air pollution and increase the mobility of the growing number of people living in this area.

Many of these displacements are implicit in the age profile of the population. Analyzing the demographic projections (Figure 1) it could be observed a substantial change that profile, leading to a potential alteration in daily flow of people. Two changes happened: the population increase in life expectancy and the fall in fertility and mortality rates. Thus day by day, there are more seniors and smaller number young people. This means that in Brazil, an increasing number of older people will need caring structures and there will be fewer youngsters to care for them in the future.

![Figure 1 – Age-sex structure and change in population pyramid, Brazil, 1980-2050. Brazilian Institute of Geography and Statistics - IBGE projections. Right side, males and left side, females.](image)


The same demographic projections point to smaller families in the future. The most common and consolidated default is 1 or 2 children per woman. This demographic trend creates a shortage of family members available to care for the elderly and small children. In this scenario, care business and related structures will be key to social support. In particular, the fact pointed out by Ramos: "The elderly in an urban center have a high prevalence of physical and mental disabilities, generating dependence in activities of daily living" (RAMOS, 2003: 794).

The so-called caregivers of elders is someone who can help them to develop actions, assuming this way the responsibility of providing support and assistance to these needs, improving their living conditions (RÓCHA JR et al., 2011). The care can be done informally (by someone: family or community) or formal, by a qualified professional, linked to a company or an entrepreneur, for example, working at home.
Lima (2010) exemplifies its viability, showing that this practice of Home-based business, already occurs in industrial clusters of footwear and clothing sector, spread over several regions of the country, highlighting the role of Public Policies (ALENCAR, 2007) in promoting the so-called “necessity entrepreneurship” through support to small business and the formalization of informal activities.

In 2008, the Brazilian government introduced the Individual Micro Entrepreneur Program - IMEP (in portuguese, Programa Microempreendedor Individual- BRAZIL, 2008) by Federal Law 128, a great national achievement in this new scenario of the economy, allowing millions of Brazilians to act in their own business, properly legalized. The IMEP is an opportunity for the workers to conquer their rights and formalize small business without paperwork or else cost (SEBRAE - Brazilian Service of Support for Micro and Small Enterprises, 2011). It also enables the implementation of projects that provide social support, not requiring either large displacements or new investments, object of this study.

The methodological approach for this study was descriptive and exploratory, qualitative basis from bibliographic and documentary research on the themes: sustainable development, carbon footprint and environmental aspects, urban centers, mobility, changing in age structure and population pyramid, quality of life, social inclusion, Entrepreneurship and public policy.

As a methodological approach, in this study the hypothetical-deductive method was adopted (DANE, 1990), where theories, concepts, data and empirical results from the literature were presented interactively, to justify the relevance of the proposal considering the future scenario.

2. CONCEPTUAL FRAMEWORK
Sustainability: an instrument for the economic, social and human development

The concept was first introduced in a Report prepared by the World Commission on Environment and Development in 1987 (Brundtland Report), where Sustainable Development (SD) was defined as one: "Development that meets the needs of the present without compromising the ability of future generations to meet their own needs." (WCED, 1987)

The concern about the environmental impacts of people and enterprises on the planet made this concept a major strategic benchmark, resulting in a continuous improvement process aimed at reducing the use of natural resources and reassessment of priorities.

In this way the concept of sustainability can be analyzed from two perspectives: the first includes both the nowadays society welfare and the society in the distant future, and the second implies the conservation of natural resources. In both cases, it should be considered in current and future policies, which include productive activities and income generation, mobility and transportation and urban land use (HEAL ;1998, apud PROSPECT, 2001).

The rapid changes in social, economic, technological and environmental, poses considerable challenges for traditional structures of governments and companies. Both non-governmental organizations and academics increasingly have expressed concern about the degradation and the eventual exhaustion of services of ecosystem due to the production and consumption processes. In this way, we can not dissociate the decrease in the use of natural resources and energy and reduction of CO₂ emissions to the commitment to sustainability.²⁰⁰

²⁰⁰ http://www.nsf.org/about-nsf/commitment-to-sustainability/
Quality of life and Urban Mobility

In the 90s the European Environmental Agency- EEA (1995) punctuated the needs of city dwellers should be provided without imposing unsustainable demands at the local level as much as the global ecological system. This study defined a series of goals to become a sustainable city:

- Minimize the consumption of space and natural resources;
- Rationalising and efficiently managing urban flows
- Protect the health of the urban population;
- Ensure equal access to resources and services;
- Maintain the social and cultural diversity.

Since January 2012, Brazil has a National Urban Mobility Policy (NUMP) - Law n.12.587 (BRAZIL, 2012), defining guidelines for regulation and planning in Brazilian cities. It is stated in According to NUMP, municipalities with more than 20,000 inhabitants (30% of Brazilian cities) should develop, until April 2015, an Urban Mobility Plan (UMP), collaboratively with civil society, covering a short, medium and long-term planning for movements of goods and people in the city (MINISTÉRIO DAS CIDADES - INSTITUTO POLIS, 2005; MINISTÉRIO DOS TRANSPORTES, 2013).

For example, in the Metropolitan Region of São Paulo (MRSP), vehicle emissions play a key role in the air quality, as they were responsible in 2005 of 97% of carbon monoxide (CO), 97% of hydrocarbon (HC), 96% of nitrogen oxides (NOx), 40% of particulate matter (PM) and 35% of sulfur oxides (SOX) released in the atmosphere (CETESB, 2007). The study by Hogan (2000) has identified that 78% of air pollution comes from vehicles operating daily in the city.

Another study shows that the transportation sector accounts for about 20% of global CO₂ emissions, which is a major cause of greenhouse gases, without regard to emissions of other gases also harmful to the environment and health (CARVALHO, 2011). The Kyoto Protocol, signed and ratified by Brazil, stated that the signatory developed countries had a period until 2012 to reduce emissions of greenhouse gases by around 5% from the total observed in 1990.

The report of World Business Council for Sustainable Development produced in the late 90 summarizes the agenda for the promotion of global sustainable development, centered on the concept of "eco-efficiency" (WBCSD, 1998), twenty years later reworked as "Green Economy" (DINIZ & BERMANN, 2012). According to the United Nations, the "Green Economy" is defined as one that "results in improved human well-being and social equity, while significantly reducing environmental risks and ecological scarcities" (UNITED NATIONS ..., 2011, p.16) because has low carbon emission, efficient use of resources and social inclusion.

The Organisation de Coopération et de Développement Économiques (OCDE) held in 2000, a forum to identify future trends under the theme "Man, nature and technology: sustainable companies in the XXI century", pointing to the emergence of a new economic and social order, based on the knowledge economy and democratic societies network (OCDE, 2001).

Individual initiatives are crucial to achieve a more sustainable society, nevertheless, it should not be forgotten that, the role of governments and public policies, are decisive. According Löffler (2001, p. 212), the term governance is related to "a new generation of administrative reforms and State, which have the purpose of joint action, carried out in an efficient, transparent and shared, by the State, companies and civil society to achieve an innovative
solution of social problems and creating opportunities and chances of a sustainable future development for all participants”.

Although several countries and cities (such as MRSP) have adopted measures to lower pollution levels, as the adjustment and adaptation of engines, reduction of toxic substances in fuels (lead and sulfur in gasoline) and even an alternating plate system of vehicles circulation in the central areas, air contamination is still a serious threat to human health and the environment.

Vormitag (2013 *apud* RUBIN & LEITAO, 2013) points out that in 2011 almost 27,000 hospitalizations in the MRSP were related to air pollution. In Sao Paulo, spending on these admissions reached approximately US$ 12 million.

Considering the 31 cities with the lowest urban mobility, Sao Paulo, is number two, right after Shanghai, China's largest city, and, in a ranking of the ten cities with longer dislocation time, five are Brazilian and all appear to be in more critical situation that the city of New York, which has one of the highest rates of motorization in the world (IPEA, 2013). The reduced mobility in an inadequate transport system and a great concentration of vehicles leads to an increased fatigue, sudden anger, anxiety and irritation of users. These factors are considered stressful and could affect one's emotional balance (ZERBINI *et al.*, 2009), compromising the quality of life and well-being of the local population. The work of Rezende (2012: 52) that evaluated the influence of transport on the worker's stress level in Brazil, mentions that "endure excessive stress on shipping may compromises the productivity and quality at work and influence on socio-emotional balance ", results also found by Wener and Evans (2011 *apud* REZENDE, 2012), comparing distances and time of urban displacement, caused by going back and forth to work in metropolitan area of New York.

In addition to the physical and psychological aspects, the loss of urban mobility has economic impacts in the city. According to study by the Getulio Vargas Foundation (FGV), the Sao Paulo traffic brought to the city losses of approximately US $ 15 billion in 2012. This represents 1% of GDP, with each citizen leaving to earn or spend about US $ 1.35 while imprisoned, totally unproductive, in traffic jams (RUBIN & LEITÃO, 2013).

In Rio de Janeiro about 47.3 minutes is spent in traffic just to get to work. In Sao Paulo, is approximately 45.8 minutes according to the PNAD 2012 (National Research by Household Sample- IBGE, 2011). This consumption of time the displacement challenges one to seek new paths of development in which the individual does not need to drive more than 20 minutes to have access to work, education and leisure.

The research Zandonade and Moretti (2012) mentions that "metropolis and urban sprawl have made the mobility system, which before was secondary in the relationship between the definition and forms of housing and ways of working, in a structuring element of these systems into the urban fabric ".

From this premise, reducing the need to travel by structuring small residential care centers for seniors and children, in regions close to the houses have the ability to contribute to an increase in the health conditions, quality of life and well being of citizens, as well as reduce emissions CO₂, promoting thus SD and a social support mechanisms in urban centers. Not to mention that, caregivers shall be released from of the stress of traffic jams, increasing willingness and attention to the complex needs of the care dependents.
Women at work and new family arrangements

The women's work has always been present in history, initially restricted to women of the lower classes. However, since the 50s, it has been observed a increasingly valuation of work by women of the middle and upper layers. Faced with the task of reconciling their professional activities and care for children, women that work outside the home seek several arrangements: grandparents, aunts, babysitters, day care centers and schools. With age changes the family caregivers will be available. Furthermore, modern family structures are quite different from previous generations ones. Numerous social changes coincided: divorces, serial marriages, single motherhood, migration to seek better alternative employment and income, option not to have children, full participation of women in the labour market. etc. All these movements cause a new venture: to built caring structure for children and seniors.

Children and their care in small residential centers

Continuous economic and cultural changes are reflected in social transformation, causing universal changes in the functioning of families and education of young children (Economic Commission for Latin America and the Caribbean - CEPAL, 1994). For Cochran (1993), the development of policies and programs of a country is the result of a combination of demographic, economic, cultural and social elements, referred to by the author as "causal factors".

For example, in the suburbs and neighborhoods of social vulnerability residents, it is common practice to increase the income of the family, to take care of small children of neighbors by receiving a monthly fee: a Minding mother. According to the study by Almeida (2007) in Rio de Janeiro, in the slums in general "there are few public day-care centers and most families can not afford a private nursery."

This is also the reality found in large Brazilian cities such as São Paulo, where the number of vacancies in the public education system for children does not meet the needs of lower classes and where the poor mobility and transportation cost can be limiting factors for working women. Alternatives and appropriate forms of child caring have been proposed to reduce social inequality. In 1986, Rosenberg had already pointed out in his article "home Kindergartens: arguments or fallacies" commenting that the practice was encouraged by international organizations (OMEP and UNICEF) since it reconcile low cost, low technology and community participation.

Rossetti-Ferreira et al (2002) mentioned that multilateral agencies such as the World Bank, have designed educational programs / child care in developing countries as a social intervention in order to overcome the inequalities where the service provided by mothers in their own homes, the so-called mother-Minding program. Worthy to mention, it is also effected in so-called developed countries, such as in the Nordic countries, which have great tradition in this type of care.

The diversity of models guard and education of young children in many countries shows an undeniable potential for the model home day care (ROSENBERG, 1989), however, these specific advantages must be supported by public policy to formalize the activity and teaching support guarantee for the substitute mother (Minding) considering her role in education at this stage of child development.

Corroborating the idea presented in this study about the implementation of small residential caring centers (home day care), there is the World Bank's suggestion for developing countries:
"The use of private houses with a minimal infrastructure [...] is sufficient" to enlarge the care opportunities of children under school age (YOUNG, 1996, *apud* ROSSETTI-FERREIRA, 2002).

Furthermore, the experience developed in Campo Grande Municipality (Mato Grosso do Sul/ Brazil) reinforces the use of this strategy, a program of home day care implemented and evaluated by the World Organization for Education - OMEP, with the conclusion that this service was relevant in the communities in which they were inserted (SIMPÃO & MORETTINI, 1996). This is also a reality applicable to the care of dependent senior with no medical issues.

**Elderly and their care in small residential centers**

Following the classification proposed by the World Health Organization (WHO) for developing countries, is considered senior, individuals aged 60 or more (IBGE, 2011). As mentioned earlier, there is a tendency of increase in the number of elderly in the coming decades, fueled by higher life expectancy, as pointed out by demographers.

In Brazil, the 1988 Federal Constitution, the Elderly National Policy (BRAZIL, 1994) and the Elderly Statute (BRAZIL, 2003) consider that the support for seniors is the responsibility of the family, the state and society. Brazilian law predicts the "construction of a network of services for the elderly, to meet biopsychosocial needs, if possible at home or nearby" (MELLO, 2007).

Despite this fact, Ribeiro *et al.* (2008) study pointed out that the permanence of the elderly in their own home requires supervision and an environment that can reduce the likelihood of accidents (which often occur due to a wet floor or a poorly positioned carpet). It is known that falls (and the injuries resulting from this fact) have considerable importance in the life of the elderly, which may include significant morbidity, mortality, functional impairment, hospitalization, institutionalization and high economic and social costs, placing a further burden on the health services. Studies in Brazil have shown that people younger than 75 years are more likely to fall outdoors and over 75 years fall more within their own homes (FABRÍCIO *et al.*, 2004; CRUZ *et al.*, 2012.).

Besides constant supervision in order to prevent falls and environmental monitoring, one can not disregard other advantages strongly associated with increasing life quality of small residential seniors care centers, such as social interaction, involvement in everyday activities, independence, security, protection and psychological well-being (HWANG *et al.*, 2003). Whereas diet, physical activity, stress management, relationships and preventive behavior are essential to the maintenance of health in all stages of human development, authors highlight the importance of socialization in old age (KUCHEMANN, 2012).

In addition, correctly points Karsch (2003), "caring for the elderly at home is surely a situation that should be preserved and encouraged; however, care for an elderly and disabled for 24 hours without a break is not a job for a woman to do alone, because usually she has more than 50 years old and without adequate support or services that may meet her needs.

Consistent with this proposal, Ordinance No 73 of the Ministry Social Security (Ministério Previdência e Assistência Social - BRAZIL, 2001) recommends that priority should be given for the elderly staying in the family, in republics for seniors and other community centers. Regarding the legal aspects of these spaces, the Elderly Statute provides that the governmental and non-governmental organizations responsible for the care of the senior
should submit their programs to the competent organ of the Health Surveillance and the Municipal Council of the Elderly for approval.

Resolution of the National Health Surveillance Agency (ANVISA, 2005) in Brazil, defines the minimum criteria for the operation and evaluation, as well as the mechanisms for looking after seniors. The small residential care centers could receive individuals with Dependency Grade I (independent elderly, even requiring use of self-help equipment). For the care of these it is recommended a proportion of "one caregiver for every 20 seniors, or fraction thereof, with a working schedule of 8 hours / day"; which is perfectly feasible in the model proposed in this study.

Entrepreneurship, Social Inclusion and Sustainable Development

The creation of small residential care centers contribute to the formalization of caregiving activities. The entrepreneurship of small business is almost unanimously seen as beneficial to the economic and social life of countries and regions. According to IBQP (Brazilian Institute of Quality and Competitiveness), "the inclusion of this type of project, which represents around eight million people in Brazil, is seen as a possibility of change in the current economic and social framework of the country" (LIMA, 2010). In Brazil there are 40 million entrepreneurs, according to research conducted in 2013 by SEBRAE. It is remarkable that, 71 of every 100 Brazilians who opens a business are motivated by a business opportunity (or bizopp) and not by the need (GEM, 2013: 19).

Recent studies in Brazil showed a strong association between entrepreneurship and unemployment: the higher the entrepreneurial activity of the municipality, the lower the unemployment rate, being the small business one of the main vehicles of entrepreneurial activity (BARROS & PEREIRA, 2008). As described in the Civil Code (BRAZIL, 2002), to be considered a businessman/ Entrepreneur, an individual must exercise economic activities through production or circulation of goods or services.

The newly created figure of Individual Micro Entrepreneur (IME) in Brazil, has been benefiting thousands of informal workers by increasing flexibility and simplicity in the process of formalization and legalization for informal workers. Given the clear importance of entrepreneurs in the economy, let them use their own residence as care structure, shall facilitate and accelerate the implementation of this kind of social support without leveraging major investments, that, in general, small entrepreneurs do not have.

3. CONCLUSION

The advantages of stimulating legal and operational feasibility of residential entrepreneur for the care of children and seniors are fully in line with Agenda 21, the NUMP, the Brazilian Federal Constitution, the suggestions of multilateral agencies and numerous national and international studies. Thus, it is urgent that this issue could be seeded in different forums and spaces for discussion and, above all, municipal and federal regulators. Municipalities have the need to regulate and discipline the activity, and the federal authorities should create legal and fiscal mechanisms to rule them.

The residential entrepreneur is a key part of the configuration of sustainable cities. It generates a positive externality in large urban centers: reducing energy consumption in the transport sector, meeting the targets for reducing greenhouse gas emissions, reducing the problems and health hazards related to pollution and traffic jams, strengthening of social
relations in the community and quality of life for those involved. Further research is needed to establish the estimated investments needed and funding for Entrepreneurship in vulnerable areas, considering a daycare center structure for seniors and children.

**LITERATURE**


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DETERMINANTS OF WORKING CAPITAL AND INVESTMENT FINANCING PATTERNS OF SMES: EVIDENCE FROM TURKEY

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ABSTRACT
This paper analyzes the firm level determinants of the financing sources composition of working capital and fixed asset investments of Turkish SMEs with a system of equations approach. Using the cross-sectional data set of 1,278 SMEs for year 2013, we find that larger firms and firms that have an internationally recognized quality certification finance a lower proportion of their working capital with internal funds. The proportion of working capital that is financed with bank loans is higher for these firms. A higher portion of working capital is financed with purchases on credit from suppliers and advances from customers by firms that are larger and firms that are younger. Firms with lower export intensity finance a higher portion of fixed asset investments with internal funds. The proportion of fixed asset investments that is financed with bank loans is lower for older firms. Older firms and firms with a lower percentage of sales made on credit use internal financing more intensively to finance both working capital and fixed asset investments. Firms with a higher percentage of sales made on credit finance a higher portion of their working capital and fixed asset investments with bank loans.

Keywords: Financing Patterns, Investments, SME, Turkey, Working Capital

1. INTRODUCTION
SMEs are important for all economies in the world because of their contribution to GDP growth, job creation and government revenues from taxation. They are central to private sector development and they serve as engines of innovation. Having access to external financing is critical for the survival and growth of SMEs which are dependent on bank lending. However, SMEs face financing obstacles that hinder their potential to grow and create jobs (Hughes, 2009; Mason and Kwok, 2010; Shen, Shen, Xu and Bai, 2009). Difficulties encountered in accessing bank financing adversely affect the day-to-day functioning and growth of SMEs.

SME literature suggests that these firms face higher barriers to bank financing than large firms (Beck, Demirguc-Kunt, Laeven and Maksimovic, 2006; Beck, Demirguc-Kunt and Maksimovic, 2008; Pissarides, 1999). SMEs encounter greater difficulties in accessing bank financing because they are informationally opaque and it is difficult for banks to evaluate their corporate capabilities (Ang 1992; Berger and Udell, 1998; Gregory, Rutherford, Oswald and Gardiner, 2005). Moreover, their financial statements are not as informative as those of large firms and they have shorter credit histories. Information asymmetry and monitoring costs that banks should incur also increases the transactions costs of SME lending for banks.

Accessing bank financing is more challenging for emerging market SMEs (Hanedar, Broccardo and Bazzana, 2014; Menkhoff, Neuberger and Rungruxsirivorn, 2012; Menkhoff, Neuberger and Suwanaporn, 2006; Zhou, 2007). Inability to access bank financing is exacerbated with “informality” in emerging economies where many SMEs operate outside the formal sector (OECD, 2006).
When SMEs do not have access to bank financing, they count on internal cash flows or informal sources of credit. Especially emerging market SMEs frequently fall into this situation (OECD, 2006). Cosh and Hughes (1994) suggest that because access of SMEs to external funds is more difficult than that of large firms, the pecking order theory (Myers, 1984; Myers and Majluf, 1984) which suggests that firms primarily rely on internal funds rather than external funds can be easily applied to SMEs.

Petersen and Rajan (1997) and Nilsen (2002) argue that firms that are financially constrained are more likely to use trade credit and informal lending as alternative sources of finance. Nilsen (2002) find that bank lending constrained firms use trade credit to finance their working capital. On the contrary, Beck et al. (2008) show that although small firms have lower access to bank loans than large firms, they do not try to compensate for this problem with higher use of trade finance.

Beck (2007) shows that small SMEs finance a larger share of their fixed asset investments with internal funds, equity and informal finance than large SMEs. The author also provides evidence that larger SMEs are more likely to use bank loans to finance investments.

Because access to finance is of critical importance for the development of the SME sector, analyzing how firm level factors affect the composition of funding sources of SMEs would be a useful contribution to the literature. This study examines the determinants of the share of different financing sources in the financing of working capital and fixed asset investments by SMEs in an emerging market context, namely Turkey. The cross-sectional data set of 1,278 SMEs for the year 2013 is used for the analysis. We estimate two system of equations models where the share of different financing sources that are used to finance working capital and investments are taken as the dependent variables and the factors that are expected to affect the choice of financing sources are taken as the independent variables. We find that the proportion of internal funds used for working capital financing is lower for larger firms, younger firms, firms with a higher percentage of sales made on credit and firms that have an internationally recognized quality certification. Larger firms, firms with a higher percentage of sales made on credit and firms that have an internationally recognized quality certification finance a higher portion of their working capital with bank loans. A higher proportion of the working capital is financed with purchases on credit from suppliers and advances form customers by larger firms and younger firms.

The proportion of fixed asset investments financed with internal funds is higher for older firms, firms with a lower percentage of sales made on credit and firms with a lower export intensity. Younger firms and firms with a higher percentage of sales made on credit use bank loans more intensively to finance fixed asset investments. Firms with a higher export intensity finance a higher proportion of investments with purchases on credit from suppliers and advances from customers.

This paper is structured as follows: Section 2 describes the methodology and section 3 depicts the sample. Section 4 presents the empirical results and section 5 concludes.

2. METHODOLOGY
The composition of the funding sources for working capital can be described with the following system of seemingly unrelated regressions model:
where the dependent variables show the proportion of each funding source used in the financing of working capital.

The composition of the funding sources for fixed asset investments can be described with the following system of seemingly unrelated regressions model:

\( \text{Internal Funds}_{\text{INV},i} = \alpha_5 + \beta_5 \text{Size}_i + \delta_5 \text{Age}_i + \chi_5 \text{Group}_i + \phi_5 \text{Sales on Credit}_i + \lambda_5 \text{Export}_i + \eta_5 \text{Quality}_i + e_{5,i} \), \hspace{1cm} (5)

\( \text{Owner and Equity}_{\text{INV},i} = \alpha_6 + \beta_6 \text{Size}_i + \delta_6 \text{Age}_i + \chi_6 \text{Group}_i + \phi_6 \text{Sales on Credit}_i + \lambda_6 \text{Export}_i + \eta_6 \text{Quality}_i + e_{6,i} \), \hspace{1cm} (6)

\( \text{Bank Loans}_{\text{INV},i} = \alpha_7 + \beta_7 \text{Size}_i + \delta_7 \text{Age}_i + \chi_7 \text{Group}_i + \phi_7 \text{Sales on Credit}_i + \lambda_7 \text{Export}_i + \eta_7 \text{Quality}_i + e_{7,i} \), \hspace{1cm} (7)

\( \text{Suppliers and Customers}_{\text{INV},i} = \alpha_8 + \beta_8 \text{Size}_i + \delta_8 \text{Age}_i + \chi_8 \text{Group}_i + \phi_8 \text{Sales on Credit}_i + \lambda_8 \text{Export}_i + \eta_8 \text{Quality}_i + e_{8,i} \), \hspace{1cm} (8)

\( \text{Other}_{\text{INV},i} = \alpha_9 + \beta_9 \text{Size}_i + \delta_9 \text{Age}_i + \chi_9 \text{Group}_i + \phi_9 \text{Sales on Credit}_i + \lambda_9 \text{Export}_i + \eta_9 \text{Quality}_i + e_{9,i} \), \hspace{1cm} (9)

The sum of the funding sources adds up to 100%. Internal Funds represents the proportion financed with internal funds and retained earnings by firm i. Owner and Equity represents the proportion financed with the contribution of the owner and issuance of new equity shares. Bank Loans represents the share of bank loans in total funds. Suppliers and Customers represents the share of purchase on credit from suppliers and advances from customers in the total funds used. Other represents the share of debt received from nonbank financial institutions and funds provided by microfinance institutions, credit cooperatives, money lenders, friends, relatives, etc. in total funding.

Among our independent variables, Size represents firm size and it is measured with the number of employees of the firm. Size is included in the model because we expect size to affect the possibility that the firm is facing financing constraints and the way investments are financed (Beck et al., 2006; Beck et al., 2008; Berger and Udell, 1992, 1998).

Age represents firm age. Firm age is also expected to affect the funding patterns of firms. Canton, Grilo, Monteagudo and Van der Zwan (2010) argue that younger firms encounter higher financing constraints because they do not have adequate credit histories that provide the banks with information about whether repayment is risky.
**Group** represents dummy variable for business-group affiliation. Group affiliation may affect the financing patterns of SMEs because existence of an internal capital market within a group that the firm is affiliated to may affect the way necessary funds are provided. **Sales on Credit** represents percentage of sales made on credit. Because the proportion of sales sold on credit can affect cash reserves, it can also have an effect on the financing patterns of firm.

**Export** represents percentage of sales exported by the firm. Exposure to foreign trade is expected to affect access to financing and financing patterns. Exporting may positively affect access to finance by bringing competitiveness and efficiency (Ganesh-Kumar, Sen and Vaidya, 2001). On the other hand, it may make SMEs credit-constrained as a result of exposure to greater uncertainty, failure risk and need of working capital (Amiti and Weinstein, 2011).

**Quality** represents dummy variable for having an internationally recognized quality certification. Having an internationally recognized quality certification is expected to positively affect access to external financing.

Industry dummies are included in the analysis to control for industry specific effects. Because none of the independent variables have a VIF value that is above the cutoff value of 4, there is no problem of multicollinearity in our data. Table 1 presents the description of the variables used in the system of equations models.

### 3. DATA

The cross-sectional data are from World Bank Enterprise Survey conducted in year 2013. The responses given to face-to-face interviews allow us to construct our variables. 1,278 firms whose number of employees is less than or equal to 250 are included in the analysis. The SMEs that are included in the analysis operate in nine industry categories (food, textiles, garments, non-metallic mineral products, fabricated metal products, other manufacturing, retail, other services). The data are accessible from www.enterprisesurveys.org. The web site also includes information on the sampling method.

Summary statistics of the dependent variables for the two models (model 1 for working capital and model 2 for fixed asset investments) and the independent variables are given in Table 2. We see that internal financing is the predominant source of finance that is used for financing working capital. On average, firms finance 71.2% of their working capital investments with internal funds. SMEs rely on bank financing as the second source for working capital financing. The proportion of working capital that is financed with bank loans is 16.9% on average. The mean of the proportion of working capital that is financed with trade credits from suppliers and advances from customers is 7.3%. Other sources make up 3.2% of working capital financing.

Firms mainly rely on internal financing also for fixed asset investments. On average, firms finance 59.8% of their fixed asset investments with internal funds and retained earnings. The proportion of fixed asset investments financed with bank borrowing is 26.7% on average.
### Table 1: Description of the variables used in the system of equations

<table>
<thead>
<tr>
<th>Dependent Variables for Model 1 (Working Capital) and Model 2 (Fixed Asset Investments)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Internal Financing</strong></td>
</tr>
<tr>
<td><strong>Owner and Equity</strong></td>
</tr>
<tr>
<td><strong>Bank Loans</strong></td>
</tr>
<tr>
<td><strong>Suppliers and Customers</strong></td>
</tr>
<tr>
<td><strong>Other</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Independent Variables</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Size</strong></td>
</tr>
<tr>
<td><strong>Age</strong></td>
</tr>
<tr>
<td><strong>Group</strong></td>
</tr>
<tr>
<td><strong>Sales on Credit</strong></td>
</tr>
<tr>
<td><strong>Export</strong></td>
</tr>
<tr>
<td><strong>Quality</strong></td>
</tr>
</tbody>
</table>

### Table 2: Summary statistics

<table>
<thead>
<tr>
<th>Dependent Variables (Model 1: Working Capital Financing)</th>
<th>Mean</th>
<th>Standard Deviation</th>
<th>Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Financing</td>
<td>0.712</td>
<td>0.342</td>
<td>0.800</td>
</tr>
<tr>
<td>Bank Loans</td>
<td>0.169</td>
<td>0.269</td>
<td>0.000</td>
</tr>
<tr>
<td>Suppliers and Customers</td>
<td>0.073</td>
<td>0.171</td>
<td>0.000</td>
</tr>
<tr>
<td>Other</td>
<td>0.032</td>
<td>0.121</td>
<td>0.000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dependent Variables (Model 2: Fixed Asset Investments Financing)</th>
<th>Mean</th>
<th>Standard Deviation</th>
<th>Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Financing</td>
<td>0.598</td>
<td>0.404</td>
<td>0.700</td>
</tr>
<tr>
<td>Owner and Equity</td>
<td>0.061</td>
<td>0.184</td>
<td>0.000</td>
</tr>
<tr>
<td>Bank Loans</td>
<td>0.267</td>
<td>0.370</td>
<td>0.000</td>
</tr>
<tr>
<td>Suppliers and Customers</td>
<td>0.025</td>
<td>0.096</td>
<td>0.000</td>
</tr>
<tr>
<td>Other</td>
<td>0.025</td>
<td>0.114</td>
<td>0.000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Size</strong></td>
<td>43.529</td>
<td>51.971</td>
<td>20.000</td>
</tr>
<tr>
<td><strong>Age</strong></td>
<td>18.042</td>
<td>12.678</td>
<td>16.000</td>
</tr>
<tr>
<td><strong>Sales on Credit</strong></td>
<td>0.475</td>
<td>0.323</td>
<td>0.500</td>
</tr>
<tr>
<td><strong>Export</strong></td>
<td>0.293</td>
<td>0.379</td>
<td>0.020</td>
</tr>
<tr>
<td><strong>Group (Dummy)</strong></td>
<td>Percentage Frequency of 1 = 19%</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Quality (Dummy)</strong></td>
<td>Percentage Frequency of 1 = 40%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The mean of the proportion of fixed asset capital expenditures that is financed with owners’ contribution or issued new equity shares is 6.1%. The mean of the proportion of fixed asset investments that is financed with purchases on credit from suppliers and advances from customers is 2.5%. Other sources make up 2.5% of fixed asset investments financing.

4. EMPIRICAL FINDINGS
4.1. Results of the system of equations model for the composition of the funding sources for working capital

We begin our empirical analysis with the estimation of the system of four equations model described by equations (1)-(4) where the dependent variables give the proportion of working capital financed with each source. Seemingly unrelated regressions are used in the estimation. The estimation results of the system of equations are given in Table 3.

<table>
<thead>
<tr>
<th>Dependent Variables</th>
<th>Size</th>
<th>Age</th>
<th>Group</th>
<th>Sales on Credit</th>
<th>Export</th>
<th>Quality</th>
<th>R²</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Financing</td>
<td>-0.001***</td>
<td>0.002**</td>
<td>-0.033</td>
<td>-0.001***</td>
<td>0.000</td>
<td>-0.022**</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td>(0.003)</td>
<td>(0.029)</td>
<td>(0.213)</td>
<td>(0.000)</td>
<td>(0.445)</td>
<td>(0.015)</td>
<td></td>
</tr>
<tr>
<td>Bank Loans</td>
<td>0.001***</td>
<td>-0.001</td>
<td>-0.008</td>
<td>0.001***</td>
<td>0.000</td>
<td>0.016*</td>
<td>0.04</td>
</tr>
<tr>
<td></td>
<td>(0.008)</td>
<td>(0.197)</td>
<td>(0.714)</td>
<td>(0.000)</td>
<td>(0.435)</td>
<td>(0.085)</td>
<td></td>
</tr>
<tr>
<td>Suppliers and</td>
<td>0.0003**</td>
<td>-0.001*</td>
<td>0.009</td>
<td>0.000</td>
<td>0.000</td>
<td>-0.001</td>
<td>0.06</td>
</tr>
<tr>
<td>Customers</td>
<td>(0.014)</td>
<td>(0.059)</td>
<td>(0.529)</td>
<td>(0.161)</td>
<td>(0.857)</td>
<td>(0.912)</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>-0.000</td>
<td>-0.000</td>
<td>0.031***</td>
<td>0.000</td>
<td>0.0003***</td>
<td>0.007</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td>(0.171)</td>
<td>(0.866)</td>
<td>(0.002)</td>
<td>(0.510)</td>
<td>(0.000)</td>
<td>(0.166)</td>
<td></td>
</tr>
</tbody>
</table>

P-values are presented in parentheses. Significance at the 1%, 5% and 10% are denoted by ***,** and * respectively.

We see that size has a statistically significant relationship with the proportion of working capital that is financed with internal funds at the 0.01 level. The negative coefficient indicates that a 10% increase in size produces a 0.01% decrease in the share of internal funds in working capital financing.

The estimated coefficient for size in bank loans regression is statistically significant at the 0.01 level. The positive coefficient indicates that a 10% increase in size brings a 0.01% increase in the proportion of working capital financed with bank loans. The positive statistically significant coefficient of size estimated in suppliers and customers regression shows that a 10% increase in size produces a 0.003% increase in the share of purchases on credit from suppliers and advances from customers in the financing of working capital. We see that size does not have a statistically significant relationship with the share of other sources in working capital financing.

The positive statistically significant coefficient of age estimated in internal financing regression shows that a 10% increase in age produces a 0.02% increase in the share of internal funds used for working capital financing. Age has a statistically significant negative impact on the share of purchases on credit from suppliers and advances from customers in working capital financing. The coefficient shows that a 10% increase in age brings a 0.01% decrease in the proportion of working capital financed with this source. Age does not affect the share of bank loans and other sources in working capital financing.
Group dummy variable has a statistically significant relationship with the share of other sources used for working capital financing. The positive coefficient indicates that firms that are part of a larger firm finance a larger portion of their working capital with sources other than internal financing, bank loans and purchases on credit from suppliers and advances from customers. This finding may signal the use of internal capital markets within the groups that the firms are operating in for working capital financing.

The negative statistically significant coefficient of sales on credit variable estimated in internal financing regression shows that a 10% increase in the percentage of sales sold on credit brings a 0.01% reduction in the proportion of working capital financed with internal funds. The statistically significant coefficient of sales on credit estimated in bank loans regression shows that the percentage of sales made on credit has a positive relationship with the share of bank loans in working capital financing. The coefficient indicates that a 10% increase in the percentage of sales made on credit produces a 0.01% increase in the share of bank loans. Sales on credit variable does not have a statistically significant effect on the share of the other sources of funds in working capital financing.

The estimated coefficient of export variable in other regression is statistically significant at the 0.01 level. However, the coefficient that is approximately zero shows that the percentage of sales exported has a minuscule effect on the proportion of working capital that is financed with other sources such as debt received from nonbank financial institutions and funds provided by microfinance institutions, credit cooperatives, money lenders, friends, relatives, etc.

Quality dummy variable has a statistically significant negative relationship with the share of internal funds used in working capital financing. The negative relationship shows that SMEs that has an internationally recognized quality certification finance a lower proportion of their working capital with internal funds. The estimated positive coefficient for quality dummy variable in bank loans regression is statistically significant at the 0.05 level. The positive coefficient shows that SMEs that have an internationally recognized quality certification finance a higher proportion of their fixed asset investments with bank loans. This finding may signal that the existence of such a certification may make it easier for firms to have access to bank financing.

**4.2. Results of the system of equations model for the composition of the funding sources for fixed asset investments**

The estimation results of the system of equations described by equations (5)-(9) where the dependent variables give the proportion of fixed asset investments financed with each source are given in Table 4. We see that size has a negative relationship with the proportion of fixed asset investments that is financed with other sources such as debt received from nonbank financial institutions and funds provided by microfinance institutions, money lenders, friends,
Table 4: Estimation results for the composition of the funding sources for fixed asset investments

<table>
<thead>
<tr>
<th>Dependent Variables</th>
<th>Independent Variables</th>
<th>Size</th>
<th>Age</th>
<th>Group</th>
<th>Sales on Credit</th>
<th>Export</th>
<th>Quality</th>
<th>R²</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Financing</td>
<td>-0.001</td>
<td>0.005***</td>
<td>-0.065</td>
<td>-0.002***</td>
<td>-0.001**</td>
<td>-0.037</td>
<td>0.02</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.218)</td>
<td>(0.003)</td>
<td>(0.165)</td>
<td>(0.001)</td>
<td>(0.034)</td>
<td>(0.214)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Owner and Equity</td>
<td>0.000</td>
<td>-0.001</td>
<td>-0.022</td>
<td>-0.000</td>
<td>0.000</td>
<td>0.017</td>
<td>0.03</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.315)</td>
<td>(0.439)</td>
<td>(0.402)</td>
<td>(0.793)</td>
<td>(0.668)</td>
<td>(0.299)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank Loans</td>
<td>0.001</td>
<td>-0.004***</td>
<td>0.052</td>
<td>0.002***</td>
<td>0.000</td>
<td>0.011</td>
<td>0.09</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.156)</td>
<td>(0.006)</td>
<td>(0.258)</td>
<td>(0.001)</td>
<td>(0.960)</td>
<td>(0.697)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suppliers and</td>
<td>-0.000</td>
<td>-0.000</td>
<td>0.017**</td>
<td>-0.000</td>
<td>0.0002**</td>
<td>0.004</td>
<td>0.03</td>
<td></td>
</tr>
<tr>
<td>Customers</td>
<td>(0.744)</td>
<td>(0.697)</td>
<td>(0.065)</td>
<td>(0.997)</td>
<td>(0.023)</td>
<td>(0.405)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>-0.0002*</td>
<td>0.0002</td>
<td>0.018</td>
<td>0.000</td>
<td>0.001***</td>
<td>0.004</td>
<td>0.07</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.065)</td>
<td>(0.731)</td>
<td>(0.220)</td>
<td>(0.645)</td>
<td>(0.000)</td>
<td>(0.674)</td>
<td></td>
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</tr>
</tbody>
</table>

P-values are presented in parentheses. Significance at the 1%, 5% and 10% are denoted by ***,** and * respectively.

etc. The coefficient shows that a 10% increase in size brings a 0.002% reduction in the share of these reduction in the share of these sources.

Age has a positive effect on the share of internal funds in fixed asset investments financing. The coefficient indicates that a 10% increase in age brings a 0.05% increase in the share of internal funds used in the financing of fixed asset investments. Moreover, age has a negative effect on the proportion of investments financed with bank loans. A 10% increase in age brings a 0.04% reduction in the share of bank loans used in investments financing.

Group dummy variable has a statistically significant positive relationship with the share of purchases on credit from suppliers and advances from customers in fixed asset investments financing. The positive relationship shows that SMEs that are part of a larger firm finance a higher proportion of their fixed asset investments with these sources.

The negative statistically significant coefficient of sales on credit variable in internal financing regression shows that a 10% increase in percentage of sales made on credit is associated with a 0.02% decrease in the proportion of fixed asset investments financed with internal funds. Sales on credit has a statistically significant positive relationship with the share of bank loans in investments financing at the 0.05 level. A 10% increase in the percentage of sales made on credit brings a 0.02% increase in the share of bank loans in the financing of fixed asset investments. These findings may signal that an increase in the proportion of sales sold on credit causes a deficiency in the availability of cash reserves and internal funds for investments of fixed assets. Eventually, firms may be obliged to finance investments with bank loans.

Export variable has a statistically significant negative relationship with the proportion of internal funds used for fixed asset investments financing. A 10% increase in the percentage of sales exported brings a 0.01% reduction in the share of internal funds used. The estimated
positive coefficients for export variable in suppliers and customers and other regressions are statistically significant at the 0.05 and 0.01 level respectively. The positive coefficients indicate that a 10% increase in percentage of sales exported brings a 0.002% increase in the proportion of purchases on credit from suppliers and advances from customers and a 0.01% increase in the share of debt received from nonbank financial institutions and funds provided by microfinance institutions, money lenders, etc.

The insignificant coefficient of quality variable estimated in all of our regressions show that having an internationally recognized quality certification does not have a statistically significant effect on the share of each source in fixed asset investments financing.

5. CONCLUSION
This paper analyzes the firm level determinants of the proportion of different financing sources used by SMEs in the financing of working capital and fixed asset investments with a system of equations approach. We use data from the World Bank Enterprise Survey conducted in Turkey in 2013 and our sample includes 1,278 SMEs.

We find that larger firms use less internal financing and more bank loans and purchases on credit from suppliers and advances from customers as sources to finance their working capital. Older firms use purchases on credit from suppliers and advances from customers less than younger firms to finance their working capital. Firms that have a group affiliation finance a higher portion of their working capital with sources such as debt received from nonbank financial institutions and funds provided by microfinance institutions, credit cooperatives, money lenders, friends and relatives. The reason behind this finding is probably the use of internal capital markets within groups. The share of these other sources of funds is also higher for firms with higher export intensity. Firms that have an internationally recognized quality certification finance a lower portion of their working capital with internal funds and a higher portion of it with bank loans.

In our analysis of the determinants of the share of five types of sources in fixed asset investments financing, we find that larger firms finance a lower portion of their investments with debt received from nonbank financial institutions and funds provided by microfinance institutions, credit cooperatives, money lenders, friends, relatives, etc. A higher portion of investments is financed with purchases on credit from suppliers and advances from customers by group affiliated firms. Export intensive firms finance a lower proportion of their investments with internal funds and a higher proportion of them with purchases on credit from suppliers and advances from customers and other sources such as debt received from nonbank financial institutions and funds provided by money lenders and friends.

The proportion of working capital and fixed asset investments that is financed with internal funds is higher for firms that are older. Firms with a higher percentage of sales made on credit finance a lower proportion of their working capital and investments with internal funds. These firms finance a higher portion of their working capital and investments with bank loans.

The level of financing constraints encountered by the firms may affect the proportion of investments that is financed with each source. Moreover, it may have an indirect impact on the share of each source by its influence on the factors that can affect how investments are financed. Analyzing whether the level of financing constraints the firms face affects the firm level determinants of the composition of financing sources is a suggestion for future research.
Finding out the effect of the level of financing constraints on the factors that are expected to affect how investments are financed would also be a valuable contribution to the literature.

**LITERATURE**

THE ROLE OF HIGHER EDUCATION INSTITUTIONS IN THE DEVELOPMENT OF ENTREPRENEURSHIP COMPETENCES ON THE STUDY PROGRAMS OTHER THAN ECONOMICS

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ABSTRACT
“Entrepreneurial Croatia” – that is the name for a strategy of education for entrepreneurship, which gives us a framework for a systematic development of educational entrepreneurship. It also supports a more market-oriented way of thinking, and serves as a preparation for the new economic trends in the development of human resources. Through the initiation and development of entrepreneurial way of thinking and the development of entrepreneurial competences, production and exports are increased as well as the overall employment rate in a particular country. Besides its positive effects on the growth of newly founded firms, entrepreneurial competence also acts positively on the more efficient ways of using the existing creative potentials of knowledge and skills in the society. The interest for educational programs that support and develop entrepreneurial competence is on the rise. The research whose results we are presenting was aimed at determining entrepreneurial competence. The research was done using the structured questionnaire and it included 321 students of The University North, enrolled in study programs that do not belong to the economic study programs nor are connected with them. Descriptive statistical method was used to analyze the data. The results of the research have shown that a higher level of entrepreneurial competence increases the affinity towards entrepreneurial behavior. The results of the research have also shown that teaching in higher education institutions does not significantly develop entrepreneurial competences. Entrepreneurial competence is a key for a higher competitiveness, personal development and sustainable employability of an individual i.e. student. It helps in the creation, recognition and use of opportunities and introducing changes. Entrepreneurial competence makes innovation, survival and growth in a dynamic and competitive environment easier.

Keywords: higher education institutions, entrepreneurial competences, study programs other than economics, competitiveness.
1. INTRODUCTION

Globalization is characterized by increasingly strict demands of business practice towards employee efficiency and effectiveness, and experience in human resource management has shifted the focus on complete capability of an individual to perform a competitive job. Constant change in the labor market is an imperative of all organizations. Organizational, technological and process changes require and drive the development of new competences, therefore organizations have the task to enable and empower their employees to continuously develop. Higher education institutions play an important role in all this, by implementing new study programs that will provide their graduates with certain knowledge and skills, based on which they can develop competences in a particular area and thus competitive in the labor market. Competitive advantage of an economy is founded on the development of entrepreneurship. Consequently, education for entrepreneurship is based on the required entrepreneurial competences on all levels of education. The development and success of any organization begins with understanding what kind of employees the organization seeks and wishes to develop. By developing a system of competences, an organization acquires a clear structure and forms of behavior that are desirable in its operations. The difference between a good and an outstanding employee lies in competences that particular employees have developed and are using in their daily work. Whether company performance is average or highly successful will mostly depend on the competence level of their employees.

2. HIGHER EDUCATION INSTITUTIONS IN THE REPUBLIC OF CROATIA

One of the outcomes of the reform about a decade ago was the reorganization of higher education system. According to the Act on Scientific Activity and Higher Education that came into force in 2003, higher education institutions in the Republic of Croatia are universities, polytechnics, and schools of professional higher education. In this Act it is stipulated that higher education is provided through professional and university studies. The mission of university studies is to train students for work in science and higher education, in business, public sector and other fields, and for implementing scientific and developmental research. The mission of professional higher education is to provide students with an adequate level of knowledge and skills that will enable them to undertake professional activities, thus allowing them to start working immediately upon graduation (ZZDVO, 2003, p. 182). Consequently, the basic task of polytechnics is to provide practice-oriented education, and for this reason students are trained for particular professions from the very beginning, through application of the acquired competences (Hunjet, Kozina, 2014, Kozina, 2011). Entrepreneurial knowledge acquired by students at higher education institutions should not be limited to theory; rather, it should be practice-oriented and applicable for innovation and devising new business processes. The basic goals of entrepreneurial education include acquiring knowledge on entrepreneurship, developing competences for creation of opportunities, introducing change in complex circumstances, and encouraging entrepreneurial behavior. The expected outcome of an entrepreneurial program is an increased level of entrepreneurial competences, which in turn ought to increase the employment prospects for young people (Kolakovic, 2006, 170). The Croatian Qualifications Framework has set up clear criteria for acquiring a set of competences that individuals can expect to have on completing their education, which are required for a qualification, i.e. the level and volume of required knowledge. The Croatian Qualifications Framework is based on our tradition in formal education, taking into account the present state of the Croatian education system, the development needs of the economy,
individuals and society as a whole, and following the European Qualifications Framework, EU guidelines and international standards. It is important for individuals to recognize how important it is to invest in their education, to understand the advantages provided by higher education, starting from competitiveness in the labor market to improved employability. It can equip them with up-to-date knowledge and skills that can make them competitive internationally. (HKO, 2013)

3. STRATEGIJA RAZVOJA OF ENTREPRENEURSHIP IN THE REPUBLIC OF CROATIA 2013-2020
In October 2013, the Croatian Parliament approved the Entrepreneurship Development Strategy in the Period 2013-2020, which is to replace all other programs and projects by providing support to SMEs (small and medium enterprises) and crafts. This Strategy is aligned with the Europe’s growth strategy Europe 2020, which has prioritized the following economic areas: energy savings and promotion of new environmentally friendly technologies, investments in people and life-long learning projects, investments in research, development and implementation of innovations, and finally, providing easier access to small business funding. Europe 2020 offers a vision of the social market economy of Europe for the 21st century. It addresses three mutually reinforcing priorities: smart growth – building an economy based on knowledge and innovation; sustainable growth – promoting greener and more competitive economy with more efficient use of resources; inclusive growth – promoting economy with high employment rates, leading to social and territorial cohesion. Smart growth will strengthen knowledge and innovations, which requires improved quality of education, better innovation and knowledge transfer in the EU, more efficient ICT usage, and turning innovative ideas into new products and services. All this will result in economic growth and high quality jobs.
Sustainable growth means creating a competitive economy with more efficient use of resources; using European leadership to develop new processes and technologies, including green technology; speeding up the development of smart networks through ICT; strengthening competitive advantages by relying on SMEs; preventing further damage to the environment, biodiversity loss and unsustainable resource exploitation.
Inclusive growth means raising employment rates, especially for vulnerable groups, combating poverty, modernizing labor markets, helping people of all ages anticipate and manage change through investment in skills & training, and ensuring social cohesion (Hunjet, Kozina, 2014, p. 27).
The Entrepreneurship Development Strategy in the Period 2013-2020 was formulated in accordance with the 2013 Economic Program of Croatia, to strengthen entrepreneurial potential and improve the entrepreneurial culture. The Croatian economy can be successful in the long term only if most citizens recognize and adopt entrepreneurship as an attractive option for their professional future (SRPRH 2013-2020, p. 2).

3.1. “Entrepreneurial impulse” 2014
“Entrepreneurial impulse” in 2014 was aimed at creating a more favorable entrepreneurial environment and fostering innovation and internationalization in order to increase added value in the small business sector. A prerequisite for competitiveness and growth in this sector is devising new or significantly improving the existing products and services, and finding new markets. It is only by raising the level of entrepreneurial competences and acquiring specific knowledge and skills that economic growth can be achieved, as these can be the crucial factor in creating jobs and realizing sustainable economic development. New competences of entrepreneurs gained through formal and informal education can lead to the emergence of new
entrepreneurs, who will set up and run their own businesses. Through promotion of entrepreneurship people can be encouraged to start their own business, especially young people and students. Life-long learning within SME sector is particularly important in order to improve the management of business processes, leading to increased efficiency. Furthermore, there should be incentives for employing more higher education graduates, who are expected to boost the development of new products and services, increase competitiveness, and introduce innovations in marketing and business operations (PI, 2014).

4. ENTREPRENEURIAL COMPETENCES
4.1. Importance of entrepreneurial competences in business operations
In addition to being a catalyst in creating new businesses, entrepreneurial competence fosters the entrepreneurial way of thinking, as well as more efficient use of creative potential and existing knowledge and skills. Both current and prospective EU members have defined the development entrepreneurial competences of their citizens as a priority. In its document European Key Competence Framework, the European Commission has included innovativeness and entrepreneurship among key life competences that need to be developed at all levels of education (König Sedlan, 2011, p. 2).
There is growing concern in Croatia that the education system is not adequately preparing its citizens for the challenges of the knowledge-based society. At the same time, employers in the Republic of Croatia often see the shortage of employees with adequate professional and entrepreneurial knowledge, skills and attitudes as the main problem of the Croatian education policy. They have also pointed out that recent graduates are frequently not prepared for teamwork, project approach, risk assessment and continuous learning. It has come to the forefront that the main reason for low competitiveness of labor force in Croatia is lack of entrepreneurial competences in an environment that does not foster entrepreneurship. (Bejakovic, CCHR, 2004, p. 13)

4.2. Types of entrepreneurial competences
Taking into account key entrepreneurial attributes and skills, entrepreneurial competence can be defined as a combination of knowledge, skills, attitudes and capabilities to create and discover opportunities in the environment, to introduce changes, and to direct one’s behavior towards successful creation and management of an organization, whose purpose it is to take advantage of these opportunities and to deal with a high level of uncertainty and complexity in a challenging environment. One of the ways to classify the elements of entrepreneurial competences is to put them in three categories: cognitive, affective and behavioral. The cognitive category of entrepreneurial competences refers to efficient management of reasoning, convictions and expectations. The affective category of entrepreneurial competences refers to the management of emotions and attitudes, while behavioral category includes management of intentions and action orientation (König Sedlan, 2011, p. 4).

4.3. Development of entrepreneurial competences
Competence development should be coupled with the development of a value system and action directions through which competence usage can be orientated towards generally accepted norms and principles in a particular social and cultural context. This is called reflexive learning since there is feedback and intertwining of acquired competences with subjective motives of action leading to responsible usage of competences. Responsible usage of competences should be encouraged, not so much through instruction or moral lectures, but rather by persuasion based on experience regarding the value of certain habits or behavior patterns (König Sedlan, 2011, p. 6).
Competence of entrepreneurship is the ability to turn ideas into concrete action. The basic components of entrepreneurial competence as it is defined in the European Key Competence Framework are the following: introduce and foster innovation, show initiative and take risks, be accountable for one’s own actions, be proactive and react positively to changes, set goals and achieve them, be a team player and be motivated to succeed (Marusic, 2014, p. 3).

4.3.1. Entrepreneurial competences through life-long learning
Entrepreneurial competence consists of knowledge, skills and attitudes which are appropriate in a particular economic, cultural and social context. Knowledge encompasses insights regarding available possibilities, and ability to recognize those that are adequate for one’s professional or business activities. There is a wide range of skills:
- skills of planning, organizing, analysis, communication, performing, reporting, assessment and recording,
- skills related to project design and implementation,
- capability to cooperate and be flexible within a team,
- recognizing one’s own strengths and weaknesses,
- capability to be proactive and respond to changes in a positive way,
- ability to assess and take risks when this is appropriate.

There are several facets of attitudes: initiative-prone, having a positive attitude to change and innovations, ready to recognize areas in which one can show a whole range of entrepreneurial skills, e.g. at home, at work or in the community.

An important entrepreneurial competence which should be constantly developed through life-long learning is the digital competence. Technology allows people to become competent information-seeking users, communicators, problem solvers and decision makers; in a word, well-informed and responsible citizens who contribute to their communities and society as a whole. (Ferk Novakovic, Bogdanovic, 2011, p. 145)

4.4. Managing employee competences

![Figure 1. Managing employee competences](http://jelenahr.com/wp/wp-content/uploads/2013/07/Kramer-Wheel-colors.jpg)

Figure 1 shows different aspects of employee competence management. Each person has a set of competences which are more or less pronounced. When employee competences are managed, this allows organizations to recognize the skills of their employees, and to use them systematically. Being aware of the skills of certain employees can be helpful in designing seminars and training sessions, in presenting or at interviewing potential recruits. Key competences can be unveiled on the basis of a survey which should be conducted within the organization. Information can be gathered by means of a questionnaire distributed to as many employees as possible, or through interviews with different employee groups. A critical event interview is the easiest way to identify the key behavior that was decisive in a critical situation, and it is this behavior that represents the desired competence. Interviews with most successful employees help to identify the behavior that sets those employees apart from the average ones, making them exceptional and successful. Again, this behavior represents the sought-after competences. An interview with executives should clarify the vision and future development of the organization, which is then the basis for determining which competences the organization will need in the future.

5. RESEARCH
In the empirical part of the research there was a survey of first-year (20%), second-year (49%) and third-year students (31%) of the following professional study programs: Multimedia – design and application, Mechanical engineering for industry, Technical and business logistics, and Nursing at University North. The survey was conducted in May 2014. The questionnaire was filled by 321 respondents, out of which 70.41% were women (226 female students) and 29.59% were men (95 male students). It consisted of 25 items, with the first 15 being statements, whereas in the second part of the questionnaire there were 10 questions with proposed answers, which the respondents assessed on a Likert scale. The aim of the research was to establish the role of higher education institutions in developing entrepreneurial competences in study programs unrelated to economics. The intensity of attitudes was measured on a five-point Likert scale (1 being the lowest and 5 the highest rating). The Likert scale is an ordered, one-dimensional scale on which the respondent chooses the option closest to his/her view. In this paper, students’ attitudes were examined by analyzing their responses to questionnaire items. Finally, there is a descriptive analysis of the obtained statistical results.

6. RESULTS
The data were processed statistically by means of the software package Statistica (StatSoft), and shown in graphs below. In Graph 1 there is a pronounced grouping of responses; namely, about 70.00% of respondents believe that the competitive advantage of economy is based on the development of entrepreneurship. Still, 35.00% of respondents is completely certain of this, rating this item with the highest grade of 5, the rating of 4 was given by 34.06% of respondents, 25.63% of them opted for the rating 3, whereas 1.56% of respondents gave no answer.
Graph 1. Competitive advantage of economy is based on the development of entrepreneurship

Graph 2. The development of entrepreneurial competences improves employment prospects for young people

Graph 2 shows that students’ expectations were met. The responses to the item ‘the development of entrepreneurial competences improves employment prospects for young people’ indicate that our students feel that people with acquired entrepreneurial competences have better chances of getting a job. The largest percentage of respondents, i.e. 40.00% believes that employment prospects for young people increase with the development of entrepreneurial competences, giving the highest rating of 5. The rating of 4 was given by 35.94% respondents, 17.81% of them opted for the rating 3, whereas 1.25% of respondents were uncertain, giving no answer.

Graph 3. Assessment of entrepreneurial knowledge acquired during studies

The item ‘Assessment of entrepreneurial knowledge acquired during studies’ received the average rating of 4.00. The largest number of respondents (101 i.e. 31.56%) chose the highest rating of 5, the rating 4 was given by 99 respondents or 30.94%, 23.75% of them (76
respondents) decided on the rating 3, the lowest rating 1 was given by 3.13% of respondents, whereas 2.81% gave no answer.

**Graph 4.** How much emphasis is put on gaining theoretical entrepreneurial knowledge at the University

Graph 4 shows that 32.19% of respondents decided on the highest rating of 5, the largest number of respondents (107, i.e. 33.44%) opted for the rating 4, 21.25% of respondents chose the rating 3, the lowest rating of 1 was given by 2.19% of respondents, whereas 4.06% of respondents gave no answer.

**Graph 5.** How much emphasis is put on gaining practical entrepreneurial knowledge at the University

As can be seen in Graph 5, the largest number of respondents (97), or 30.31% of them chose the highest rating 5, the rating 4 was given by 28.13%, the rating 3 was chosen by 24.06% of respondents, the lowest rating 1 was the choice of 4.38% of respondents, whereas 4.06% respondents gave no answer.

7. **CONCLUSION**

The development of entrepreneurial competence is the development of an entrepreneurial individual who has been trained to notice opportunities in which his or her ideas can be turned into an activity or a venture. This can happen in any situation or environment, such as work, education, or life in general. Higher education institutions should strive for a culture that fosters initiative and taking more responsibility for one’s own future. Through interdisciplinary study programs higher education institutions can create new or additional roles for themselves by developing entrepreneurial competences in their students and by assuming more responsibility for the technological, economic and social growth and development. Furthermore, there is a need for projects that would enable people to continue learning and to build upon entrepreneurial skills. Entrepreneurial impulses and the strategy of learning for entrepreneurship can be of great help in achieving the ambition for Croatia to become a truly “entrepreneurial” country.
In addition to helping companies grow, entrepreneurial competence promotes the entrepreneurial way of thinking and efficient use of the creative potential of the existing knowledge and skills. In terms of individuals, entrepreneurial competence is very important, since it is a key to becoming more competitive and to achieve personal growth, and finally, the key to sustainable employability. Entrepreneurial competence helps in recognizing and creating opportunities, introducing changes, and dealing with increasing levels of uncertainty and complexity in the environment. It is to be expected that more complete knowledge and more developed skills will have a positive impact on perceptions of own competence.

The intention of this survey was to provide an insight into the role of entrepreneurial training at higher education institutions. It is hoped that these institutions will help in solving the problems in its environment and ultimately contribute to a knowledge society by producing competent, entrepreneurial professionals, who are employable in the labor market.

Our survey has shown a growing interest for entrepreneurial education and acquisition of entrepreneurial competences among students in study programs unrelated to economics. It is recommended to continue conducting similar surveys in order to raise the awareness and positive attitudes of students towards entrepreneurship, so that expected learning outcomes can make them more competitive in the labor market.

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THE IMPORTANCE OF FAMILY BUSINESSES IN THE ECONOMY

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ABSTRACT
Family businesses belong to a small group, which has a significant share in the domestic business. Among family business there was decidedly smaller number of falls recorded, as well as wrong financial decisions or reduction than for other entities in the same sector. Family businesses contribute to the fact that the Polish economy has one of the better results. The article shows the role and importance of family businesses in the economy based on family companies registered in Ciechanów.

Keywords: family business, specificity of family business, economic impotence of family business.

1. INTRODUCTION
In Poland, there are many family businesses, but in the literature it is difficult to find a clear definition of a family business, due to the fact that to the same economic entity, several terms, apply including family business or family business household. These terms indicate that all of these concepts are characterized by a combination of economic activity with sphere of family. Influence of family is a common point that connects all family businesses which develop and their shape depends on sector in which they operate and size of the entity.

2. THE CONCEPT OF FAMILY BUSINESS
Many publications deemed to family businesses for a specific type of businesses. Specificity results from coupling components: the family and the company (Miączyński, Kostrzewski, online). Family business stands out from other operators as interdependence of businesses and families. Between family and company there is some bilateral interaction. Private life intertwines family members and professional life, company becomes center of family life and shall appoint a career of its members. Business is not only families’ source of income, but also a binder, object of pride, identification, and prestige. The family company is “a company of any size or legal form, whose capital is wholly or decisive part is located in possession of family, at least one member of family has a decisive influence on the leadership or executives functions, he performs with intention of permanent maintenance of project in hands of the family. Thus, it is an enterprise whose property is controlled by one family,” (Jeżak, Popczyk, Winnicka-Popczyk, p.19) and in the functioning of economic entity is involved more than one family member.
Family businesses meet the following conditions (Sułkowski, Marjanski, pp.16, 91-92):

1. the company belongs to family, its members are also - at least in part, its employees,
2. the company is main source of income of family,
3. the company is passed on from generation to generation,
4. family members are strongly committed to work for common good, are jointly responsible for fate of company, support it financially and morally.

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Definition the family company explains its socio-economic characteristics, but among the most defining criteria taken into account, there dominates the criteria of ownership or management.

3. SPECIFICITY OF THE FAMILY BUSINESS

Family businesses are characterized by the fact that family members take the most crucial and strategic decisions concerning company, management positions and maintain control of shares in company. This is connected with desire to control spending and decision-making on investment or payment of dividends. Family businesses are less likely to accept foreign investors due to decision-making, can occur in their reluctance to promote employees to senior management positions of non-family members, etc.

In international family businesses, family members often fulfill role of experts in supervisory board, and from non-family managers are expected to integrate values of family, knowledge, predictability, skills and efficiency. So organized family businesses are responding to survive in long term rather than to maximize financial profit in the short term (Hadryś, 2011, pp.16).

The specificity of the family business also includes its life cycle. The life cycle of family business has an impact on its nature. "Young" family businesses will have both other restrictions, as well as other possibilities than those in second or third generation.

The company which is in phase of the first generation, the owner will most likely be the managing director, issues related to survival and growth will dominate over business decisions, and formal involvement of family will be rather limited.

With attainment of maturity by the company, family can turn its attention to supporting and encouraging family members to formally engage in affairs of family business. At this stage attention of family can focus on creating "entry criterias" for company and planning career paths for younger family members who would like to work in family business.

Assuming that the company is already well placed in market, the family owners may have opportunity to focus on the goals of family, business development, strategic choice of customers to a much greater extent than could be done in earlier phases, for example in process of acquiring market position (Hadryś, 2011, pp. 15-16).

4. FACTORS AFFECTING FORMATION OF FAMILY BUSINESSES

Own business is becoming an increasingly attractive form of pursuing a career and life. In terms of individual autonomy, it gives a chance to make an action and fulfill plans and dreams of the individual. From a social perspective it is a way to introduce new products and services, creating new jobs and improving general welfare.

The development of family entrepreneurship manifested in setting up new companies, as well as developing existing ones, is conditioned by both internal factors - related to entrepreneur and enterprise (the desire for self-reliance in terms of decision-making, need for fair wages, a tendency to take action and personal creativity) - and external, related to legal system, financial, infrastructure, unemployment and cultural (material or immaterial nature) (Glinka, Gudkova, pp. 42-55).

One of the factors that determine functioning of family business is great level of trust that family members involved in work of his own company have. The degree of confidence is different from trust that people have for workers from outside the family.

Education and vocational training of entrepreneurs belongs to a group of factors that have the greatest impact on ability of enterprises to remain on market, but are also important features of psycho-founders and subsequent leaders inherit. They shall be strong, determined, conscious of their own competence, ambitious, low need for social support in event of
difficulty, requiring from each other, but also from others. Thus, people who make a family business should be entrepreneurial (Hadryś, 2011, p. 243).

5. CONSEQUENCES OF FAMILY BUSINESSES

Research shows that in the initial stage of business development, there are positive consequences of family in form of greater confidence to the employees of family, a greater involvement of employees with family in work and the low degree of formalization, which translates into more efficient, effective communication within company, as well as personalization organizational relationships (paternalism, family atmosphere). The family nature of company is also associated with long-term objectives, related to expectation of stable growth of company in long term and greater adaptability of business of ability to adapt to changing environmental conditions (Kowalewska, p. 100).

The consequence of the business domination by family ties is a low degree of formalization and bureaucratization in company, especially in small enterprises. Family businesses are characterized by less extensive management structure, so that the flow of information, decision-making is much faster than non-family firms. Key decisions are taken by family members, which is easier to communicate with each other. Family businesses are characterized by a flexible approach to organization of work and demands raised by customers.

Interaction between family and business can also be the source of many dysfunctions. The presence of families in business can mean in particular:

1. too close integration of family life with life of company and possibility of transfer of any family conflicts in the sphere of business;
2. difficulties in combining work and family roles by employees of the family;
3. unequal treatment of workers in the family and outside the family;
4. resistance to allowing external managers to manage.

Threat to achieving objectives of family is involvement of family members in business are and different treatment of family members in relation to other employees. Subordinate employees of family are harder to point out errors, execute commands, not to mention dismissal (Kowalewska, pp. 109-118).

6. THE ECONOMIC IMPORTANCE OF FAMILY BUSINESSES

Family businesses are a very large group of companies with significant economic potential, that play an important social role. Thanks to these businesses and their owners fundamentally economic situation of the country has changed. Several million Poles have decided to make an effort to establish and maintain businesses, but often don’t have the skills, experience, technology and capital. By creating their company could count only on their own talent and hard work, support and commitment of their loved ones.

The final report on the study of family businesses, shows that over 10% of Polish GDP - more than 121 billion PLN, was produced by family businesses. Micro family businesses produced 7% of GDP, small family businesses - 1.9% of GDP, and the average family businesses - 1.4% of GDP. A total of family businesses in the MSME sector produced 10.4% of GDP (Kowalewska, pp.65-66). Such a significant part in building of GDP due to the fact that family businesses generate their income in long term, in a safer and more stable. Among other things, because it is estimated that family businesses are least affected by international economic crisis (Kurcz, on line).

The importance and role of family businesses during the economic crisis underscores report "Family businesses: “Sustaining performance”, published in September 2012. Credit Suisse presents the results of a survey conducted on 280 family-owned companies from 33 countries that are members of the association of Family Business Network International.
According to the report, family businesses are an important engine of economic recovery and contribute significantly to mitigate effects of the crisis. Specific business model found in family businesses is characterized by long-term prospect of action, well-functioning supervision of ownership and focus on providing products and services of the highest quality (Zaniewska, on line).

Family businesses often operate in market niches. They are able to realize custom orders and more quickly adapt to changing market conditions and new customer expectations. Family businesses much faster than big companies adapt to new conditions in times of turbulence. Flexibility, trust, custom solutions, commitment, responsibility for name and brand result that these companies are competing for big corporations (Lublińska-Kasprzak, on line).

Family businesses achieve also better financial results in the stock market. Credit Suisse a few years ago created the index of family companies listed on the stock exchange. Based on the financial results of these companies in the five years, it was found that they were better on average by 8% from the results of non-family firms. Over 60% of companies surveyed reported a family at the same time min. 5% increase in sales revenue. The reasons for this state of affairs owners of family businesses perceive the long-term operation of enterprises or the willingness of family members to make sacrifices in crisis situations (Zaniewska, on line).

7. THE IMPORTANCE OF FAMILY BUSINESSES IN CIECHANÓW

Family businesses in Ciechanów are mainly local, but their share in the total number of enterprises is very large. This is due to the occurrence of a few larger factories and high unemployment.

Family businesses in Ciechanów, representing one different sections of PKD, make economic activity more diverse and also to some extent conducive to meeting the needs of market, both local and regional (Szymańska K., pp. 307 – 321), or even national. It includes especially road freight transport, activities related to food service type pizza and real estate market (purchase, sale, rental), as well as support services, crop production in the production and market seed.

Family businesses play an important role in local development. The specificity of these companies means that their owners are reluctant to think about migration, searching maximum benefit for company - from an economic point of view - the geographical location. Companies located in Ciechanow are linked to reports of a lesser degree of formalization, the more "visible" and, therefore, more likely to be active in this environment, and above all aimed at, among others, maintain a good reputation.

Family businesses aren’t only an important part of local community due to contribution to the regional economy and job creation. They are involved in the building of local communities - they are willing to allocate funds for supporting local cultural initiatives, activities or educational institutions sponsoring small local clubs. Authorities Ciechanow appreciate the sponsorship was voted "Sponsor of the Year". Title Sponsor of the Year 2008 President Ciechanow admitted the family business Metaltech - Piasecki. Metaltech financially supported, among others, city events: a historic "Back Light Cavalry Guard", New Year's Eve Concert Waldemar Malicki and organized by Ciechanowski People's Sports Club "Mazovia" Polish Championships Weightlifting. This honorable title Metaltech has already been awarded in 2002 (website of the city council).
8. CONCLUSION

Article showed the role and importance of family businesses in the country as well as locally in Ciechanów. Family businesses influence character and development of local economy, both regional and national. They encourage innovation, promote local community. They are also focused on the effects of longevity and stability, they depend on survival and transfer company to younger generation.

LITERATURE

1 Monograph
a) One or two author(s)

b. Three to six authors

2. Monograph chapter, journal article


4 Research reports
Web
7 Online sources

Author of the contribution is known:

Author of text unknown:
9th International Scientific Conference on Economic and Social Development