



Универзитет „Св. Кирил и Методиј“
ЕКОНОМСКИ ИНСТИТУТ

ISSN 1857-7741 (online)
UDC -338

Economic development

ЕКОНОМСКИ РАЗВОЈ

Journal of
The Institute of Economics - Skopje
Year. 18
No. 3/ 2016





Универзитет "Св. Кирил и Методиј"
ЕКОНОМСКИ ИНСТИТУТ

ISSN 1857-7741 (online)
UDC -338

Economic Development **Економски развој**

JOURNAL OF THE INSTITUTE OF ECONOMICS - SKOPJE

Year. 18 No. 3/ 2016

Skopje, February, 2017

Economic Development

Published by:

Institute of Economics- Skopje, University "Ss.Cyril and Methodius",
Republic of Macedonia

Editor in chief:

Biljana Angelova, Ph.D. (Institute of Economics- Skopje, Macedonia)

Editorial Board:

Biljana Angelova, Ph.D. (Institute of Economics- Skopje, Macedonia)

Diana Boskovska, Ph.D. (Institute of Economics- Skopje, Macedonia)

Natasha Daniloska, Ph.D. (Institute of Economics- Skopje, Macedonia)

Vasile Dinu, Ph.D. (Academy of Economic Studies, Bucharest, Romania)

Angelo Manaresi, Ph.D. (Alma Mater Studiorum-University of Bologna, Italy)

Maja Micevska Scharf, Ph.D. (Netherlands Interdisciplinary Demographic Institute, The Hague, Netherlands)

Goran Penev, M.Sc. (Institute of Social Sciences, Belgrade, Serbia)

Ivan Tchalakov, Ph.D. (University of Plovdiv, Bulgaria)

Secretary of editorial board: Sretanka Gjorgjievska

Cover design: Koco Fidanovski

Computer preparation and printing:

UDK -CIP Catalogue record from National and University Library

"St.Kliment Ohridski"- Skopje

© Institute of Economics-Skopje

Address:

Institute of Economics-Skopje

Prolet 1

1000 Skopje

Republic of Macedonia

phone : +389 2 3115 076

fax : +389 2 3226 350

E-mail: eis@ek-inst.ukim.edu.mk

Published **three times per year**

Available on the websites: www.ek-inst.ukim.edu.mk

Abstracted/ indexed in: *EBSCO Business Source Complete, EBSCO Discovery Service (EDS) in EBSCO Publishing Database, (Ipswich USA); CEEOL Central and Eastern European Online Library, (Frankfurt am Main, Germany)*

Price: 350, 00 MKDenars; 15 EUR

Copyright © 2017 Institute of Economics- Skopje - All rights reserved

The Ministry of Education and Science of the Republic of Macedonia has financially participated in printing the journal. In accordance with the decision No.07-3266/20 as of 11 July 1999 by the Ministry of Finance of the Republic of Macedonia, a reduced tax rate has been paid for publishing "Economic Development".

CONTENTS

Biljana Angelova, Diana Boskovska

SHARE OF LOANS TO HOUSEHOLDS IN NON-
PERFORMING LOANS OF BANKS IN MACEDONIA
(Original scientific paper) (1-10)

Marija Ackovska, Neda Petroska- Angelovska

FEATURES IN IMPLEMENTATIONS OF FINANCIAL
CALCULATIONS IN TOURISM SECTOR ENTERPRISES
(Original scientific paper) (11-22)

Verica Janeska, Silvana Mojsovska, Aleksandra Lozanoska

BRAIN DRAIN FROM THE REPUBLIC OF
MACEDONIA-TRENDS, IMPLICATIONS, POLICIES
(Original scientific paper) (23-37)

Tatjana Petkovska Mirchevska, Meri Karanfilovska

SOCIAL MARKETING AND ITS APPLICATION IN THE
REPUBLIC OF MACEDONIA
(Original scientific paper) (38-49)

Diana Boskovska, Biljana Angelova

APPLICATION OF THE SIMPLIFIED CUSTOMS PROCEDURE –
THE CASE OF THE REPUBLIC OF MACEDONIA
(Original scientific paper) (50-60)

Vasil Popovski, Hristina Serafimovska

ORGANIZATIONAL CULTURE IMPERATIVE FOR HIGHER
INNOVATION IN ENTERPRISES IN THE REPUBLIC OF
MACEDONIA
(Original scientific paper) (61-74)

Klimentina Poposka, Elena Mihajloska

THE IMPLICATIONS AND AFTERMATH EFFECTS OF
THE FINANCIAL CRISIS ON STARTUPS IN EU
(Original scientific paper) (75-90)

Vasil Popovski, Slobodan Levkovski, Ljubisha Nikolovski

SELF EMPLOYMENT PROGRAM VIA CREDITING AS AN
INCENTIVE FOR INCREASING ENTREPRENEURIAL
ACTIVITY IN REPUBLIC OF MACEDONIA
(Original scientific paper).....(91-107)

- Neda Petroska- Angelovska, Marija Ackovska**
 FINANCIAL RATIOS FOR ASSESSMENT OF
 OPERATIONS SUCCESS IN ENTERPRISES OF
 MACEDONIAN HOSPITALITY INDUSTRY
 (Original scientific paper)(108-119)
- Irina Majovski, Elena Davitkovska**
 DEVELOPING EMPLOYEE SKILLS IN
 CHALLENGING TIMES
 (Original scientific paper)(120-133)
- Natasha Daniloska**
 INSURANCE IN AGRICULTURE-SITUATION IN THE
 REPUBLIC OF MACEDONIA
 (Original scientific paper)(134-151)
- Elizabeta Djambaska, Vladimir Petkovski,
 Aleksandra Lozoska**
 CAPITAL MARKET AND THE DETERMINANTS
 OF DEVELOPMENT IN THE REPUBLIC OF MACEDONIA
 (Original scientific paper)(152-165)
- Iskra Stanceva-Gigov**
 THE BENEFITS OF TRADE LIBERALIZATION AND ITS
 CONTRIBUTION TO ECONOMIC GROWTH
 (Original scientific paper)(166-178)
- Vladimir Petkovski, Elizabeta Djambaska,
 Snezana Kostadinovska Milosovska**
 THE FUNDAMENTAL CONSIDERATIONS OF THE
 PUBLIC DEBT
 (Original scientific paper)(179-191)
- Katerina Hadzi Naumova -Mihajlovska**
 OPPORTUNITIES FOR TQM TRAINING IN
 ASSOCIATIONS OF ORGANIC PRODUCERS IN
 REPUBLIC OF MACEDONIA
 (Original scientific paper)(192-207)

- Marko Andonov, Zoran Janevski,
Elena Davitkovska, Irina Majovski**
CURRENT LEGAL SETTING AND FUTURE MARKET
REGULATORY CHALLENGES OF SECURITIES
MARKET IN THE REPUBLIC OF MACEDONIA
(Original scientific paper)(208-219)
- Fatmir Besimi, Azis Pollozhani**
EDUCATION AND HUMAN CAPITAL: ECONOMIC
GROWTH AND SOCIAL COHESION IN MACEDONIA
(Original scientific paper)(220-235)
- Janka Dimitrova, Olivera Gorgieva – Trajkovska,
Blagica Koleva, Aleksandra Nachkova, Eftimija Dimitrova**
CORPORATE GOVERNANCE AND FINANCIAL
REPORTING IN MACEDONIA THROUGH THE PRISM
OF INDEPENDENT AUDITORS REPORTS
(Original scientific paper)(236-254)
- Dejan Krstevski, Gjorgji Mancheski**
TELECOM COST OPTIMIZATION:HOW TO
SUBSIDIZE HANDSET SUBSIDIE
(Original scientific paper)(255-266)
- Sergej Naumovski, Marjan Bojadjiev,
Ana Tomovska-Misoska, Miodraga Stefanovska-Petkovska**
ORGANIZATIONAL ALIGNMENT IN THE FOOD
INDUSTRY: CASE STUDY OF A COMPANY IN THE
REPUBLIC OF MACEDONIA
(Original scientific paper)(267-280)
- Tome Nenovski, Ninko Kostovski, Dobrila Dejanoska**
INFLUENCE OF FOREIGN DIRECT INVESTMENTS
TO EXPORT AND GROSS DOMESTIC PRODUCT OF
DEVELOPING COUNTRIES – SPECIFICS OF REPUBLIC
OF MACEDONIA
(Original scientific paper)(281-294)

Katerina Fotova Čiković	
EFFECTS OF THE ENTRANCE OF FOREIGN CAPITAL IN THE MACEDONIAN BANKING SECTOR	
(Original scientific paper).....	(295-308)
Edvin Mushe	
CUSTOMER SATISFACTION IN THE MACEDONIAN OIL RETAIL SECTOR	
(Original scientific paper)	(309-326)
Tome Nenovski, Jadranka Mrsik, Simona Trpovska	
A FRAUDULENT BEHAVIOR OF INVESTMENT BANKING AS ONE OF THE REASONS FOR THE APPEARANCE OF 2008 WORLD ECONOPMIC CRISES	
(Professional paper)	(327-339)
Mite Mitevski	
AUDIT ON THE EU INSTRUMENT FOR PRE- ACCESSION ASSISTANCE (IPA) – THE CASE OF THE REPUBLIC OF MACEDONIA	
(Professional paper)	(340-353)
Marija Magdinceva Sopova, Tanja Angelkova Petkova, Zoran Temelkov	
THE IMPACT OF SMALL AND MEDIUM ENTERPRISES IN THE DEVELOPMENT OF SPORTS TOURISM IN THE MINICIPALITY OF DOJRAN, REPUBLIC OF MACEDONIA	
(Review paper).....	(354-365)
Authors` guidelines	366
Editing instructions	368

Dear reader,

“Economic Development”, published by the Institute of Economics – Skopje, is an academic journal in the field of economic development and has been an important medium for 14 years. The main goal of “Economic Development” is to provide intellectual platform to the wider academic and professional publics, and promote the development of economic thought in the country and the world. The interest and need for publishing of the journal were continuously increased all these years.

On the path of development of the economic thought and building a wide network of research and professional cooperation with other countries in the world, we set new goals, criteria and challenges in order to improve the journal’s quality. In this regard, during 2010 and 2011, significant changes have been made in editorial policy, design and its availability to broader academic and professional public in the region and worldwide. As result of all this changes, starting from no. 3/2010 “Economic Development” will shift into international journal, will be published in English language and will be distributed in all countries of the region and worldwide.

This academic journal covers theoretical and empirical researches in the field of economic and social development, demography, education, corporate governance, international economics, international management, administrative management, corporate and public finance, economics and tourism management, agricultural policy and agricultural management, marketing and marketing management, entrepreneurial management and other areas in the field of social sciences.

The journal “Economic development” has an open approach in accepting and publishing the papers reviewed by an international editorial board consisting of three domestic and five foreign experts. The journal is available in print and online form, through the database of academic papers published by the Institute.

Skopje, May 2016

prof. Biljana Angelova, PhD
Editor-in-chief

BILJANA ANGELOVA*
DIANA BOSKOVSKA**

**SHARE OF LOANS TO HOUSEHOLDS IN
NON-PERFORMING LOANS OF THE BANKS IN MACEDONIA**

Abstract

Banks as key financial institutions have the greatest importance in the financial system, its main function is the transformation of deposits in funding. Activities pursued by modern banks often include both banking and non-banking services. For sound monetary policy is necessary to take-over key reforms and restructuring of the banking system. The banking system in the Republic Macedonia has possibilities for increasing and improving the efficiency of the banks, since the index of household loans / GDP according to we are among the last countries in transition countries. Unlike the banking systems of transition economies, the performance of the Macedonian banking system has been a trend in the improvement of banking processes and procedures. Depending on all types of loans contained in the range of products offered by banks and their functionality depends on the growth and profits of banks since the credit activity is one of the basic functions and carries the greatest profitability for banks. Borrowers apply for a loan may have various purposes. Banks create products to meet the different needs of different users.

Key words: bank, loans, households, non- performing loans.

JEL classification: G21

* PhD, full-time professor, Institute of Economics-Skopje, University „Ss. Cyril and Methodius“-Skopje, E-mail:angelova@ek-inst.ukim.edu.mk

** PhD, associate professor, Institute of Economics-Skopje, University „Ss. Cyril and Methodius“-Skopje, E-mail:diana@ek-inst.ukim.edu.mk

1. NON-PERFORMING LOANS AND CLASSIFICATION OF BORROWERS

According to the Decision (Official Gazette No. 21 / 02- revised text) of the Central Bank in laying down and classified according to their risk balance sheet and off balance sheet assets, which are required in determining the loans classified in risk categories B, C and D in the case of outstanding matured or fully matured obligations (interest, annuity or full principal) that stems from ongoing personal accounts, payment (debit and credit) cards, short-term and long-term credit transfer for a period exceeding 90 days from the date of maturity of accounts for bad and doubtful debts as non-performing loans.

After their transfer it requires analysis to monitor the collection of such disputed claims, to calculate interest, to align payments, to perform calculations and prepare reports to finally liquidate suspiciously claim or if they charge disputed due receivables (due installments interest) return to regular accounts or to respect the agreement on rescheduling of the loan. Maturity of the loan is the day when the amount of principal and all accrued fees and interest should be covered by the loan.

After the transfer of receivables, after balancing the credit party full habitual condition is transferred to the account of bad and doubtful debts with full and complete documentation in order processing trial. If the loan is secured by a promissory note used all tools for payment and make contact with the guarantors, if any, then inform the borrower from the consequences of the process of enforcement, with ultimate payment of the claim and avoiding court proceedings, and court costs.

Total claims classified in the riskiest category “D” of a bank customer that spent two consecutive quarters is obliged to reenter to the account that will recorded claims with a degree of probability of recovery.

2. THE CASE OF NON-PERFORMING LOANS OF REPUBLIC OF MACEDONIA

Banks' lending activity results in wearing the most profitable solutions, but credit activity if placed unsecured and forcing an increase in credit activity only to be ahead of competitors and maximize profits is the

most common cause of bankruptcy of banks. Thus non-performing loans in credit portfolios of banks are increasing and affecting adversely working efficiency.

The biggest problem of Macedonian banks, based on information from the Central Bank, is a high credit risk, which occurs as a result of weaknesses in the full application of policies and procedures and internal control system. Mainly, the credit risk is manifested by inadequate identification systems, quantification and its monitoring.

Riskiness of banks and their dexterity in dealing with risk, Central bank has determined by CAMEL's methodology that despite the risk, analyzes banks' assets, capital adequacy, profitability, liquidity and market risk. According to this methodology, the banks get the grades from 1 to 5. These analyzes also give information for the degree of harmonization of regulations on banks and their operations with the legislation, respecting the decisions taken by the Central Bank, particularly respecting decisions for quantification of the risk of errors and so on.

The Macedonian banks are most exposure on credit risk primarily due to weakness in credit analysis, high concentration of credits in few companies and consequently low diversification of risks. Then high level of foreclosed mortgages which are great burden on banks. All these indicators represent a consequence of the accumulation of bad loans in operation.

Credit risk has most important role and is outstanding factor that affect performances of Macedonian Banks, which is result of dealing with traditional business model – collecting deposits from the domestic private sector and their placement in form of credits intended for domestic non-financial sector.

The range of credit products for households in the period after the independence of Macedonia was relatively weak and with poorly developed market. In the period of privatization and transformation of ownership structure it is characterized by applying the conservative monetary policy by the Central bank, mostly due to a high level of non-performing loans in the portfolios of some biggest banks.

After a difficult period and economic stabilization, banks gradually began to build a system for dealing with risks and to promote and expand the supply of wide range of credit products and reduce non-performing loans. From 2004 until 2008 the credit growth in the country is characterized by double-digit annual growth rates, and the share of non-performing to total loans was marked by historic minimum rate of

6.6%. But the picture is beginning to change with the onset of the financial global crisis in September 2008, after the non-performing loans have continued growing. In recent years, the years after the crisis the share of non-performing loans to total loans increased almost twice and at the end of September 2015 was 11.7%, which is twice the rate recorded in 2008. The situation is similar with the countries in the region and European economies, sometimes even more dynamic and intensity. In line with MMF and WB statistics at the end of 2013 developed economies have significant fall in economic growth and non-performing loans reached almost 90% of total credits in Ireland, or near 80% in Italy and approximately 30% of non-performing loans in average for the rest developed EU countries and USA. The situation with non-performing loans in developing countries is much worse as a result of their weak and vulnerable economies. In average non performing loans reached up to 40% of total loans, except Turkey, where non-performing loans were up to 5% of total loans. Banking sector of Serbia, Albania and Montenegro was most affected by financial crisis and non performing loans reached almost 70% in Serbia and near 60% in Albania.

Non-performing loans are significant category of research, that brings losses for banks and increased financing costs. Nonperforming loans reduce economic growth, increase the level of unemployment, affect macroeconomic policies and restrict credit supply to the private (non-financial) sector where banks play a major role in the financial market. Slower credit growth in recent years is around 9% versus rapid growth of non-performing loans. In the period before the economic crisis credit growth amounted up to 30%. Theoretically, the high share of non-performing loans is an indicator of the occurrence of financial crises and destabilization of the financial sector. Dealing with nonperforming loans by Macedonian banks, is almost reduced to zero as it reported in the financial statements.

Potential losses and unfavourable effects arising from the amount of non-performing loans on capital positions of Macedonian banks are quite limited. High concentration of non-performing loans in the banking system deteriorate the quality of bank's portfolio and unfavourable affect their portfolio particularly when their portfolio is composed by certain number of customers and when their creditworthiness is seriously deteriorate.

In the past few years the share of non-performing loans given to domestic companies in the total amount of non-performing loans is 85%.

Loans to sectors wholesale and retail, manufacturing industry and construction accounted for the majority of non-performing loans. Traditional high concentration in the loan portfolio of the corporate sector accounted for 60% of the total amount of non-performing loans, and this percentage is composed fifty largest amounts of loans granted to legal persons. In dysfunctional household loan portfolio accounted for most of the loans for personal consumption and resulted in relatively lower amounts compared to the loan portfolio of the corporate sector. Macedonian banks as long as there is the slightest possibility of recovery is not using the opportunity to write off the claims but use all collateral given in loan approval.

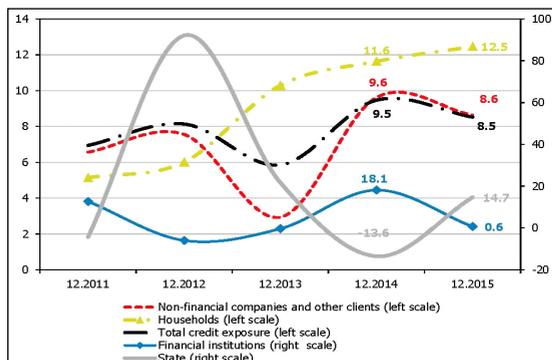
Such an approach to non-performing loans keeps them very long in the balance sheets of domestic banks, and it can determine by analysing the age structure of these loans. Besides activation of the instruments given as collateral for the loans, the opportunities that are available to domestic banks but are less commonly used is secondary trading with non-performing loans.

In the past year despite political turmoil, unstable domestic and external environment, the banking system maintained its stability and resilience to shocks. Amid slow recovery of the global economy, but solid economic growth in the country, banking intermediation between savers and borrowers continued to strengthen, but slowly

Assets, loans and deposits, on an annual basis, rose by 5.8%, 9.7% and 6.7%, respectively (2014: 8.3%, 9.9% and 10.7%, respectively). Environment in which banks worked in the previous year was characterized by the debt crisis in Greece, the political turmoil in the country, low interest rates have limited opportunities for higher growth in the sources of funding for banks. The most significant risk to the banks or credit risk does not cause increased concern in 2015.

The slower growth of nonperforming loans in solid growth in bank lending contributed to the reduction of the share of non-performing loans to total loans at the end of 2015, which after several quarters falls below 11%, and reduced to 10.8%. Non-performing loans in total loans to the corporate sector at the end of 2015 was 15.2%. The capacity of the banking system to absorb unexpected credit losses is increasing and requires more attention be paid and restructured loans because their condition is impaired in previous years, with growth of nonperforming loans, a decrease of standard loans.

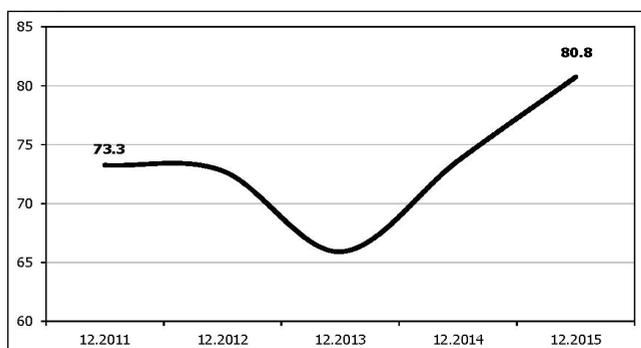
Chart 1: Annual growth of sectors, credit exposure to all, by sector in %



Source: http://www.nbrm.mk/WBStorage/Files/Regulativa_Annual_2015.pdf accessed on 15 July 2016

In 2015, the total credit exposure of the banking system grew by 36,084 million or 8.5% to 459,658 million denars. Growth in 2015 is almost equally distributed between households and non-financial companies. The analysis of credit risk in this section refers to credit risk arising from both non-financial sectors, households and non-financial companies.(see Chart 1)

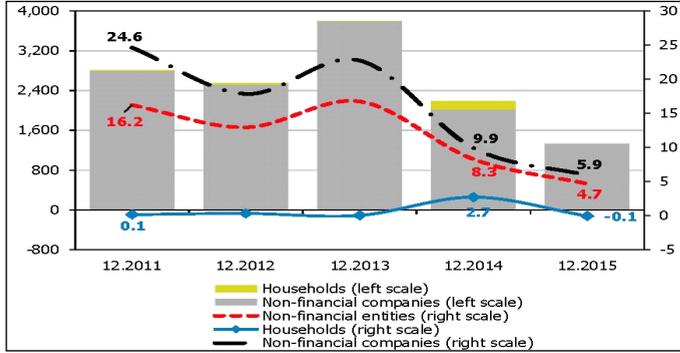
Chart 2: Share of the large exposures to nonfinancial entities in the banks' own funds



Source: http://www.nbrm.mk/WBStorage/Files/Regulativa_Annual_2015.pdf accessed on 15 July 2016

Receivables from non-financial companies registered a high level of concentration in the credit risk. Share of large exposures in banks' own funds has an annual growth as of 31.12.2015 was 80.8% (See Chart 2)

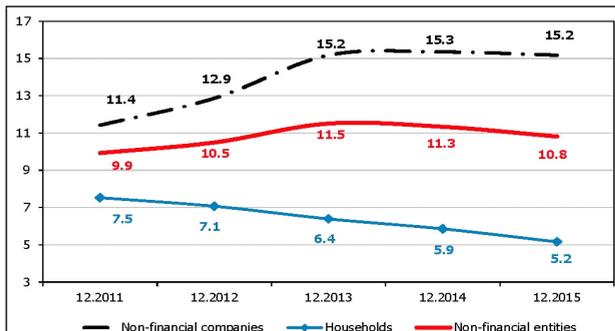
Chart 3: Annual growth in the non-performing loans for non-financial entities (in millions denars and in %)



Source: http://www.nbrm.mk/WBStorage/Files/Regulativa_Annual_2015.pdf accessed on 15 July 2016

The annual increase in non-performing loans to non-financial entities in the portfolio of banks is characterized by a reduction or improvement over previous years. Non-performing loans in bank portfolios of banks in 2015 decreased to 4.7%, which is also the lowest rate since 2008. The trend of non-performing loans mainly depends on the participation of non-performing loans to non-financial companies is decreasing in 2015 and is 5.9%. Loans of households still are relatively small and stable, decreased in 2015 by 0.1%.(see Chart 3).

Chart 4: Share of non-performing to total loans (for non-financial entities) in %



Source: http://www.nbrm.mk/WBStorage/Files/Regulativa_Annual_2015.pdf accessed on 15 July 2016

Non-financial companies represent the growth of total non-performing loans and in 2015 the growth rate was 10.8%. The majority or 89.2% of the portfolio is in regular repayment. The trend in the share of non-performing to total loans recorded a slight decrease, which is due to the faster growth of total nonperforming loans, but it is twice higher than in the crisis period of 2008. (see Chart 4)

Expanding the range of banking products and increase the efficiency of banking is a trend to which Macedonian banks aspire to reach the level of developed economies in transition. Improvement of systems for handling credit risk not only in the analysis of credit requirements, but in the whole life process of the loan is the best way to deal with a dysfunctional status of borrowers.

Careful reprogramming of claims and change of conditions agreed with their adaptation to the conditions favorable to the borrower that will yield positive results, can maintain or reduce the growth of non-performing loans.

Conclusion

Banks as key financial institutions have the greatest importance in the financial system. Although the most important functions of banks' are credit and deposit function, activities of modern banks besides traditional spread to a number of non-banking services. For sound monetary policy is necessary to take key reforms and restructuring of the banking system. The banking system in the country has possibilities to increase and improve the efficiency of the banks, because according to the index of household loans / GDP, we are among the last countries in transition countries. Unlike the banking systems of transition economies, the performance of the Macedonian banking system has been a trend in the improvement of banking processes and procedures. Depending on all types of loans contained in portfolio of products offered by banks and their functionality depends on the growth and profits of banks since the credit activity is one of the basic functions and carries the greatest profitability for banks.

More intensive lending by banks by easing the conditions for obtaining credit, lower interest rates and diversified supply of credits ranging upwards share of loans in GDP. GDP / Loans relate directly proportional, ie if we have economic growth and increased lending activity.

upwards share of loans in GDP. GDP / Loans relate directly proportional, ie if we have economic growth and increased lending activity.

From the research component if the trade deficit has an impact on retail lending, then observed correlation, or relatedness between consumer credit and import of a wide and personal consumption. Correlations inflation - consumer loans are not exhibits significant connectivity and interdependence.

Credit risk is highly determined by the approvals of loan applications, increased credit activity brings greater risk, which if not controlled can only worsen the loan portfolio and to increase the percentage of non-performing clients. Credit risk associated with currency and liquidity risk.

Domestic drivers of growth and resilience of the economy, despite the unfavorable environment that prevails in the country, however, resulted in a positive trend, ie accelerated pace of growth of GDP, the credit activity of the banking system.

Management of banks with dysfunctional portfolio and their reduction is a result of constant monitoring and control of bank officials primarily. As previously well conducted credit analysis when approving the application and consideration of the potential hazards, which in turn depends on the training and skills they possess or to teach clerks, better results would have been if banks invest in their staff, upgrade as well as continuous improvement of the working process. The analysis of the loan portfolio shows that the dominant category in the portfolio is category „A,, which approve credit applications.

Compared with countries in the region according to the indicator households' debt / GDP we can conclude that the indebtedness of the population in Macedonia is higher only than the indebtedness of the population in Serbia, Romania and Hungary.

Nonperforming loans reduce economic growth, increase the level of unemployment, difficult macroeconomic policies restrict credit supply to the private sector where banks play a major role in the financial market.

Expanding the range of banking products and increase the efficiency of banking is a trend to which Macedonian banks aspire to reach the level of developed economies in transition. Improvement of systems for handling credit risk not only in the analysis of credit requirements, but in the whole life process of the loan is the best way to deal with a dysfunctional status of borrowers.

References:

1. Angelova B., Poposka K., Vlijanieto na finansikata kriza vrz nefunkcionalnite krediti i zadolzenosta na kompaniite i na gragjanite vo Republika Makedonija, Ekonomski institute, Skopje, 2015.
2. Chmelar, Ales, "Household Debt and the European Crisis", European Credit Research Institute, 2013.
3. Madzova B. „Kreditna politika“, UGD, Stip, 2011.
4. Juselius, Mikael, Drehman, Mathias, "Do debt service costs affect macroeconomic and finansial stability?", Bank for International Settlements, 2012.
5. Petreski G. „Upravuvanje so bankite, UKIM, Ekonomski fakultet, Skopje, 2011
6. Jappelli, Tullio, Pagano, Marco, "Households' Indebtedness and Financial Fragility", 9th Jacques Annual Research Conference, Washington DC, 2008.
7. Trpeski Ljube, "Bankarstvo i bankarsko rabotenje", Ekonomski fakultet, Skopje, 2009.
8. http://www.nbrm.mk/WBStorage/Files/Regulativa_Annual_2015.pdf

MARIJA ACKOVSKA*
NEDA PETROSKA-ANGELOVSKA**

FEATURES IN IMPLEMENTATIONS OF FINANCIAL CALCULATIONS IN TOURISM SECTOR ENTERPRISES

Abstract

This article is focused on issues related to specific characteristics of financial calculations in tourism sector enterprises. Features of calculations in this sector arise from the differences in tourism products and services, time distribution of tourism flow and the level of capacity utilization.

The implementation of financial calculations in tourism sector enterprises has two main aims: taking into account of all costs related to tourism products and services, their proper allocation and quantification. Mentioned aims of calculations are basic prerequisites for real and exact estimation of product and service prices in the sector. It is also important to specify that final price of this product and service is formed not only as a result of quantification of all costs but also it is influenced by the tourism market supply and demand.

Elaborated issues in this paper notify the importance of implementation of financial calculations in this sector regarding the better price estimation, improvement in controlling process of internal operations and managing of capacity utilization in tourism sector enterprises.

Key words: financial calculation, cost estimation, calculating methods, enterprises, tourism sector.

JEL Classification: M21; M41; Z3

* Ph. D, associate professor, Institute of Economics-Skopje, University "St. Cyril and Methodius", e-mail: marija@ek-inst.ukim.edu.mk

** Ph. D, associate professor, Institute of Economics-Skopje, University "St. Cyril and Methodius", e-mail: neda@ek-inst.ukim.edu.mk

Introduction

Implementation of financial calculation, price and margin estimation and normatives of tourism product and services are legal obligation in tourism sector enterprises. In tourism sector, total income and expenditures are planned with the aim of satisfactory profit level achievement. Those presumptions are built according the prices established on the basis of financial calculations. It is therefore very important to keep in mind the importance of applying calculations, pricing, margin and regulations in decision making of management in tourism business, both in terms of adequate quality of tourism products and services, and in terms of the positive business performance and achieving profit which seeks to every enterprise.

It should be emphasized that in pricing there is some difference depending on whether enterprise refers to hospitality or catering industry. There is also a difference in pricing in hospitality depending on the duration of working period and location (the place of performance of individual hotel facilities).

Namely, in catering industry that products and services are sold to domestic population ie domestic guests, the prices are formed mainly under the conditions prevailing on the domestic market. It means that the level of prices of goods and services in catering industry depend on supply and demand for those products and services that are formed in this branch of catering. Important is to emphasize the fact that prices in catering industry are equal both for domestic and foreign guests or tourists.

Prices of goods and services in hospitality industry that works for all seasons on non - touristic locations are also formed depending on conditions prevailing on domestic market and they are generally the same for the whole year. Exception of this are countries where inflation phenomena very high. Price differences that occur in these facilities are result of their different location and the level of capacity utilization ie the absorption volume of products and services by domestic and foreign guests or tourists.

In seasonal hospitality and hotel facilities in tourist areas that operate for a whole year, selling prices of products and services are interchangeable depending on the stay period of guests. For example, in the tourist season prices of goods and services are higher even though the price of the cost per unit or per unit of service in that period is lower. Conversely, outside the season, when cost price of products and services are higher in general, selling price of goods and services are lower.

Also in tourist areas, price of products and services, hoteliers calculate primarily depending on conditions prevailing on foreign markets and ex ante for one year in advance. So, in these situations cost price is only approximate size that influence the final price. Therefore, the selling price of hotel products and services in tourist areas differ from those in other places. Namely, while hotels in tourist areas usually are offering boarding services, those in non - touristic places mainly provide only accommodation services ie night (possibly with breakfast).

1. TYPES OF FINANCIAL CALCULATIONS IN CATERING INDUSTRY

Financial calculation means to calculate cost price and selling price for certain products and services in general and therefore for products and services in hospitality industry, also. Hence, main tasks of financial calculation are - as accurately as possible to calculate the cost price for separate goods and services that in general is orientation in process of determining selling price of same products and services.

According to various criteria can be executed various types of calculations. The classification of financial calculations commonly is performed according to the following criteria:

- 1) According to the time period;
- 2) According to price calculation of catering products and services;
- 3) According to the method of cost calculating ie of cost price of certain products and services in different operating conditions;
- 4) According to whether in calculating process margin is taken into account.

From the standpoint of the time period that calculation is made for, calculations vary:

- 1) Previous or planned calculation, and
- 2) Next or accrual calculation.

Previous or planned calculation is the calculation that is usually compiled at the beginning of the year. It is based on statistical data that are available in catering enterprises for the previous period, and corrected with the predicted flow of revenues and costs in the future period. Previous calculation serves as the base for:

- determining the intended scope of products and services,
- for determining selling prices and
- to calculate the planned indicators which reflect planned productivity, efficiency and profitability in the operation of catering enterprises and their business units.

During the preparation of planned calculation, commonly comparative method of planned and realized costs is applied. which points to certain derogations for certain planned costs and also is the first step in the analysis of the reasons for such deviation.

Next or accrual calculation is that calculation. which is compiled based on data about actual costs by places and units (products and services) in the previous accounting period. The data from this calculation are base for analysis and evaluation of realized productivity, efficiency and profitability of certain catering establishments as a whole and especially in their business units commonly represent as a separate profit centers. This calculation shows how realistic were assumptions of planning calculation.

According to the price calculation of certain catering products and services, mainly are distinguished the following types of calculations:

- Calculation for BB;
- Calculation for HB;
- Calculation of FB;
- Calculation of certain types of foods;
- Calculation per type of drinks
- Calculation of various other services to guests or tourists (barber, hairdresser, car services, washing, ironing and cleaning of clothes, postal services, etc.).¹

¹ Ackovski, N.; Ackovska M.: *Ekonomika i organizacija na ugostitelstvoto*. Grafomak

According to the cost calculating method, ie cost price for certain products and services in different operating conditions following types of calculations can be distinguished:

- Division calculation;
- Calculation of equivalent numbers and
- An additional calculation.

Whether in process of price calculation of products and services is included margin or no, is differ following calculations:

- Calculation without margin included and
- Calculation with included margin.

Calculation without margin included is that which serves for calculating only sells price of the basic material without inclusion of margin.

Calculation including margin is that which determines total sales value, sales value of a particular group or subgroup of products or services and the sales value (sales price) in certain products and services. For example: the total sales value (sales value of all products and services of a catering organization) is obtained so that the total cost of consumable basic material is added to the margin.² The sales value of a particular group or subgroup of products or services are obtained when the value of the used base material for the appropriate group of products or services are added to the appropriate amount of margin. Finally, the selling value (selling price) of individual catering products or services is obtained so that the total sales value i.e sales value of the particular group or subgroup of products and services is divided by the number of goods and services.

Specifics of calculations in the hospitality industry derive from the number of products and services, calculation for time period of turnover and capacity utilization that make difficult the assessment of supply and demand for catering products and services. Hence, in hotels almost decisive role have fixed costs, variable costs in catering industry have no

Kicevo, Ohrid, 2003.p.189.

² Ibid p. 195.

significant effect on total costs for certain products.³ According to the subject, calculations might be for: overnight, board and lodging, accommodations, consuming food and beverages, and other complementary commodity and non-commodity services. It should be emphasized that the calculations for products significantly differ from the calculations of services taking into account the participation of various inputs in the process of their production.⁴

2. PREPARATION METHODS OF CALCULATIONS IN HOSPITALITY INDUSTRY

Methods of compiling accrual calculations as technical costing procedure is different because there are differences among the numerous products and services in hospitality. Different methods of costs estimation are called methods of calculations. Main objective of all the methods of calculation is units of expenses (products and services) to be burden with costs incurred in the production of those products and services. Moreover, purpose is products or services to be burden more realistic in order to determine their actual cost price.

From previous, it can conclude that related to direct costs there is no problem in allocating to products and services. These cost are known per unit through various calculations. In hospitality, mostly used calculations are:

- Division calculation
- Calculation of equivalent numbers
- An additional calculation.\

Division or divided calculation is applied in circumstances where there is only mass production of only one product or mass performing of only one service. Construction of this kind of calculation is very simple

³ Unkovic, S. *Ekonomika turizma, Savremena administracija*, Beograd, 2001. p 156.

⁴ .Bull, A.: *The economics of travel and tourism*. Longman. Sydney, 2008. p. 241.

operation because it is performed only by dividing the total cost by number of goods and services. Namely, for example, the total amount of indirect costs in a garni hotel for total number of overnight stays in 2015 are 100,000 denars, and in that year period is generated 1,000 overnight stays then the amount of the total cost of one night will amount to 100 denars ($100.000 / 1.000 = 100$). So, in this calculation it is not necessary to carry out separation of costs on direct and indirect.

The calculation of equivalent numbers is applied in circumstances where a catering company is producing identical products or services that differ in quantity and quality. This is for example the case when the overnight stays of guests is done in rooms with different quality of accommodation ie in rooms of category I (single rooms) category II (double rooms) etc. In that case, first is calculating the so-called equivalent numbers for each quality of service so that each equivalent number is actually a conditional number of nights for the appropriate quality of service, and the sum of these numbers shows the total number of contingent nights. The cost for one conditional night are estimated so that the average amount of daily expenses is divided by the sum of contingent nights.

Further on, also is presented an example of calculating equivalent numbers and cost price for one overnight stay by the quality of service by applying the calculation of equivalent numbers. Moreover, these calculations are implemented under following assumptions:

- 1) The capacity of the hotel "X" is 300 beds of which 50 beds are in single rooms, 160 beds in double rooms and 90 beds in triple rooms.
- 2) The percentage of utilization of that capacity for the year 2015 is 70 %, ie 252 days per year .
- 3) The total amount of indirect costs to the respective hotel in the same year is 10.000.000 denars and average daily cost at 27, 777.77 denars.
- 4) The ratio of costs between III 's, II 's and I's category of service accommodation is 1.0: 1.2: 1.6 .

Calculating the equivalent numbers (conditional number of overnight stay by the quality of service accommodation)

Quality of accommodation service	Number of beds	Number of overnights per day	Ratio between expenditure and service quality	Equivalent numbers (conditional number of overnight stay)
Single room	50	35	1.6	56.0
Dauble room	160	112	1.2	134.4
Triple room	90	63	1.0	63.0
Total:	300	210		253.4

Otherwise, in application of this method is sufficient to know total costs, ie, it's not needed to distinct direct from indirect costs.

Calculating the cost (cost price) for one over night according to quality of service using equivalent numbers

Quality of accommodation service	Equivalent numbers (conditional number of overnights per day)	Costs per con- ditional number of overnights deily (in denars)	Total costs per separte quality of accommoda- tion Service (in denars)	Overnights per day	Costs per one overnight daily (in denars)
Single room	56.0	109.62	6.138.72	35	175.39
Dauble room	134.4	109.62	14.732.93	112	131.54
Triple room	63.0	109.62	6.906.06	63	109.62
Total:	253.4		27.777.77	210	132.27

Additional calculation is estimated when catering enterprises are engaged in production of different types of products or services. Such is, for example, the case in catering establishments that prepare various foods, which offers various kinds of drinks and where there are various types of services. For more realistic preparation of calculation of cost for FB or HB services, or for certain foods, drinks and beverages as well as for various types of accommodation services and other personal services to the guests, total cost must be divided into direct and indirect. Moreover, given that the direct costs per unit of product or service eg unit costs are known, the problem boils down to calculating the indirect costs of the products and services. The division of indirect costs on certain cost units is done by cost key (criteria). Moreover, as key for differentiation of indirect costs per individual assortments (types) of products or services can serve share of wages for production of certain products and services or the cost of materials for the manufacture of those products and services, or commonly sum of two elements. Finally, the amount of costs obtained in any of the aforementioned methods (keys, criteria) is added to the amount of total costs, ie, of cost of individual products and services. That's the reason why this calculation is called additional calculation.

The percentage of indirect costs is obtained when the amount of direct costs per assortment (product or service) is multiplied by 100 and so result is divided by amount of direct costs or applying the following formula:

$$\% \text{ of indirect costs per assortment} = \frac{\text{Direct costs per per assortment} \times 100}{\text{Total direct costs}}$$

By multiplying the direct costs range with the established rate, amount of indirect costs is calculated.

Otherwise, except for certain types of products and services, additional calculation can be applied for estimation of cost price on group of products or services. Often this calculation is performed for different types of food as well as for certain groups of foods. Further on, is presented an example of additional calculation for cost estimation of certain types of food as well as for group of products, if it is you know that:

- Catering company “ X” produced (prepared) three kinds of products including kebabs, burgers and steaks;
- In July 2015 it plans to spend and therefore to produce 15, 000 kebabs, burgers 2.000 and 1.000 veshalici;
- For production of barbecue products planned direct costs for the amount of: for cevapi 60.000 denars, 40.000 denars for hamburgers and for veshalicite 50.000 denars or 150, 000;
- The total indirect costs of enterprise amounted to 50.000.

Additional calculation for food company “X” for the month of July 1995

Type of products	Number of products	Amount of direct costs (MKD)	Participation (In%)	Amount of in-direct costs (MKD)	Amount of total costs (MKD)	Price per unit (MKD)
kebab	15.000	60.000	40.00	20.000	80.000	5.33
burgers	2.000	40.000	26.67	13.335	53.335	26.67
steaks	1.000	50.000	33.33	16.665	66.665	66.67
Total:		150.00		50.000	200.000	

3. BASES FOR MAKING CALCULATIONS

When we take into account preparation process of calculations, there are few bases for their making:

- Accounting sheet;
- Data on trade and
- Plan of turnover and costs of catering enterprise as a whole and on individual buildings or units.⁵

Accounting sheet is compiled for each place (economic or unit of account) or any unit (separate product or service). This sheet shows the actual costs.

⁵ Ibid. p. 294

Data on turnover may be related to natural or value indicators of products and services. However, given the fact that catering is engaged in production and sales of many products and services, and costs depend on many other conditions it is very difficult to compile cost calculations on certain products and services. So, it is better rather than direct calculations for certain products and services first to make calculations for certain groups of goods and services (food, alcoholic drinks, soft drinks), and within these groups to make calculations for individual subgroups and ultimately calculations for individual products and services to be made.

The plan of turnover and costs can also be used for making calculations of catering company as a whole and for individual buildings or units. However, planning the scope of the cost of future operations in the hospitality is very difficult, complex and thankless job. The planning of future cost amount and turnover are mostly based on data for the past period and the evaluation of the possibilities and conditions for the costs and turnover in the future.

Conclusion

Business policy is a conscious activity of employees, and particularly of bodies of governance and management in enterprises. The main objective of the business policy in complex terms of doing business is achieving as much as possible income that could realize personal, common and general interests of the employees. This is achieved as with rising volume, structure and quality of products and services and with price policy, also.

Namely, in market economies where prices of products and services are set up, generally according to supply and demand that is present on the market, managers in order to achieve greater income will be necessary to reduce prices under market value (price). This is because in that case the demand for products and services offered by the respective catering enterprises will significantly increase, on the account of lower price per unit product or per unit service, it will be able to achieve something greater total profits. In circumstances, however, when a catering organization or any of its business unit has some monopoly (provide special services or offers special products that cannot be found in other organizations or were locat-

ed in the city center where frequency of the local population or tourists is greater in general) for their products and services might achieve a higher price and thus will result in higher income.

Hence, clearly leads to the conclusion that prices of goods and services is one of the most significant instruments in decision making and business policy guide of entrepreneurs and managers in catering enterprises.

References:

1. Ackovski, N.; Ackovska M.: *Ekonomika i organizacija na ugostitelstvoto*. Grafomak Kicevo, Ohrid, 2003.
2. Brealey A. Richard, Myers C. Steward, Allen Franklin: *Principles of Corporate Finance*, The McGraw-Hill Companies, (izdadero na makedonski jazik od ARS lamina 2015) 2011.
3. Brigham F. Eugene, Daves R. Philip: *Intermediate financial management*, Gengage learning Company, (izdadero na makedonski jazik od ARS lamina 2014) 2010.
4. Bull, A.: *The economics of travel and tourism*. Longman. Sydney, 2008.
5. Dohchevikj Sima: *Finansiska analiza kako instrument upravljanja finansijama u preduzeca*, Beograd, 1979.
6. Stefanovic, V.: *Ekonomika turizma*, PMF, Nish, 2003.
7. Spasic Vesna, Cerovic Slobodan: *Ekonomsko –finansijska analiza poslovanja preduzeca u hotelijerstvu i turizmu*, Univerzitet Singidunum, Beograd, 2013.
8. Stojiljkovic M. and Krstic J: *Finansiska analiza*, Ekonomski fakultet, Nis, 2000.
9. Unkovic, S. *Ekonomika turizma, Savremena administracija*, Beograd, 2001.

VERICA JANESKA*
SILVANA MOJSOVSKA**
ALEKSANDRA LOZANOSKA***

BRAIN DRAIN FROM THE REPUBLIC OF MACEDONIA - TRENDS, IMPLICATIONS, POLICIES

Abstract

This article reviews the brain drain trends from the Republic of Macedonia and its implications in the last two decades. Since 2008, the Republic of Macedonia is in a group of the ten countries with most intensive brain drain. As for the brain drain impact the following conclusions can be drawn: Direct “brain drain” effects are manifested in the reduction of the economic growth and innovation capacity of the country due to the human capital decrease; The long-term unfavorable brain drain implications on the research and development are evident, particularly in terms of the availability of scientists and engineers and quality of scientific research institutions; Feedback effects also are unfavorable because return of the highly educated emigrants is very small and occasional; Brain drain rise is not accompanied by an increase in remittances, and there isn’t significant impact on the diaspora and technology transfer; Brain drain accelerate the population and labor force ageing and the reduction of the reproductive population because of its family character and longevity. The article concludes with proposals for policy approaches towards a more systematic treatment and integrated approach of the pre-emigration measures by placing the emphasis on the

* Professor, Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: verica@ek-inst.ukim.edu.mk

** Professor, Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: s.mojsovska@ek-inst.ukim.edu.mk

*** Assistant professor/Scientific researcher, Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: sandra@ek-inst.ukim.edu.mk

retention of the tertiary educated population though educational sector policies and economic development, and post-emigration measures, particularly creation of diaspora networks.

Keywords: Republic of Macedonia, brain drain, socio-economic implications, demographic consequences, brain drain policies

JEL classification: J110, E60

Introduction

Emigration of highly skilled persons from developing to developed countries has significantly increased over the past two decades. The United Nations data shows that the international migrant stock (millions) in the World in the last decades noticed continuous increase: 154.2 (1990); 174.5 (2000); 220.7 (2010); 231.5 (2013).¹ The number of tertiary educated (highly-skilled) immigrants in the OECD countries has increased by 70% in the past decade to reach 27 million in 2010/11, and about 30% of all migrants were highly educated.² In the last decade, emigration rates of the highly-skilled exceeded total emigration rates for most of the countries of origin, reflecting the selective nature of migration by educational attainment. This was the case for 137 out of the 145 countries of origin with available data (95%).³ The highest emigration rates to OECD countries are registered for small countries and island states. Since 2000, the highest rise in emigration rates have been recorded by the European countries.

Republic of Macedonia is not excluded from these trends of emigration. In this paper, the brain drain trends in the last two decades, as well as its consequences and implications on the socio-economic and demographic development of the country are identified. This paper has the purpose to show how serious and complex is the brain drain problem in the Republic of Macedonia, which requires considerate policy approach.

¹ United Nations, (2013), *Trends in International Migrant Stock*, <http://www.un.org/en/development/desa/population/migration/data/estimates2/estimates2total.shtml> (Approached on: 5.9.2016)

² Ibidem

³ OECD, <https://data.oecd.org/>, (Approached on: 1.9.2016)

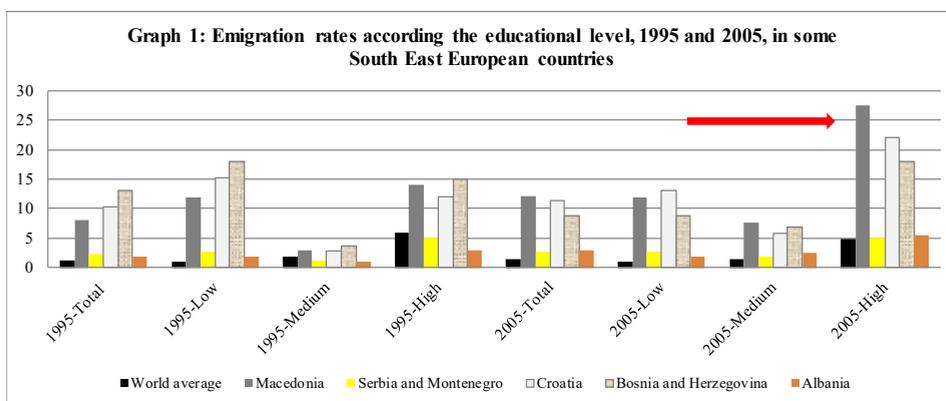
1. BRAIN DRAIN FROM THE REPUBLIC OF MACEDONIA

1.1. Brain drain changes and current situation

The intensified emigration from the Republic of Macedonia in the period after 1990 was characterized with large increase of the number of migrants with tertiary level of education. There are no relevant data about Macedonian citizens that have left the country, especially about the highly educated emigrants. Besides, no international system for recording skilled emigration exists. It draws upon several sources to construct somewhat crude, but reliable estimates of the emigration of highly educated persons from the country.

According to the estimations, at the beginning of the new millennium around 20% of the Macedonian citizens with university education were abroad.⁴ In addition, the World Bank estimations shows that in the period 1997-2005, the emigration rate of the tertiary educated persons in the Republic of Macedonia was over 29%.

Furthermore, the World Bank data shows that in the period 1995-2005, the Republic of Macedonia stands out with the highest emigration rate of the tertiary educated persons (Graph 1) among the South East European countries. Its numerical value almost doubled, which implicates significantly higher intensity of the intellectual emigration compared to the region.



Source: Docquer F., Lodigiani E., Rapoport H. and Schiff M., Emigration and Democracy, World Bank Policy Research Paper No. 5557, World Bank, Washington, DC, 2011

⁴ Janeska V., (2003), *Potential intellectual emigration from the Republic of Macedonia*, "Economic Development", Journal of the Institute of Economics – Skopje, Year 5, No. 1-2-3, p.65.

Also, as noted into the European Commission study “Social Impact of Emigration and Rural-Urban Migration in Central and Eastern Europe” for 25 countries (based on the World Bank data), the Republic of Macedonia stands out with the highest emigration rate of the tertiary educated persons in the group of the candidate countries for membership in the European Union.⁵

The intellectual emigration from the Republic of Macedonia continued with almost the same intensity after 2005. It is confirmed with the brain drain indicators of the World Economic Forum (WEF). In the period 2008-2013, on the global level, the Republic of Macedonia was in the group of the ten countries with the largest brain drain intensity. The data for 2011-2012 shows that according to the brain drain indicator Republic of Macedonia is ranked as 142 out of 142 countries (Table 1).

Table 1: Ranking of the Republic of Macedonia, according the brain drain indicator, the capacity to retain and to attract talent

Countries	Brain drain indicator	Capacity to retain talent	Capacity to attract talent
2008-2009 rank among 134 countries	126		
2009-2010 rank among 133 countries	125		
2010-2011 rank among 139 countries	126		
2011-2012 rank among 142 countries	142		
2012-2013 rank among 144 countries	135		
2013-2014 rank among 148 countries		123	134
2014-2015 rank among 144 countries		127	134
2015-2016 rank among 140 countries		129	133

Source: World Economic Forum, The Global Competitiveness Reports: 2008-2009; 2009-2010; 2010-2011; 2011-2012; 2012-2013; 2013-2014; 2014-2015; 2015-2016

⁵ European Commission & GVG, (2012), Social Impact of Emigration and Rural-Urban Migration in Central and Eastern Europe (VT/2010/001) – Synthesis Report, June 2012, p. 58.

Starting from 2013-2014, the brain drain indicator was replaced by two indicators: Capacity to Retain Talent and Capacity to Attract Talent. Regarding both indicators, the position of the Republic of Macedonia is unfavorable. In 2015-2016, according to the first indicator, Macedonia was ranked as 129 out of 140 countries, while for the second indicator as 133. These rankings imply that the country doesn't have capacity neither to retain nor to attract the talents, which contributes to intensification of the brain drain.

The estimations of the tertiary educated persons' emigration rates, according to the age at entry into the receiving country, shows that this indicator for the Republic of Macedonia in 2000 was 29.1% (for the age group of 0+), 26.9% (12+), 25.9% (18+) and 24% (22 and more)⁶. Relatively higher emigration rates of the young confirm the assumption that the significant part of the existing intellectual emigration is formed on the basis of the increased family emigration and the continuation of the education abroad. The indicator about the participation of the tertiary educated persons as a percentage of the total emigrants in the OECD countries is very significant. The value of this indicator for the Republic of Macedonia in 2011 was 8.9%⁷.

The available data from the domestic and foreign sources, although incomplete, undoubtedly confirm that the Republic of Macedonia faced very intensive emigration of the highly educated persons in the last two decades. The implications are discussed below.

1.2. Brain drain consequences and implications

The emigration, and particularly the brain drain from the Republic of Macedonia in the last two decades were influenced by various factors: High and long-term unemployment of the highly educated persons; Determinants related to the labour such as: violation of the labour, underestimation of expertise, limited opportunities for promo-

⁶ Beine, M., Docquier, F. and Rapoport, H., (2007), "Measuring international skilled migration: new estimates controlling for age of entry", World Bank Economic Review, Vol. 21, No. 2, p. 249–254

⁷ World Bank, (2016), *Migration and Remittances Factbook 2016*, Country tables, p.2

tion of the profession; Decrease of social and personal living standard; Long-term decrease (or retention at a low level) of the economic and investment activities, Low economic growth; The long-term transition process; Political instability in the country and its surrounding; Institutional and non-institutional factors (tradition, established migration networks, deteriorated system of values etc.) and Changes in the migration policies in the receiving countries.

The indicator about the “Labour market efficiency (Pillar 7)” in the Global Competitiveness report (GCR) of the WEF shows that despite the oscillations, the position of the Republic of Macedonia remains rather unfavorable. This pillar consists of several indicators, out of which the following are important for the brain drain: *Pay and productivity*, *Reliance on professional management* and *Female participation in the labour force*. According to the first indicator, the ranking of the country has significantly improved in the period 2008-2016 (Table 2). However, considering the indicator - *Reliance on professional management*, the country was continuously ranked below 100 position over the period. Also, the position of the country in terms of the *Female participation in the labour force* is unfavorable. Furthermore, since 2014-2015, within the 7th pillar in the GCR, there is a sub indicator *Efficient use of talent*⁸ which shows that Macedonia in the last two years is ranked as 110 i.e. 111. All these indicators confirms that the country does not provide enough support for the educated persons to work in satisfactory conditions.

⁸ This indicator includes: Pay and productivity, Reliance on professional management, Country capacity to retain talent, Country capacity to attract talent and Female participation in the labour force.

Table 2: Efficiency in the "use of talents" in the Republic of Macedonia

2008-2009 rank among 134 countries	2009-2010 rank among 133 countries	2010-2011 rank among 139 countries	2011-2012 rank among 142 countries	2012-2013 rank among 144 countries	2013-2014 rank among 148 countries	2014-2015 rank among 144 countries	2015-2016 rank among 140 countries
113	86	71	72	94	79	71	84
Pillar 7 - Labour market efficiency							
Pay and productivity							
79	60	51	54	75	49	18	34
Reliance on professional management							
110	113	115	126	133	110	107	102
Female participation in labour force*							
94	97	101	96	106	108	104	103

* Starting from 2011-2012 the indicator is women in labour force, ratio to men

Source: World Economic Forum, The Global Competitiveness Reports : 2008-2009; 2009-2010; 2010-2011; 2011-2012; 2012-2013; 2013-2014; 2014-2015; 2015-2016

Consequences and implications of the brain drain in the Republic of Macedonia are manifested in many domains and as the most important the following could be distinguished:

- Decrease of the average level of human capital in the country with all negative effects on the innovation indicators;
- Long-term unfavorable implications on the research and development;
- Poor feedback effects in terms of return of the highly educated persons, remittances, diaspora and technology transfer;
- Stimulus to domestic education;
- Acceleration of the population and labour force ageing process and significant reduction of the population reproductive base.

First effect of the brain drain is the decrease of the human capital, which is one of the key factors for the economic development. In the period 2003-2016, the Republic of Macedonia faced increasing intellectual emigration and relatively low or negative growth rates (with exception for the period 2006-2008 when the growth rates were above 5%).⁹ The results of the recent research about the human capital shows that in the period 2000-2012 the employment (number of employees) had the highest significance as a growth factor. The relative contribution of this factor is 35.8 percent of the average rate of economic growth, while of the human capital (education improvements) is approximately 22 percent.¹⁰

The share of the human capital, in form of higher and post-secondary education amounts up to 43.2% of the total capital value of education in the country, while this category of employees participated with 21.2% in total employment (in 2012).¹¹ The authors of the research conclude that the government should pay special attention to the higher education, as the most important form of human capital because of its positive “spillover” effects on R&D and technology diffusion.

⁹ Government of the Republic of Macedonia, Ministry of Finance, <http://www.finance.gov.mk/mk/node/401> (Retrieved on: 31.8.2016)

¹⁰ Lazarov Darko and Petreski Goce, Human Capital as a Binding Constraint to Economic Growth: The Case of Macedonia, *Croatian Economic Survey*, Vol. 18, No. 1, June 2016, p. 48

¹¹ *Ibid.*, p. 56

In the context of the brain drain consequences and implications on the economic development of the Republic of Macedonia, we should have in mind the link between innovations and emigration of the highly skilled persons. The innovation indicators from the GCR for the period 2008-2016 point out several relevant findings discussed below (Table 3).

Table 3: Innovation indicators for the Republic of Macedonia

Year	Global indicator - Innovation	Capacity for innovation	Company spending on R&D	Government procurement of advanced tech products	Quality of scientific research institutions	Availability of scientists and engineers	University - industry collaboration in R&D	PCT patent applications
2008-2009 rank among 134 countries	99	83	98	111	95	70	89	88
2009-2010 rank among 133 countries	92	86	114	106	90	81	78	61
2010-2011 rank among 139 countries	97	87	111	110	71	95	74	90
2011-2012 rank among 142 countries	105	86	109	110	86	114	92	90
2012-2013 rank among 144 countries	110	99	123	102	100	106	105	59
2013-2014 rank among 148 countries	86	94	91	81	86	92	81	72
2014-2015 rank among 144 countries	68	91	67	56	71	81	60	91
2015-2016 rank among 140 countries	58	91	62	22	59	86	60	79

Source: World Economic Forum, The Global Competitiveness Reports: 2008-2009; 2009-2010; 2010-2011; 2011-2012; 2012-2013; 2013-2014; 2014-2015; 2015-2016

As evident in the Table 3, the Republic of Macedonia in terms of the ranking by global *Innovation indicator* (12th pillar of the global competitiveness index) experienced oscillations over the period, reaching the best ranking at 58th position in 2015-2016. The improvement has been largely attributable to the notable improvement of the ranking in the sub-indicator *Government Procurement of advanced tech products*, up to the 22nd position in 2015-2016 from 111th in 2008-2009. However, it could be argued that this sub-indicator does not stand in direct correlation with brain-drain, i.e. the attention must be put on the two most important sub-indicators for brain drain – Capacity for innovation and Availability of scientists and engineers. Their ranking worsened over the analyzed period (2015-2016 compared to 2008/2009) which indicates that the brain-drain has affected the innovation potential of the country in a rather negative way.

The consequences of the highly educated persons' emigration on R&D in the country were also confirmed by the results of the research project: "Scientific diaspora from the Republic of Macedonia" which shows that, at present, Macedonia have respectable scientific diaspora which is

mostly created from the intellectual emigration and young persons who are studying abroad.¹² Out of 85 Macedonian scientists abroad, only 5 of them were doctors of sciences and 7 persons were masters of sciences or specialists at the time when they left the country. Clearly, the impact on the Macedonian human capital is considerable.

Given that the participation of the young population prevails in the intellectual emigration, it has direct and indirect effect on the intensification of the population ageing process. In the period 2008-2015, the share of the children born abroad in the total number of children born in the country amounts 17.4%.¹³ Furthermore, the return of the highly educated emigrants is very small and occasional, with frequency of remigration. In this respect, the know-how and technology transfer to Macedonia is rather limited, along with the insufficient links of the diaspora with the institutions and private sector of the country. Also, although there is no separate statistics about the remittances from this category of emigrants, the data from the National Bank of the Republic of Macedonia show that in the period of intensified intellectual emigration, the net remittances decrease, mostly owing to the share of family migration and its long-term i.e. permanent character. This implies that the positive implications of the brain-drain are minor compared to the losses for the human capital of the country.

2. BRAIN DRAIN POLICY IN THE REPUBLIC OF MACEDONIA

The problem with the brain-drain in the Republic of Macedonia has been widely recognized by the policy-makers. The major document in this field, “The Resolution of Migration Policy of the Republic of Macedonia 2015-2020”, provides an insight into the state of affairs of the migratory movements and sets out migration policy platform, including instruments for alleviation of the migration problem, as well as goals and measures for actions in this field. Prior to this one, there was first Resolution, covering period 2009-2014. The existence of such important document since 2009 could be viewed as a serious approach to the problem at the policy level, although the results from the migratory measures, in particular those

¹² Project: *Scientific Diaspora from the Republic of Macedonia* (Group of authors, Editor: Verica Janeska), Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, 2014, p. 104-129

¹³ Calculated according the data of the State Statistical Office of the Republic of Macedonia, www.stat.gov.mk (Approached on: 7.9.2016)

targeting the brain-drain migration, could not be assessed as satisfactory. There is a wide range of related strategic documents to the migration that focus on issues that serve as factors or implications from the migration. Therefore, a coordinated policy-making is strongly needed.

The strategic goals for emigration set in the Resolution are as follows:¹⁴

- Decrease of the intensity of the permanent migration, in particular with regards to the intellectual emigration, through continuous addressing of the causes of the migratory intentions. This goal also tackles brain-drain;
- Gathering relevant data for Macedonian citizens abroad and greater use of their potentials in purpose of country's development, through establishing cooperation networks with the migrants and upgrading the cooperation with the migration organisations. This goal particularly deals with migration statistics, as well as instruments for brain-gain from the migrants;
- Encouraging reverse migration flows and re-integration of the returned migrants, in purpose of larger use of their potentials for developments.

The first goal aims to prevent emigration, while the second and third are mainly focusing on post-emigration. The post-emigration measures mostly include networking with the diaspora, brain-gain from emigrated Macedonian citizens through fostering different forms of cooperation in various fields, as well as strengthening of institutional cooperation between the Republic of Macedonia and the receiving countries.

Although the post-emigration measure are very important, the undertaking of pre-emigration measures could be more effective, as it's very difficult for any state to create reverse migrant flows. In the most important pre-emigration brain-drain measures, the following should be included:¹⁵

- Cross-cutting of the policy of intellectual migration with the relevant policies: Research and development (R&D), Education, Labour market and Industrial policy;

¹⁴ Ibid, p. 46-49

¹⁵ Project: *Scientific Diaspora from the Republic of Macedonia*op., cit., p. 217

- Encouraging the cooperation among the business sector and the institutions for tertiary education;
- Programs for talent recognition and management.

Cross-cutting of the policy for intellectual emigration with the other relevant policies is of high importance. The very low finances for R&D imply limited available jobs in this field, which contributes to increase of the intellectual emigration or brain-drain. Therefore, it's necessary for the state to integrate these R&D measures into its migration policy.¹⁶

- Ensuring financial and other assets for R&D sector which will enable continuity of the research work and start of the new, propulsive projects;
- Ensuring new jobs into the R&D sector in purpose of prevention of the brain-drain from the Republic of Macedonia and, at the same time, will ensure normal functioning of this sector with regards to the staffing;
- Inclusion of the state into the international R&D programmes and ensuring necessary assets for co-financing international research projects in which Macedonian institutions participate.

In addition to the R&D policy, the educational and labour policy are also very important. The current state of affairs in the Republic of Macedonia indicates hyper-production of faculty educated staff which could not be largely absorbed by the public or private sector. There is need for finding balance between the demand and supply on the labour market, through creation of programmes for further specialisation of the unemployed. In this context, establishing a link between the educational and industrial policy is necessary, with focus on propulsive industries. The instrument of “apprenticeship” has been already used in the Republic of Macedonia, which could be assessed as positive sign for upgrading the theoretical knowledge of the students with practice. However, further co-ordinated activity is needed. Cross-cutting of these policies should ensure adjustment of the tertiary curricula to the needs of the companies, as well as increase of the flexibility level of the tertiary institutions to respond to

¹⁶ Ibidem.

the newest trends in higher education in Europe and wider. Furthermore, the strategic goal of the Republic of Macedonia for attracting FDI adds to the importance of the higher education curricula, as labour has been proclaimed as one of the main attributes of the country.

Another important aspect of the pre-emigration measures has been “talent management”, i.e. establishing programmes for recognition and nurturing of talents. These programmes should include long-term investment into the talented children and young people. However, these programmes are very expensive and require strong institutional system. Other type of talent management programmes are scholarships for undergraduate, graduate and doctoral studies of Macedonian citizens abroad, under terms for scholarship grantees to return home after completion of the studies. The Macedonian government practices such system of scholarships for 15 years, which supplies the country with skilled professionals. The major challenge is proper integration of the returnees into the public administration institutions, in purpose of maximisation of their contribution to the country. This system is less expensive than the long-term talent management, but still very effective, which adds to its applicability as a migration policy measure.

The above mentioned measures has already been included into the Resolution, suggesting that there is awareness at the policy level about the available instruments. However, the implementation of the Resolution remains to be under question, as there is need for systematic, not ad-hoc measures. Any further postponement of creation of systematic treatment to the problem of brain-drain is likely to be devastating for the human capital of the Republic of Macedonia.

Conclusion

In the last two decades, the Republic of Macedonia faced intense highly educated emigration. The analysis in this paper showed that highly skilled emigration from the Republic of Macedonia by all its attributes is brain drain. The estimations indicate that at the beginning of the new millennium around 20% of the Macedonian citizens with university education were abroad. In addition, the World Bank estimations shows that in the period 1997-2005, the emigration rate of the tertiary educated persons from

the Republic of Macedonia was more than 29%. In the period 2008-2013, the Republic of Macedonia belonged to the group of the ten countries in the world with the largest brain drain. The data for 2011-2012 shows that according to the brain drain indicator, the country was ranked as 142 out of 142 countries. Starting from 2013-2014, instead of the brain-drain indicator, two other indicators were introduced: Capacity to Retain Talent and Capacity to Attract Talent. In 2015-2016, according to the first indicator, Macedonia was ranked as 129 out of 140 countries, while for the latter as 133. These confirms the seriousness of the problem of brain-drain in the country, which has many implications.

The most notable direct “brain drain” effect include decrease of the human capital with impact on the economic growth and innovation capacity of the country. In addition, the brain drain implications on the research and development are negative, due to decrease of the potential staff in R&D institutions by emigration of talented persons, as well as very low return on the highly educated emigrants. Also, the effects of brain-drain on the remittances are not particularly high, while brain-gain and the technology transfer from the diaspora are rather limited. Furthermore, the brain drain accelerates the population and labor force ageing.

The brain-drain implications require proper policy response. The country has post and pre-emigration policy measures, identified in major strategic documents. According to the state of affairs in the Republic of Macedonia, the pre-emigration measures are more relevant in purpose of prevention/alleviation of brain-drain. The most important pre-emigration brain-drain measures are: Cross-cutting of the policy of intellectual migration with other relevant policies; Encouraging the cooperation among the business sector and the institutions for tertiary education and Programs for talent recognition and management. All these measures could bear results only if there is a systematic undertaking of measures, combined with improvement of the economy in the country and boosting job creation. In this respect, systematic policy actions in the migration field are necessary.

References:

1. Beine, M., Docquier, F. and Rapoport, H., (2007), “*Measuring international skilled migration: new estimates controlling for age of entry*”, World Bank Economic Review, Vol. 21, No. 2.

2. Docquier F., Lodigiani E., Rapoport H. and Schiff M., (2011), *Emigration and Democracy*, World Bank Policy Research Paper No. 5557, World Bank, Washington, DC.
3. European Commission & GVG, (2012), *Social Impact of Emigration and Rural-Urban Migration in Central and Eastern Europe* (VT/2010/001) – Synthesis Report, June.
4. Government of the Republic of Macedonia, Ministry of Finance, <http://www.finance.gov.mk/mk/node/401> (Retrieved on: 31.8.2016).
5. Janeska V., (2003), *Potential intellectual emigration from the Republic of Macedonia, “Economic Development”*, Journal of the Institute of Economics – Skopje, Year 5, No. 1-2-3.
6. Lazarov D. and Petreski G., (2016), *Human Capital as a Binding Constraint to Economic Growth: The Case of Macedonia*, Croatian Economic Survey, Vol. 18, No. 1, June.
7. OECD, <https://data.oecd.org/>, (Approached on: 1.9.2016).
8. Project: *Scientific Diaspora from the Republic of Macedonia* (Group of authors, Editor: Verica Janeska), (2014), Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje.
9. Resolution on Migration Policy of the Republic of Macedonia 2015-2020.
10. United Nations, (2013), *Trends in International Migrant Stock*, <http://www.un.org/en/development/desa/population/migration/data/estimates2/estimatestotal.shtml> (Approached on: 5.9.2016).
11. World Bank, (2016), *Migration and Remittances Factbook 2016*, Country tables.
12. World Economic Forum, *The Global Competitiveness Reports: 2008-2009; 2009-2010; 2010-2011; 2011-2012; 2012-2013; 2013-2014; 2014-2015; 2015-2016*.
13. http://makstat.stat.gov.mk/PXWeb/pxweb/mk/MakStat/MakStat__PazarNaTrud__AktivnosNaNaselenie/125_PazarTrud_Mk_011RabNasO_mk.px/table/tableViewLayout1/?rx-id=46ee0f64-2992-4b45-a2d9-cb4e5f7ec5ef (Approached on: 9.9.2016)

UDC 658.8:316.334.2]:303.725.3(497.7)

Original scientific paper

TATJANA PETKOVSKA MIRCHEVSKA*

MERI KARANFILOVSKA**

SOCIAL MARKETING AND ITS APPLICATION IN THE REPUBLIC OF MACEDONIA

Abstract

This paper analyses the principles, characteristics, meaning and application of social marketing in the Republic of Macedonia. For this purpose, a primary research was conducted in terms of several ground criteria elaborated by several authors in the literature, with the standpoint of Andreasen being the most popular. Following the aspects he emphasized as most relevant, the research conducted in the paper shows where weaknesses and strengths of the implementation of social marketing in the Republic of Macedonia can be defined up to now, with the opportunity to promote its future application. Considering the global importance of this concept, this paper stresses its importance for the Republic of Macedonia and gives directions for improvement, obtained through empirical research.

Key words: social marketing, social campaign, marketing mix

JEL classification: M3

* Ph.D., full professor, Institute of Economics, Skopje, Republic of Macedonia, e-mail: tatjana@ek-inst.ukim.edu.mk

** Ph.D., associate, Institute of Communication Studies, Skopje, Republic of Macedonia, e-mail: merik@vs.edu.mk

Introduction

Over the past few decades, social marketing has been applied as a tool to promote initiatives, campaigns and programmes for change of awareness and behaviour around the world. Social marketing provides the greatest contribution in different areas of social progress such as preventing/quitting smoking, global health epidemics, transport and traffic safety, drugs and alcohol abuse, etc.

The research in this paper concerns the application of social marketing in the Republic of Macedonia. Based on survey results from social programmes in the Republic of Macedonia (in governmental, non-governmental and commercial sectors), information about the current development of social marketing in the country is presented. Primary data obtained through empirical research were analysed, addressing the use and representation of the marketing features in social programmes and their evaluation according to the generally accepted and applied Andreasen criteria¹. Possible guidelines and recommendations for wider application of social marketing in the country were defined from the conducted analysis.

1. CONCEPT AND IMPORTANCE OF SOCIAL MARKETING IN THE REPUBLIC OF MACEDONIA

An increasing number of people across different countries are ready for social changes in their lifestyle, economic and social systems, their behaviour, beliefs and values. Social marketing implies achieving certain goals through knowledge, marketing techniques and technology in the organization and implementation of social programmes. It basically represents applying marketing concepts in social programmes (projects, campaigns, interventions, etc.) that bring benefit to society (public health, safety, environment and communities)². Social marketing can shape an effective framework for social programmes for behav-

¹ Andreasen, A. R. (2002). Marketing social marketing in the social change marketplace. *Journal of PublicHealth Management and Practice*, 21(1), p7.

² Kotler, P., and Nancy, R. Lee (2008).” *Social Marketing: Influencing behavior for good*”. Sage Publication, California, p.7-12

itorial change and can offer useful tools to organizations that are trying to make changes in behaviour.

The most commonly used approach to define social marketing is that of Andreasen, which describes social marketing as applying commercial marketing technologies in the analysis, planning, implementation, and evaluation of programmes designed to affect the free conduct of the target groups in order to improve individual well-being and societal welfare³. This definition illustrates four key features:

- The first is focusing on the change of free behaviour/conduct: social marketing is not connected to coercion or duress;
- The second is that social marketers are trying to initiate change by applying the principle of exchange - the notion that a clear benefit for the consumer must exist for change to take place;
- The third refers to the need of use of marketing techniques, such as consumer oriented market research, segmentation and targeting, and marketing mix.
- The ultimate goal of social marketing is to improve individual well-being and general social welfare, not just organisational welfare which distinguishes social marketing from traditional marketing.

In the Republic of Macedonia, social marketing represents a relatively new and popular issue that needs to be monitored in order to improve and increase the effectiveness of social programmes, thus benefiting society as a whole. The significance of social programmes emphasises and increases the necessity of applying global trends, more specifically, national governments should increasingly transfer the implementation of these programs to NGOs. It is also helpful that social marketing is quite developed in Western countries, thus enabling implementation of successful and investigated techniques through good practice in the country.

In order to assess the current application of social marketing in the country, the results from the conducted survey on the application of social marketing in the Republic of Macedonia are presented below.

³ Andreasen, A. 1995. *Marketing social change: Changing behavior to promote health, social development and the environment*. San Francisco: Jossey Bass, p.7

2. EMPIRICAL RESEARCH ON THE APPLICATION OF SOCIAL MARKETING IN THE REPUBLIC OF MACEDONIA

2.1. Objective and methodological approach

The research was conducted in order to obtain primary data on the use and representation of the marketing characteristics of social marketing and their evaluation according to the generally accepted and applied Andreasen criteria⁴.

Relevant data was obtained by using a questionnaire to systemise information from people that design social programmes. In addition, organizations that implement social programmes in the Republic of Macedonia (Red Cross, MCIC, UNDP, USAID, World Bank, REC and 25 local non-governmental organizations) were asked to identify programmes (campaigns) aimed at solving a social problem. The programme coordinators were identified and asked to present leading programmes addressing social problems in various fields: health, community participation, injuries, environment, poverty and the like. These efforts led to the identification of twenty-seven programmes, but it was found that four of them did not have enough documents to support further analysis or the documents were not available to the public.

The standardized questionnaire was implemented to people who devised the programmes. The questionnaire included the possibility of a free answer, and multiple choice answers that assessed the knowledge and use of social marketing, programme features and social marketing features.

Testing was conducted with several people who devised programmes before the implementation. The analysis included qualitative data that helped clarify whether the criteria were met for it to be considered as social marketing.

Knowledge of social marketing and its acceptance among the survey participants was assessed through four questions. Participants were asked whether they had heard of social marketing, had they used it previously, had any of their colleagues used it, and whether it was used in the programmes concerned by the questionnaire. In order to assess the features of the campaign, information regarding the pro-

⁴ Andreasen, A. R. (2002). Marketing social marketing in the social change marketplace. *Journal of PublicHealth Management and Practice*, 21(1), p7.

grammes was collected through questions concerning the name of the programme, country and region of its implementation, its starting date, the purpose of the programme, the target group, its objectives and intentions, theoretical information, exchange and research of the competition, the research methods used in the strategic development of marketing mix, the product (the idea and specific product), the price (incentives and disincentives), the place, the promotional elements (the message, channels and target group) and “partnerships” and the previous testing. More questions were asked regarding the monitoring (results, outcomes) and adjustment during the implementation of the programme. The final section included questions about the assessment of the result, the process and the outcome of the programme.

Questions assessing each of the six Andreasen criteria of social marketing were used to determine the extent to which current practices correspond to social marketing, namely behavioural change, target group research, segmentation, exchange, marketing mix and competition.

The survey identified 25 programmes. In 16 cases, the people who devised the programmes did not participate in the questionnaire and did not provide additional material for analysis. Therefore, the results are comprised of data from 9 programmes that had questionnaires completed about them. The findings are supplemented by secondary data collected from existing official sources in this area.

2.2. Survey results

Regarding the findings of the survey, the results are presented in Table 1 according to the research key points. To get a clearer picture of the analysis, the data from the survey are presented in percentage (%).

Thus, in terms of *knowledge and acceptance of social marketing*, only 33.3% of participants said they had heard of social marketing. The remaining 66.7% said they did not know of social marketing, although according to the definition of its techniques, they had used some them. 22.2% said they had colleagues who have used social marketing.

Types of programmes. The analysed programmes involved the field of healthcare (three programmes), environmental protection

(three programmes), community involvement (two programmes) and combating poverty (one programme).

Purpose, goals and intentions. All programmes had a clearly identified purpose. While some of them aimed at the facilitation of specific problems (e.g. Increased number of people that measure blood sugar levels, increased number of people trained for emergency or an increased number of blood donations, enabling greater citizen participation in decision making and creation of policies at the local level), more than half of the programmes (5 cases) determine rather broad categories such as “poor students who do not attend secondary school” or “daily increasing waste” as a problem to be solved.

In all the programmes, there are listed goals which at least partially focus on the behaviour of target groups. In 66.6% of cases, these goals were expressed in common terms and were not specific to each target group or segment separately (e.g. “Environmental education for students” or “sustainable waste management”). More than half of the programmes failed to explicitly define methods to measure the attainment of the goals.

The goals for change at the policy level were explicitly mentioned in three cases (33.4%). Three programmes had clearly stated intentions. Methods for measuring the fulfilment of intentions in the implementation phase were defined in one of the cases.

Target groups. Although all campaigns are focused on at least one specific target group, these target groups were defined in fairly general terms. Segmentation variables were often limited by age, geographical area or general behaviour (e.g. “Blood donor”) or role (parent, student, teacher, etc.). Other behavioural or psychographic characteristics (e.g. Health, social class or personal beliefs) in most cases were not explicitly taken into account.

In over half of the cases, the main target groups were children, students or young people.

Theory. The use of the behavioural theory was not explicitly observed in the analysed sample. Two cases, or 22.2% indicated they had used theory, including a model for attention-interest-desire-action (AIDA) and the theory of equal access.

Exchange. Over 44% of people who devised the programmes had conducted some kind of research to identify ways of encouraging

the target group to behave as predicted by the campaign (benefits) and/or ways that could hinder it from doing so (costs). Benefits were not identified in 55% of the cases (5 programmes), and costs were identified in 33.3% (3) of the cases. About 11.1% of campaigns (1) gave an explicit definition of the exchange, wherein they tried to develop an exchange that would motivate the target group to follow the intentions of the programme.

Competition. Research was conducted in 2 cases (22.2%) in order to identify the external competition for the campaign. Measures to counter the competition were also reviewed in this case.

Product. The majority of sampled programmes promoted at least one specific behaviour. Almost all programmes (89%) highlight the advantages of accepting the promoted behaviour. About 77% of the campaigns promoted improving individual social reputation as one of the main advantages. Health aspects were also promoted frequently. Finally, the main target of the campaign, which was reducing the problem itself, was promoted as a major benefit in three cases (33%) and 44% of participants stated they chose which benefit to promote based on research.

Price. About 77% of the performed effects used means of encouragement, where more than half used tangible (e.g. financial aid, rewards, meals) as well as intangible means. Disincentive measures were used less commonly, by 11% of programmes, and only in combination with the means of encouragement. The choice of measures of encouragement and/or disincentive was based on research in 3 cases (33% of the total sample, which means that in over half of the cases, the choice to use measures to encourage and/or discourage was based on research).

Place. Places where the target groups would be exposed to the offers of the programmes were explicitly defined in 89% of cases. Most campaigns (44%) chose their place strategy based on evidence. Locations where everyday life takes place (e.g. Schools, municipalities, streets, organizations, etc.) and places that had organized special events (such as sports and other cultural events) were used frequently. Educational institutions (all types of schools, including universities) were used in 44% of cases.

Promotion. In each programme the Internet (websites) was also used for promotion. The most popular include: websites (89%), billboards (22%), leaflets (44%) and posters (33%). The number of projects that aim at live interaction with the target group or direct communication is also high (89%). Use of electronic mail or social networks is listed in only 11% of cases. Less popular were the forums, blogs and chat channels that were used in only one case. Print media advertisements were used in 55% of the cases, and other “traditional” media channels like radio, TV or cinema were used in 22% of the programmes. In 33% of cases, the selection of these channels was based on research.

Previous testing. The programme material was previously tested with the target group (target group only or target group and experts) in 22% of cases.

Monitoring and assessment. The implementation phase was followed in terms of outcomes (e.g. number of distributed leaflets, training courses, debates or website visitors) in 89% of campaigns. The monitoring (behaviour) results were listed in 44% of cases. In 11% of the impacts, the need for adaptation of the campaign elements was assessed.

The efficiency of the programme was assessed in 22% of cases in terms of the awareness and involvement of the target group (e.g. number of people who are considering behavioural change). The effects of the programmes on the target group behaviour and the general well-being (within the community/society of the target group) were assessed in 33% of cases. The impact of the campaign on social norms was not assessed in any of the cases. In assessing the effectiveness of the campaign, the results were almost always positive.

Table 1. Results obtained on the use of social programmes

Research is used to:	do not know	%
Support the selection/definition of target groups	1	11.1
Support the selection/definition of realistic, specific goals	1	11.1
Use the most appropriate theory for the situation	5	55.6
Identify what can hinder the target group from pursuing the objectives of the program/campaign (obstacles, costs)	1	11.1
Identify means to motivate the target group in pursuing the objectives of the program/campaign (motivations, benefits)	1	11.1
Identify potential threats/competition for the success of the programme/campaign	1	11.1
Identify measures to combat such threats/competition	1	11.1
Identify which benefits from the recommended behaviour should be emphasised for the target groups	1	11.1
Choose from incentives and disincentives (monetary and non-monetary incentives and disincentives) which are likely to be most effective for the target groups	1	11.1
Identify the best/most appropriate locations and/or time for the given target group	1	11.1
Identify the message/messages that are likely to be most effective for the given target group	1	11.1
Identify channels for transmission of messages that are likely to be most effective for the given target group	1	11.1
Measure outcome and/or evaluate the results of the programme/campaign	1	11.1

Source: Results obtained from the survey

No	%	Primary	%	Secondary	%	Primary and secondary	%	Total	%
3	33.3	3	33.3	0	0	2	22.2	5	55.6
3	33.3	4	44.4	0	0	1	11.1	5	55.6
2	22.2	2	22.2	0	0	0	0.0	2	22.2
5	55.6	2	22.2	0	0	1	11.1	3	33.3
4	44.4	2	22.2	0	0	2	22.2	4	44.4
6	66.7	1	11.1	0	0	1	11.1	2	22.2
6	66.7	1	11.1	0	0	1	11.1	2	22.2
4	44.4	2	22.2	0	0	2	22.2	4	44.4
5	55.6	2	22.2	0	0	1	11.11	3	33.3
4	44.4	3	33.3	0	0	1	11.11	4	44.4
3	33.3	4	44.4	0	0	1	11.11	5	55.6
5	55.6	2	22.2	0	0	1	11.11	3	33.3
2	22.2	6	66.7	0	0	1	11.11	7	77.8

Conclusion

Numerous conclusions can be made based on the conducted research, with one of the more general ones concerning the incompatibility of the objectives regarding programme creation and functioning according to social marketing criteria.

Regarding the terminology used in “social marketing”, it is not properly used in the Republic of Macedonia and it has different connotations (e.g. Social media marketing, marketing of non-profit organizations, marketing for a cause, social advertising, healthcare communication, social media). This underlines the need for dissemination of knowledge of social marketing, the tools or criteria used to help people who plan the programmes and researchers in the development and assessment of programs to address social problems.

Crucial for the development of social marketing in the Republic of Macedonia are the policies that support social marketing and encourage its use. Certainly, if there is such a policy, integration of training courses on social marketing will be required, including extending the opportunities for education by organizing workshops, seminars and so on. It is worth noting that an important link in the development of social marketing in the Republic of Macedonia is the development of a database for implemented programmes and including data on the results. Such an extensive database can be used to invite major investments in new programmes or expanding the programs that have proved effective. The implementation of impartial assessments of social marketing can also contribute to more comprehensive solutions for the policies in the Republic of Macedonia in various fields.

The development of social marketing in the Republic of Macedonia requires broadening of the social marketing knowledge, tools or criteria used to help programme planners and researchers in the development and assessment of programmes designed to address social problems. This involves creating educational programmes for people who work on the creation of social programmes in the public sector, NGOs, and the commercial sector as a future major partner in solving a wide range of social problems. The necessity of terminological understanding of social marketing is emphasised, to detailed knowledge of the tools and models

used by it: introduction to the theories and models of behavioural change, introduction to the various kinds of research and methods of their use, knowledge of the theory of exchange and definition of the benefits as equal or greater than the cost for each promoted behaviour, knowledge of many methods and variables that can be used to identify different target groups, proper application and understanding of the strategies of the marketing mix, especially the various incentives and disincentives, use of digital and new social media, identification of the competition, introduction to the various methods and tools for assessment of the results, understanding of the process of planning a social marketing programme, etc.

References:

1. Andreasen, A. 1995. *Marketing social change: Changing behavior to promote health, social development and the environment*. San Francisco: Jossey Bass
2. Andreasen, A. R. (2002). Marketing social marketing in the social change marketplace. *Journal of PublicHealth Management and Practice*, 21
3. Kotler, P., and Nancy, R. Lee (2008).” *Social Marketing: Influencing behavior for good*”. Sage Publication, California
4. Kupfermann, I., Kandel, E. R., and Iversen, S. (2000). Motivational and Addictive States. In E. R. Kandel, J. H. Schwartz and T. M. Jessell (Eds.), *Principles of Neural Science* (Fourth ed., pp. 998-1013). New York: McGraw-Hill.
5. Lajunen, T., and Rasanen, M. (2004). Can social psychological models be used to promote bicycle helmet use among teenagers? A comparison of the Health Belief Model, Theory of Planned Behavior and the Locus of Control. *Journal of Safety Research*, 35(1)
6. MacFadyen, L., Hastings, G., and MacKintosh, A. M. (2001). Teenagers susceptible to tobacco marketing. *Brown University Child and Adolescent Behavior Letter*, 17(4), 3.

DIANA BOSKOVSKA*
BILJANA ANGELOVA**

APPLICATION OF THE SIMPLIFIED CUSTOMS PROCEDURE – THE CASE OF THE REPUBLIC OF MACEDONIA

Abstract

The simplified customs procedures are introduced in the Republic of Macedonia in 2005. The introduction of this type of customs procedure provide positive fiscal effects to the budget of the economy and also other effects such as: reduce the cost of mediation, advocacy and terminal costs, than the time required for completion of customs formalities enabling increased efficiency and effectiveness, the consistency and continuity in planning, import and export of products and goods, etc.

The focus of research is to determine the total fiscal effects that are achieved by the application of simplified customs procedure, with the particular attention on the fiscal effects of implementation of this custom procedure in the agriculture sector on the sample of four agriculture products.

From the data of the analysis, it can be concluded that the application of simplified procedures for import and export clearance at the border crossings, the exporters have benefited so far, that includes specific effort by the Customs Administration and inspection services to increase this type procedure for import, too. Analysis determined that the application of simplified customs procedure achieved positive fiscal impact to the budget of the Republic of Macedonia. Also, the results of the analysis show that the application of simplified customs procedures have not been applied in the manner, form and level as it is in the case of the developed countries. This can largely be attributed to the fact that this type of customs procedures applied in relatively short period of time in country.

* PhD, associate professor, Institute of Economics-Skopje, University „Ss. Cyril and Methodius”-Skopje, diana@ek-inst.ukim.edu.mk

** PhD, full-time professor, Institute of Economics-Skopje, University „Ss. Cyril and Methodius”-Skopje, angelova@ek-inst.ukim.edu.mk

Key words: simplified customs procedures, regular customs procedures, fiscal revenue, agriculture sector.

JEL classification: H25, H29, Q13

Introduction

Macedonia is an example of a small and open economy. As such, its economic growth and development is essentially determined by the level of foreign trade, especially by the export component. So, for the Republic of Macedonia, it is very important to improve competitiveness of Macedonian companies. In that direction were introduced simplified customs procedures in 2005 year. Namely, customs procedure is conducting numerous activities for certain goods described and defined by numerous documents through strict adherence to the legal regulations in order to be released for free circulation, exported or transiting through the customs area.

The simplified customs procedures are tools for relief, and also to reduce the cost of mediation, advocacy and terminal costs. Also they have significant impact on reducing the time required for completion of customs formalities enabling increased efficiency and effectiveness, but also the consistency and continuity in planning, import and export of products and goods. The adoption of the Customs Act 2005 (Official gazette no. 39/2005) and the Regulation on the implementation of the Customs Act (Official gazette no. 66/2005) began implementation of simplified customs procedures in our country in foreign trade exchange.

Application of simplified customs procedures allows customs supervision and control to raise to a higher level and to establish a higher quality of the customs procedure. Nevertheless, they have certain effects, positive and negative which are discussed below. Namely, the application of these procedures provide:¹

- import, export or transit to carry out outside of the customs terminals;
- import, export or transit to carry out outside from the working hours

¹ http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/evaluation_customs_union_en.pdf

- of customs offices, 24 hours 7 days a week, 365 days a year, regardless of holidays and weekends;
- reduction of formalities, and also reduce the role of intermediaries, i.e. of the terminals and shippers in the customs procedure;
 - avoid the high amounts of terminal fees for staying on the terminal, for weighting, and others;
 - avoid the crowds on terminals, avoiding waiting for clearance the following day if the vehicle does not come on line for clearance during the working hours of customs offices, as well as avoiding the waiting on the terminal for the weekends and holidays;
 - avoid the traffic jams on the roads and border crossings.

The use of simplified customs procedures implies multilateral effects. First, here are the direct and indirect effects on fiscal grounds. Direct fiscal revenues primarily relate to the customs. Indirect fiscal effects are a result of increased foreign trade operation of the companies through the greater competitiveness and accessibility of foreign markets, that will provide higher revenues in the budget on the basis of personal income tax and on the basis of income tax. In the paper in the focus are the direct fiscal revenues of the implementation of the simplified customs procedures in the Republic of Macedonia, with the particular review of its effect in the agriculture sector.

1. FISCAL EFFECTS ON THE BUDGET OF THE REPUBLIC OF MACEDONIA ON THE BASIS OF USING SIMPLIFIED CUSTOM PROCEDURES

This paper presents an analysis of the revenue budget of the Republic of Macedonia as a result of the application of simplified customs procedure. Firstly, it's presented the main items of revenue in the budget of the Republic of Macedonia, that are relevant to obtain valid conclusions related to the rationalization of the application of simplified customs procedures and its fiscal impact to the budget of the Republic of Macedonia.

Table 1. Budget revenues based on import and export of goods in applying simplified customs procedures for period 2009 – 2013 (in million denars)

Year	Total revenue collected from customs procedures	Collected revenues from simplified customs procedures	Participation of revenue of simplified custom procedures
2009	39.047	5.068	12, 97%
2010	41.000	7.441	18, 14 %
2011	61.724	16.666	27%
2012	64.064	19.206	30%
2013	61.883	17.946	29%

Source: Custom administration of Republic of Macedonia– own calculation from the Reports of working of Custom administration - <http://www.customs.gov.mk/DesktopDefault.aspx?tabindex=0&tabid=57>

Table 1 presents data on total revenues that are collected by the customs procedures in the period from 2009 to 2013. Namely, in 2009 the income from customs procedures amounts to 39 047 million denars, of which the simplified customs procedure proceeds amount to 12, 97%, or 5.068 million denars. In 2010 simplified customs procedure accounts to 18, 14 % of the total revenue of customs procedures. Already in 2011, the share of simplified customs procedure increases nearly double that is even 27%, in 2012 the percentage of its share has risen to 30%, but in 2013 reported a marginal fall in the share of 29%, which is certainly not neglect.

Figure 1 shows the contribution of simplified customs procedures in import and export of goods in the state, given in percentage terms.

Table 2. Participation of simplified customs procedure in imports and exports for period 2009-2013 (in %)

Year	Import	Export
2009	10, 92%	25, 44%
2010	14, 89%	33, 67%
2011	22%	36%
2012	25%	40%
2013	25, 50%	33%

Source: Custom administration of Republic of Macedonia– own calculation from the Reports of working of Custom administration for period 2009-2013.

From the given structure of revenue in the budget of the Republic of Macedonia in the period from 2009 to 2013, in Table 2, it can be concluded that the percentage of the simplified customs procedures for import of goods in the first four years was much lower than the exports of goods. Namely, in 2009 the application of simplified customs procedures for export was doubled in terms of its application in imports. In 2010, the situation is similar, but in 2011 and 2012 shows its increased application in imports. But in 2013 data represents approximation of the percentage of imports and exports of goods, which means that the application of simplified customs procedures are increasingly being applied to the import.

From the above data, calculations and analysis can come to the conclusion that in the country are made greater efforts to simplify customs procedure, in order to shorten the time of clearance and to reduce costs, which means that the simplified customs procedure in Macedonia from year to year is more and more applicable.

2. THE SIMPLIFIED CUSTOMS PROCEDURES IN THE AGRICULTURAL SECTOR IN MACEDONIA

Agriculture (including hunting, forestry and fishing) is the third largest sector after services and industry. The share of agriculture in total GDP has remained relatively stable at around 10-12%, and together with the processing industry, the percentage increases to 16-18%². Given that the Government is taking measures to encourage production by reducing customs tariffs on more products, then on the raw materials that are input in certain industries, as well as machine tools necessary for the production process. With this measure, the Government believes that will stimulate investment, production and export of finished products, they will be more competitive on the world market. It also considers that the reduction of tariff rates of seeds, seedlings, fertilizers and insecticides, will encourage the cultivation of crops and their processing. Thus reduced customs rates should have positive effects on the economy, trade and industry, which, in turn, normally contributes to increased collection of public duties on other grounds, such as VAT, personal income, contributions, income tax.

There is noticed an increased interest among companies from the agricultural sector for the use of these procedures, dominant for exports

² [http://www.mchamber.org.mk/\(S\(vgfa2qrqptlpr045c30u3w45\)\)/default.aspx?mId=73&lId=1&smId=19](http://www.mchamber.org.mk/(S(vgfa2qrqptlpr045c30u3w45))/default.aspx?mId=73&lId=1&smId=19)

on the grounds that it exceeds the biggest problem in customs representation, as regards to the time limit for implementation of customs procedures outside of the working hours of customs services. The biggest advantage for agricultural companies is that customers with these procedures are not time limited in the implementation of customs formalities, that is accessible to the client 24/7, which is essential for faster flow of goods. With simplified customs procedures, surpassed the problem with delivery deadlines that companies have, due to the inability to implement the customs procedures outside of the working hours of customs services. In order to simplify and expedite the movement of goods, many companies emphasize another change that follows, and which is expected to give further impetus in this direction. The announced introduction of the New Computerized Transit System (NCTS) which will provide direct reference to the trucks from one country to another country without customs registration (which is now being done on entry into each country), that should enable increased competitiveness and expected foreign transport companies to be come more interested in the transport of macedonian goods. With the implementation of NCTS has expected to creating opportunities to increase cooperation again with companies from Greece, Hungary, Croatia, the Czech Republic that they were very present in this region in the past.³

3. ANALYSIS OF THE FISCAL IMPLICATIONS OF THE USAGE OF THE SIMPLIFIED CUSTOMS PROCEDURES ON SOME AGRICULTURAL PRODUCTS IN MACEDONIA

Based on data from the Customs Administration can review the fiscal implications of the use of simplified customs procedures, i.e. their share in the budget of the Republic of Macedonia through the analysis of imports and exports of agricultural products between 2009 and 2013. Specifically, we will make an analysis of four agricultural products sweet peppers, watermelons and cauliflower and broccoli that are exported. For that purpose, the fiscal effects of such agriculture products are analyzed in two cases, with implementation of regular as well as of simplified customs procedure.

³ http://www.kapital.com.mk/mk/prilozi_edicii.aspx/94852/lokalnoto_carinenje_ja_zgolemuva_konkurentnosta_na_kompaniite.aspx?ild=3115

Table 3. Fiscal implications for the national budget of exports of agricultural products by applying the regular customs procedures between 2009-2013 (in 000 denars)

Year	Sweet peppers	watermelons	cauliflower and broccoli	Total amount in regular customs procedure
2009	446.754	201.641	905	21.362.227
2010	1.003.303	328.058	7.889	24.043.572
2011	1.003.733	246.739	2.133	27.212.883
2012	893.445	229.298	5.618	27.646.008
2013	1.002.426	274.521	452	29.042.378

Source: Custom administration of Republic of Macedonia - <http://www.customs.gov.mk/DesktopDefault.aspx?tabindex=0&tabid=57>

Table 4. Fiscal implications for the national budget of exports of agricultural products by applying the simplified customs procedures between 2009-2013 (in 000 denars)

Year	Sweet peppers	watermelons	cauliflower and broccoli	Total amount in simplified customs procedure
2009	372	711	347	341.860
2010	6.237	16.850	1.397	1.660.255
2011	79.631	10.099	35	992.568
2012	43.613	17.659	8	1.171.999
2013	40.049	38.972	2.282	1.287.384

Source: Custom administration of Republic of Macedonia - <http://www.customs.gov.mk/DesktopDefault.aspx?tabindex=0&tabid=57>

Analyzing data from the Customs Administration presented in Table 3 and 4, can be seen that the export of agricultural products mentioned going upwards, as when using the regular and in application of the simplified customs procedure.

According to the data in Table 3, the export of watermelons, in applying the regular customs procedure, from 2009 to 2013 is in a continuity,

ranging from 201 641 000 denars in 2009 to 274 521 000 denars in 2013. As for cauliflower and broccoli, there was a significant increase in exports of these products in 2010, when income from exports from 905 000 in 2009, increased to 7 889 000 denars in 2010. In 2011, when applying regular customs procedure, their exports again been reduced since the displayed amount of 2 133 000 denars, but again in 2012 increased to 5, 618 000 denars. A significant reduction in exports of cauliflower and broccoli is recorded in 2013, when revenues from their exports amounted to only 452 000 denars. However, major fiscal implications when applying the regular customs procedure notes on exports of sweet peppers. Namely, in 2009 revenues from exports of sweet peppers amounted to 446 754 000 denars, but the amount was doubled in 2012 (893 445 000 denars), and in 2010, 2011 and 2013 was about 1, 003, 303 or 1, 003, 733, or 1, 002. 426 000 denars, respectively.

In the Table 4 shows data on tax revenue from exports of these product applying the simplified procedures in period from 2009 to of 2013. It is evident that the smallest revenue are realized from the export of cauliflower and broccoli. Revenues from exports of these products in 2009 amounted to 347 000, which in 2010 grew even massive 1.397 000 denars. Again huge reduction occurs in 2011, when revenues amounted to only 35 000, and in 2012 further are reduced and amounted to 8 000 denars. But in 2013 revenues climb again on the satisfactory level and amounted to 2.282 000 denars. The fiscal implications for the national budget of exports of watermelons are in constant growth in applying the simplified customs procedure and they are in range from 16.850 000 in 2010, to 38.972 000 denars in 2013. The only exception is 2009 when revenues from exports of watermelons was only 711 000 denars. The fiscal revenue on the budget of the fresh peppers from the export is the largest, in both customs procedures. In 2011 revenue from exports of these products is the most favorable and is on high level of 79 631 000 denars. The next two years, 2012 and 2013, revenues decreased and amounted to 43.613 or 40. 049 000 denars, which is quite satisfactory compared to 2010 when revenues were only 6. 237 000, or in relation to 2009 when they amounted to minimum 372 000 denars.

If we consider the data for fiscal revenue on the budget of exports of the mention agriculture products in the period from 2009 to 2013, we can notice that the revenue from the application of the regular customs procedure is disproportionately higher than revenue from the application of simplified customs procedure.

Conclusion

Initial findings from the application of simplified customs procedure or so called local clearance are more than encouraging and give positive results in terms of arrival of customs goods to its contractor on terms of the time, facilitating business planning, and developing the existing system of exchange. Thus, from the perspective of participants in international trade it enables more efficient operation of companies, avoiding overload on the customs terminals, no shipping and bank guarantees, thereby the custom procedure becomes simplify, shorten and less expensive, allowing faster turnover of capital, establishing a high-quality internal control and etc. In the same time the firms perform the customs alone, without coming to the customs terminals. Customs officers coming into the company headquarters, which provide to simplify customs procedures, and in the same time it's avoiding the retention goods at the border, paying multiple fees, bank guarantees and sipping services, but on the other hand it provides 24 hours working time and the whole process takes place without major delays.

In terms of the state, the application of simplified customs procedures have positive results in terms of direct fiscal impact on the budget of the country, and they are step closer to the harmonization of legislation of the Republic of Macedonia to the EU regulations.

However, there are still some anomalies and deficiencies that need to be overcome, which primarily reflected in the conditions to be met by applicants for approvals to use the simplified customs procedure.

Furthermore, from the company point of view as the main obstacle to the introduction of simplified customs procedure is the cost accounting and keeping adequate records of the goods, shipments, the time of release of the good for the required procedure, possession of an instrument of security and so on. However, the relief which is obtained by the use of simplified customs procedures, brings more benefits than costs in the procedure for clearance of goods.

Based on the analysis in this paper can be concluded that the simplified customs procedure is in progress. Namely, its share in the budget of the Republic of Macedonia from 12, 97 % in 2009, rising to over 30% in 2012, i.e. 29% in 2013. Increasing the use of simplified customs procedure is evident to exports and imports of goods. The percentage share of simplified customs procedures for imports from 11% in 2009 increased to

25% in 2013, and in exports from 25% in 2009 increased to 33% in 2013.

Analyzing data from the Customs Administration that regard to customs procedures in agriculture sector, can be seen that the export of agricultural products mentioned going upwards, as when using the regular and in application of the simplified customs procedure. But, we can notice that the revenue from the application of the regular customs procedure is disproportionately higher than revenue from the application of simplified customs procedure.

Generally, despite the positive trend in the implementation of the simplified customs procedures, remains to be working in this area, because as a country in terms of the application of this procedure we are lagging relative to the other countries, particularly in view of the developed countries.

References:

1. Atanasovski Zivko, Javni finansii, Ekonomski fakultet, Skopje, 2004.
2. Custom Administration of Republic of Macedonia, Annual report of the custom administration in 2008, 2009, 2010, 2011.
3. Customs Administration of the Republic of Macedonia (CARM) 2009, Customs/Newsletter of the Customs Administration of the Republic of Macedonia No. 12, CARM, Skopje.
4. Customs Administration of the Republic of Macedonia (CARM) 2010b, Guidelines for simplified procedures, CARM, Skopje.
5. Customs Administration of the Republic of Macedonia (CARM) 2011b, List of licences approved in EXIM, CARM, www.customs.gov.mk.
6. Customs Administration of the Republic of Macedonia (CARM) 2012b, 'Customs administration twenty years for the future of Macedonia', CARM, Skopje.
7. Biljanovska Jovanka, Atanasovski Zivko, Carinski sistem i politika, Ohrid, 2006.
8. Biljanovska Jovanka, Megunarodna trgovija, Ohrid, 2009.
9. Chandana Karunaratne, Ashani Abayasekara, Impact of EPZs on poverty reduction and trade facilitation in Sri Lanka, working paper, ASIA-PACIFIC RESEARCH AND TRAINING NETWORK

- ON TRADE, Working Paper, NO. 134, OCTOBER 2013 (<http://www.unescap.org/sites/default/files/AWP%20No.%20134.pdf>).
10. Custom law (Official gazette of Republic of Macedonia no. 39/2005).
 11. Gordhan, Pravin (March 2007), Customs in the 21st Century, World Customs Journal, Vol. 1.
 12. Regulation on the implementation of the Customs Law (Official gazette no. 66/2005).
 13. Reforming the regulatory procedures for import and export: guide for practitioners, Small and medium enterprise department, The world bank group, June 2006.
 14. State statistical office, Publications, <http://www.stat.gov.mk>
 15. Single authorisation for CPEI Single authorization/simplified procedures Imports Transit Export Customs
 16. http://ec.europa.eu/taxation_customs/customs/procedural_aspects/general/centralised_clearance/index_en.htm
 17. The WTO and preferential trade agreements: From co-existence to coherence, World Trade Report 2011.
 18. http://www.worldcustomsjournal.org/media/wcj/-2014/1/WCJ_V8N1_Tosevska-Trpcevska.pdf
 19. http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/evaluation_customs_union_en.pdf

UDC 334.72:005.591.6]:005.73(497.7)
005.73(497.7)

Original scientific paper

VASIL POPOVSKI*
HRISTINA SERAFIMOVSKA**

ORGANIZATIONAL CULTURE IMPERATIVE FOR HIGHER INNOVATION IN ENTERPRISES IN THE REPUBLIC OF MACEDONIA

Abstract

The subject of study of this paper is the question of determining the impact that organizational culture has in enterprises in the Republic of Macedonia on achieving higher innovation. The benefits of using the established organizational culture result from orientation of the whole energy and existing enthusiasm of the collective in one or more common objectives. That is why thought out establishment of a specific type of organizational culture in enterprises can be a solid foundation for achieving high results in relation to established organizational objectives and the chosen business strategy of the enterprise. This paper treats the question of innovation and emphasizes that the results in this field in enterprises in the Republic of Macedonia are as a result of the established specific organizational culture that encourages intrapreneurship, i.e. the managers in the Republic of Macedonia are aware of the benefits and use similar attitudes, values and beliefs of employees for achieving specific organizational objectives.

Keywords: innovation, organizational culture, intrapreneurship,

JEL Classification: O, O3, O31, O310

* Ph.D. Vasil Popovski Ph.D. Institute of Economics, University Ss. Cyril and Methodius–Skopje, Republic of Macedonia Email: vasil@ek-inst.ukim.edu.mk

** M.Sc. Hristina Serafimovska M.Sc., University Goce Delchev –Stip, Republic of Macedonia, E-mail: hristina.serafimovska@ugd.edu.mk

Introduction

The strong organizational culture leads to positive business results. It encourages employees to commit to achieving organizational goals; it appears as a strong motivational factor and can certainly help the company to learn from its own experiences. These benefits arise from the fact that the related attitudes, values and beliefs of employees contribute to directing the total energy and existing enthusiasm towards one or more common objectives, which simultaneously each of them have recognized. On the other hand, this common commitment creates a special business environment that provides a sense of belonging to something recognizable and different and at the same time it motivates employees. The established values, ways of behaviour, implanted routines in a company give its own recognition and also create a tradition that lingers and thus provides consistency in the company.¹

The strong organizational culture besides from contributing to the achievement of better performance of the company in the most general sense, it can be adjusted towards achieving specific objectives. The term specific objectives actually mean a specific business strategy that the company has chosen. In this case we are talking about a strategy of innovations and characteristics of the kind of organizational culture that will enable and encourage more innovative activity among employees.

Why is it important that the set business strategy has to be favored by the organizational culture of the enterprise?

The organizational culture actually is a type of model of mutual basic assumption of a group for resolving its problems of external adaptation and internal integration, which is functional enough to be considered as valid and as such can be transferred to the new members in a form of a proper way to seeing and solving problems. The organizational culture emphasises the fact that there are things in common, views, opinions and so on, that are shared within a group, which are common, similar and equally acceptable for the members of that group and it actually makes the group specific and special. However, the culture is much more than a common stand of a number of individuals for one thing. It gives the organ-

¹ Popovski, V., (2001), "Vlijanie na organizaciskata kultura vrz delovnosta na pretprijateljata", Ekonomski institut - Skopje, p. 186.

ization a structural stability, depth, width, shape and integrity in general.² And that are the prerequisite needed by an enterprise to ensure unity and perseverance on the road to realization of the objectives or strategies.

This paper treats the question of innovation and it aims to determine whether the obtained results in this field in Macedonian enterprises are as a result of the established specific organizational culture that encourages intrapreneurship.

From a methodological point of view, the paper is mainly based on applying analytical and descriptive method, inductive-deductive method, and the statistical method for processing the collected data from the survey conducted in 31 enterprises in Republic of Macedonia.

1. CHARACTERISTICS OF ORGANIZATIONAL CULTURE THAT SUPPORTS INNOVATION

To understand how organizational culture affects the development of innovation in the enterprise, first we must start from the carrier of innovative activity in the organizational context. The question of innovation sets on the agenda the concept of intrapreneurship, i.e. the intrapreneur. Unlike the close term – entrepreneur, the role of the intrapreneur is much more complicated. More precisely, as part of the broader organizational context it is necessary to function within a defined group with already established rules, values and norms of behaviour. In such conditions the intrapreneur is directly dependent of the established organizational culture characteristic in which it works. The process of intrapreneurship can be self-fulfilling and motivating for its initiators and carriers if it's accompanied by organizational culture that supports innovation development. However, if the innovative organizational culture is absent in the work context then there is a risk that the carrier of the intrapreneurship process to become counterproductive not only for achieving the organizational goals and results, but also for their personal goals, as a result of the frustration caused by the conflict with non- supportive work environment.³

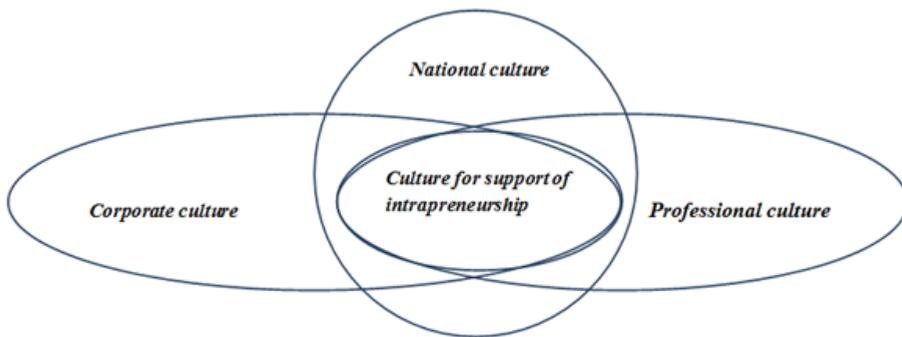
² Schein, E.H., (2004) 4-th Edition, "Organizational Culture and Leadership", John Wiley&Sons, San Francisco, p.14 – 17.

³ Fulton, J.S., Lyon, B.L., Goudreau, K.A., (2010) "*Foundations of Clinical Nurse Specialist Practice*", Springer Publishing Company, New York, p. 312.

Unlike the entrepreneurship where the entrepreneur appears in the role of a business owner i.e. self-employed, in intrapreneurship the role of the intrapreneur is much more complicated. The organizational culture that supports the development of intrapreneurship can be seen as a model of cultural relations which are shared between individuals within a group. Such model is shaped, modified and maintained through the interaction of individuals in the group i.e. the organization.⁴

When we talk about individuals we should bear in mind that each of them has its own background. Specifically, each individual is a part of a national context, has a certain professional culture and a certain degree of education and as such appears in a work community where there is a specific corporate culture. As it can be seen from Figure 1, these three types of culture (national, professional and corporate) can be considered as constituents of the organizational culture which supports intrapreneurship.

Figure 1- Intrapreneurship culture as a function of national, corporate and professional culture.



Source: Fayolle, A., Kyro, P., “The dynamics Between Entrepreneurship, environment and Education”, Edward Elgar Publishing Limited, 2008, p.80

Given that people’s behavior is somewhat programmed by the context in which the individual was born, developed, educated, where he gained his habits, work and life experience, it can be said that the national culture can be considered as a factor that impacts innovation and

⁴ Fayolle, A., Kyro, P., (2008) “*The Dynamics between Entrepreneurship, Environment and Education*”, Edward Elgar Publishing Ltd., p. 79

the development of intrapreneurship. The same applies to the professional culture acquired from previous work experience of the individual and the acquired education that combined with the national context can give different results. Apart from the impact of the national and professional context, special attention attracts corporate i.e. organizational culture.

After determining the role and place the organizational cultural has in the individual, it is necessary to determine what type of organizational culture is most suitable for development of the intrapreneurship in terms of the characteristics it should have?

Exactly to this question adds to the model of Hofstede⁵. The model is developed by Hofstede and originally served to identify the basic differences that exist between national cultures. The initial concept referred to four main dimensions, namely: distance from power, avoiding uncertainty, individualism versus collectivism and masculinity versus femininity. Thus the developed model was suitable for making studies for organizations on matters for determining the organizational culture. The convenience of the model derives from its simplicity, clarity and ability for empirical testing. This model provides a typology of dimensions of the organizational culture that is the most appropriate for encouraging innovation and development of intrapreneurship. It is a question of the following dimensions:

- **Low level of distance of power** - it means a decentralized management structure with established informal networks between employees and equally distributed authority. In such manner the supervisor can be in contact with employees from all levels and thus to get to know the problems and uncertainties faced by the employees, also in this way it would create preconditions for easier and more efficient execution of tasks.
- **Low level of avoiding uncertainty** - leads to individual awareness of the individual of risk, as well as tolerance of the failed attempts without a lot of rules and formalities in operation.
- **Medium level of individualism** – to strengthen the intrapreneurial process a combination of individual and collectivist orientation is needed. It can be achieved in a way that the leaders will mobilize

⁵ Ibid., p. 81

the individual talents for achieving and executing the collective objectives in order to make the employees feel responsible for their companies.⁶

- **Quite high level of masculine oriented organizational culture** – intrapreneurship has the need of two dimension of orientation (masculine and feminine), with emphasis on the masculine dimension. This implies a more aggressive commitment to the goals and focus on the level of achieving them, the ability to solve problems, determination and implementation of solutions. However, we cannot neglect the wider organizational context with the established working atmosphere and favourable relations between employees who need investing because of their maintenance.⁷
- **Quite a long-term orientation** – for the organizational culture that supports intrapreneurship is distinctive and suitable a long-term oriented dimension. As much as the idea is radical, the process will be longer including greater number of repetitions. Important values that need to be nurtured are discipline, perseverance, endurance and strength needed to overcome the technical and market barriers, which are always confronted with new ideas. However, the right balance between renewal and stability must be maintained, which especially is a task for the management for research and development that needs to maintain a close link between short-term and long-term research.
- **Medium level of open system of orientation** – the system shouldn't be fully opened or fully closed, but the borders of the organization should be optimally vent form the inside to outside and vice versa. Namely, to maintain the intrapreneurship a medium open system is needed for best use of the internal and external factors and sources of innovation.⁸

⁶ H.C Menzel, R.Krauss, J.M.Ulijn, M.Weggeman, (2006) “*Developing characteristics of an intrapreneurship–Supportive culture*”, Eindhoven Centre for Innovation Studies, p.19 - 23

⁷ Fayolle, A., Kyro, P., op.cit., p. 93

⁸ H.C Menzel, R.Krauss, J.M.Ulijn, M.Weggeman, op.cit., p.28 - 30

Human beings from a psychological point of view possess a certain dose of creativity in nature itself, but for this ability to be awakened, encouraged and developed it is necessary to be stimulated in an appropriate manner. Exactly in this direction is the purpose of having a special type of organizational culture, which with the characteristic that it possesses will be able to encourage innovative activities.

2. THE ORGANIZATIONAL CULTURE AS AN IMPERATIVE FOR HIGHER INNOVATION IN ENTERPRISES

Numerous facts influence the successful implementation of the established business strategy in enterprises. Among them it is important to properly manage human resources and the selection of practices that contribute towards achieving the set objectives which are the subject of other researches. In the research it is focused on the established model of organizational culture which largely depends on the implementation of the set strategy. Its influence is present in all stages of strategic management so that without well-established organizational culture it is almost impossible for the strategies to succeed.

The issue of human resources in companies in the Republic of Macedonia is a particular issue that from researches made so far there is a general conclusion that Macedonian companies have yet to work on this issue.⁹ The question, how much the Macedonian companies rely on organizational culture in achieving specific objectives such as innovation, remains open.

Basic assumptions, attitudes, values and beliefs are those who position the enterprise, the study of this paper is how much Macedonian companies use these mechanisms in terms of achieving their objectives. Organizational culture contains at that particular stereotype of judgement. For the strategy to be successfully implemented there must be consistency with the current organizational culture. Precisely that is the task of managers. The establishment of this connection takes place in stages:¹⁰

⁹ Toseva, E., (2011), “Ulogata na konfiguraciskiot pristap kon strategiskiot menadzment na covecki resursi za postignuvanje odrzliva konkurenstka prednost”, UKIM, Ekonomski institute, Skopje, p. 198.

¹⁰ Popovski, V., op. cit, p. 99 – 101.

- First of all it is necessary to perform diagnostics on the necessary compatibility. Namely, at this stage are scanned the views of employees and are determined those who support or don not support the chosen strategy.
- Thereupon follows the modification of cultural surrounding and creating an environment related to the set strategy. This stage is crucial for management that if it determines that there is incapability is on the move to establish a mechanism that will ensure proper cultural placement of the organization.

Innovation often means change, whereas change involves risk. In that sense the organizations which are determined to support innovations have to create organizational culture that will perceive risk-taking from a positive aspect. Apart from taking risk and encouraging changes, what is considered as a characteristic of innovative organizational culture is encouraging and promoting new ideas and creativity as crucial for development of new products. Contrary to this, as obstacle of innovative organizational culture is preference to short-term thinking, repugnance towards taking risk, practicing decision making from the top down and so on.¹¹

First, from the process of creating of the idea it necessary the employees to feel it like its own, i.e. to feel that they are expected to participate in its creation. Delegating ready ideas by the management that wait to be realized by employees is part of the past. Modern courses impose greater participation of human resources especially when it comes to developing the innovativeness of companies.¹²

Organizational culture is a main determiner in the processes in the organization; it can be a carrier in the progress or a setback depending on the determination of the organization. What appears as common among different companies that have distinguished themselves as innovative, whether it is an American or Chinese company, it's the established organizational culture. The main task of management is to establish an innova-

¹¹ Davila, T., Epstein, M.J., Shelton, R., (2007) "*The Creative Enterprises*" Three Volumes, Greenwood Publishing Group, p. 128

¹² Katie, J., (2013) "*The Role of Organizational culture in Innovation Management: A case of Foxconn Technology Group - China*", Grin Verlag, p. 9

tive organizational culture at every level of the company and to be sure that the innovative way of thinking is totally accepted by all employees in all departments. Innovative organizational culture also implies changes, since its installation means abandoning a previously established organizational culture that should be abandoned.

Existing research confirms that the organizational culture and the structure in the enterprises in the Republic of Macedonia in the past marked numerous observations. Namely, from the established practice in enterprises in the Republic of Macedonia it was obvious that it could not be a question of existence of any practical application of the concept of organizational culture what is able to generate intrapreneurial structure. The issues related to culture in enterprises in the Republic of Macedonia was very little developed, and where it was present there was a partial access. As for the structure prevail enterprises with conservative-traditional organizational model that is hierarchically structured and based on strict division of labour. Whereas, in the entrepreneurial type of enterprise was dominant the position of their owners, with subjectively placed relations in the enterprise and power concentrated in informal groups created by the owner.¹³

What is the current situation in companies in the Republic of Macedonia regarding the issue of organizational culture and how it is used for entrepreneurial purposes and increasing innovation we will see in the analysis of the data obtained from the field study.

3. ANALYSIS OF THE RESULTS FROM A RESEARCH OF THE SITUATION IN ENTERPRISES IN THE REPUBLIC OF MACEDONIAN REGARDING THE CURRENT ORGANIZATIONAL CULTURE

In order to determine how much enterprises in the Republic of Macedonia rely on appropriate organization culture in achieving objectives or in other words, what is the impact of established organizational culture on achieving innovation of Macedonian companies a survey was conducted

¹³ Popovski, V., op.cit., p. 123 - 125

which covered 31 enterprises from the Republic of Macedonia. The values of the variables are determined based on data from the questionnaire, i.e. questions that the participants could answer in five possible assessments (from 1 to 5) according to the Likert scale.

The indicators of organizational culture are determined generally by the defined characteristics of the organizational culture that supports intrapreneurship according to Hofstede.

These include:

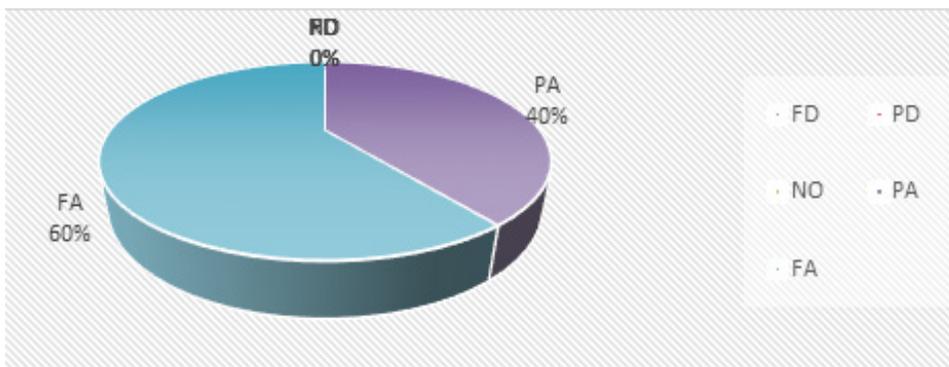
- Authorization and autonomy on the workplace
- Level of distance of power perceived through equality in the relations with superiors, cooperation, consensus, and so on.
- Adherence to the plan, rules, flexibility and way of deciding that is practiced within the enterprise.
- The degree of individualism expressed through the priority of personal goals or business goals.

On the other hand, innovation in function of sustainable competitive advantage of enterprises is determined as composite grade of 6 questions, i.e. it is defined by using the model of competitiveness proposed by Michael Porter, known as the five forces model. The questionnaire covers perception of enterprises for own competitiveness developed based on innovation perceived in terms of the industry to which they belong. This model because of the components it includes (existing competitors, suppliers, new competitors, substitutes and buyers) gives a broad image of where is the company regarding the listed factors i.e. forces that affect competitiveness. The indicators of innovation refer to:

- Growth of profitability
- The attitude towards consumers perceived through the growth of demand
- Attitude towards substitute perceived through preference of products regarding those from competitors.
- The attitude towards exiting competition perceived from taking their customers
- The attitude towards new competitors and possible integration in the industry

As far as the selection of enterprises it is important to note that these are companies which show status of innovation, recognized through their own perception on this question can be seen form Chart 1 (Meaning:FD – fully disagree, PD – partially disagree, NO – have no opinion, PA – partially agree and FA – fully agree).

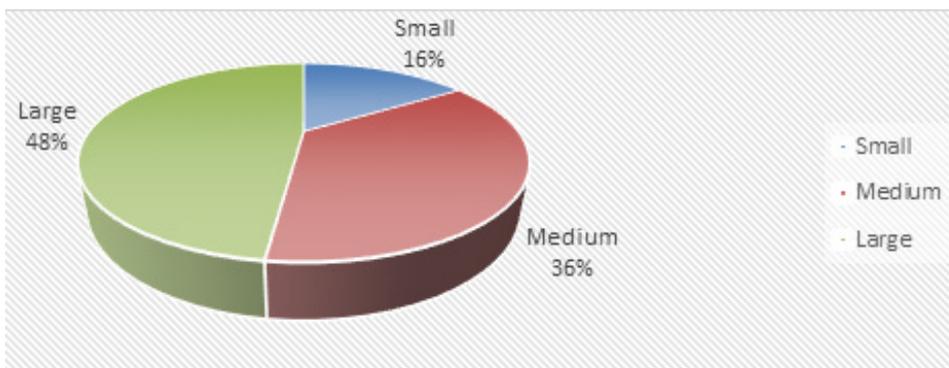
Chart 1: Perception of surveyed enterprises for their own innovation



Source: Own research

Chart 2 shows that the smallest share in the analysed sample have small enterprises (up to 50employees), while the share of large enterprises with over 250 employees is dominant. Not even one micro enterprise is included in the survey.

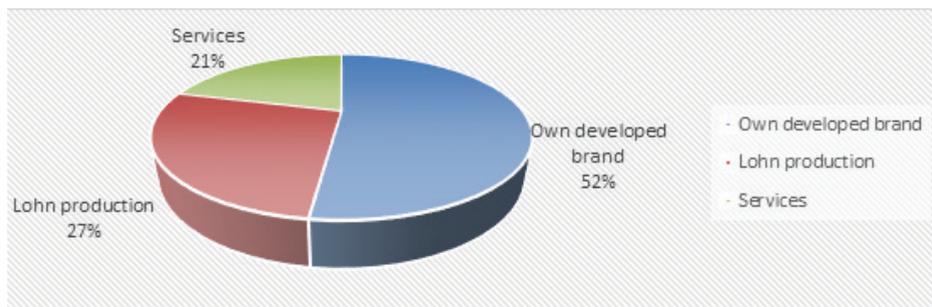
Chart 2: Size of surveyed enterprises



Source: Own research

As far as the work whose representatives are the selected enterprises, it can be seen from Chart 3 that it covers enterprises from different sectors among which the smallest share is from the service sector, and dominate are the enterprises who occupy with production, primarily those with their own developed brand.

Chart 3: Type of work of the surveyed enterprises



Source: Own research

In order to obtain the necessary knowledge there is a hypothesis which needs to show the type of established organizational culture and its connection with the results noted in the field of innovation of enterprises.

The hypothesis which set is as follows:

- **The organizational culture with features that support intra-preneurship affects innovation as a sustainable competitive advantage of enterprises in the Republic of Macedonia.**

Table 1: Results from χ^2 - test

Chi-SquareTests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	136, 773 ^a	96	, 004
Likelihood Ratio	77, 882	96	, 912
Linear-by-LinearAssociation	7, 238	1	, 007
N of Valid Cases	31		

a. 117 cells (100, 0%) have expected count less than 5.

The minimum expected count is, 03.

Chi-square value is 136, 773, and the probability of the chi-square test (p) is 0, 004 or less than the alpha level of significance of 0.5, making the particular hypothesis 3.2 accepted

It can be concluded that the organizational culture established in Macedonian companies that show innovation in their work is with features of a type of organizational culture which supports development of intrapreneurship and as such is a solid foundation for building innovation in enterprises in the Republic of Macedonia.

Conclusion

The conducted research examines the practice of enterprises in the Republic of Macedonia to create proper organizational culture, which will be towards supporting entrepreneurship and innovation within enterprises. As it can be seen from the obtained results enterprises in the Republic of Macedonia that with their commitment have innovation within its collective have embedded attitudes, values and beliefs in favour of this commitment. Testing of the hypothesis shows that there is a significant association between the development of innovation in the enterprises in the Republic of Macedonia and the established organizational culture.

It can be noted that unlike in the past there was a lack of practice the organizational culture to generate intrapreneurial structure, today The companies in the Republic of Macedonia successfully use the benefits that result from the organizational culture that goes to support on intrapreneurship.

The main settings that offer this organizational culture proved to be characteristic for enterprises in the Republic of Macedonia. Namely, innovative i.e. intrapreneurial spirit in enterprises in the Republic of Macedonia develops thanks to the established decentralized management structure in established informal networks of relationships between employees and equally distributed authority. Also it is noticeable a low level of avoiding uncertainty that is manifested through individual awareness of the individual for risk, as well as tolerance of failed attempts without many rules and formality that in this case would be experienced as unnecessary burden. As a practice of companies in companies in the Republic of Macedonia also appear the sustainable combination of individualistic and collectivist orientation. Such balanced orientation of objectives allows fulfilment of individual ambitions, objectives and needs of employees parallel with suc-

successful realization of established organizational objectives. In this way the individual and the organization mark benefits from the implemented activities. This practice enables leaders to achieve innovation as an objective, through mobilization of individual talents for achieving and enforcing the collective objectives. Also this is one of the ways through which employees identify with their companies and raise their sense of responsibility towards them.

References :

1. Popovski, V., (2001), "Vlijanje na organizaciskata kultura vrz delovnosta na pretprijateljata", Ekonomski institut – Skopje.
2. Schein, E.H., (2004) 4-th Edition, "Organizational Culture and Leadership", JohnWiley&Sons, San Francisco.
3. Fulton, J.S., Lyon, B.L., Goudreau, K.A., (2010) "Foundations of Clinical Nurse Specialist Practice", Springer Publishing Company, New York.
4. Fayolle, A., Kyro, P., (2008) "The Dynamics between Entrepreneurship, Environment and Education", Edward Elgar Publishing Ltd.
5. H.C Menzel, R.Krauss, J.M.Ulijn, M.Weggeman, (2006) "Developing characteristics of an intrapreneurship –supportive culture", Eindhoven Centre for Innovation Studies
6. Toseva, E., (2011), "Ulogata na konfiguraciskiot pristap kon strategiskiot menadzment na covecki resursi za postignuvanje odrzliva konkurenstka prednost", UKIM, Ekonomski institute, Skopje.
7. Davila, T., Epstein, M.J., Shelton, R., (2007), "The Creative Enterprises" Three Volumes, Greenwood Publishing Group
8. Katie, J., (2013) "The Role of Organizational culture in Innovation Management: A case of Foxconn Technology Group - China", Grin Verlag

UDC 334.72.012.63/.64:658.14(4-672EU)
338.124.4:336.7]:334.72.012.63/.64:658.14(4-672EU)
Original scientific paper

KLIMENTINA POPOSKA*
ELENA MIHAJLOSKA**

THE IMPLICATIONS AND AFTERMATH EFFECTS OF THE FINANCIAL CRISIS ON STARTUPS IN EU

Abstract

The 2008 Financial Crisis (FC) has been the most severe since the great depression. The interconnectedness of the financial sector has worsened the conditions enabling fast and unstoppable spillover of the negative effects across European markets. In a period of high unemployment levels, small business, especially start-ups have been recognized as one solution for reviving the economy. For that reason the paper at hand analyses the impact of the 2008 FC on start-up activity, their nature and survival rate. Special focus is placed on the financial availability in the contracting financial markets. The activity and role of alternative source of funding in the form of Business Angels (BA) and Venture Capital (VC) are particularly studied. The conclusion suggests that future research and policy actions should focus not only on increasing the level of capital available for start-ups, but also enriching and strengthening networks and linkages between all business actors.

Keywords: Financial crisis, SME start-ups, EU

JEL classification: G01, G21, 052, M13.

* Klimentina Poposka, Ph.D., Associate Professor, Institute of Economics – Skopje, University Ss Cyril and Methodius-Skopje, Republic of Macedonia. E-mail: klimenti@ek-inst.ukim.edu.mk.

** MSc, Elena Mihajloska, University of Edinburgh. E-mail:mihajloskae@gmail.com

Introduction

The 2008 financial crisis has, once more, challenged the efficiency of the market mechanisms to cope with the risks that lead to market failures, such as: asymmetric information, moral hazard and principal-agent problem. The responsibility for this catastrophic event was divided among policy makers, irresponsible borrowers, lenders, and rating agencies led by motives for personal gain. Hence, macroeconomists are constantly researching causes and initiators of crises and reestablishing fiscal and monetary policies for better risk management and avoidance of bubbles.

The interconnectedness of the financial sector initiated the spill over from the US to the EU market causing contraction of the European market and hardships for businesses, especially for small business and startups. The paper at hand aims to provide better understanding of the impact of the crisis on start-ups in the EU and aftermath effects in their operations. In addition, the paper compares start-up funding on EU level aiming to give more in-depth insight in the hurdles for financial availabilities in the very beginning of the business cycle.

The paper is structured as follows. First, we look into the post-crisis environment in EU countries with special emphasis on the start-up activity prior and after the hit of the crisis. Later, we seek to investigate survival rate of startups in the pre and post-crisis environment. The analysis in the paper covers data from the years close to the hit of the crisis aiming to better understand the immediate effect and spillover of the FC in the real sector. The end of the paper provides findings regarding financing startups in recessive economy after the hit of the crisis and proceses for reviving startups after the crisis.

1. THE POST-CRISIS ENVIRONMENT WITH FOCUS ON START-UP ACTIVITY PRIOR AND AFTER THE HIT OF THE CRISIS IN EU COUNTRIES

The domino effect struck the member countries of the Euro zone where the crisis primarily has resulted in rapid increases in unemployment, deceleration of growth, and economic contraction. Many countries, even in the European Union (EU) have sunken in negative GDPs, like Greece, Italy and Spain, while others have struggled to retain a GDP growth only above 1%. The most severe drops in GDP occurred in 2008

and 2009 which reflected the official hit of the crisis in Europe. In addition, unemployment has escalated in recent years, in Greece and Spain reaching 27% and 26% respectively. Many people who lost their jobs in the recessive economy were compelled to search for alternative employment options. The effect of the overall economic situation exerted opposing forces on entrepreneurs and SMEs, particularly startups.

From one side, the lower wages and lower cost of the capital decreased the opportunity costs for starting a business stimulating entrepreneurship. In addition, the extreme high levels of unemployment have implied entrepreneurship as the only alternative. There has been a modest decline in unemployment rates in years 2011 and 2012 in some member countries like Germany, Estonia, Latvia and Lithuania. However majority of the EU countries have only stagnated, unable to recover 2008 unemployment levels. The question emerges what has been the role of SMEs, especially startups in retaining unemployment from further intensification? Have the increased unemployment pushed more people into self-employment? Note that, in the most severely affected countries, high unemployment was persistent in the post-crisis period as well.¹

On the other side, the decreased demand, reduced disposable income, and especially the more difficult access to finance diminished the potential for high rates of start-ups in these conditions.² The overall contraction of the economy has shrunk excessively the demand which has had major effect on the number of both SMEs and startups. There has been increasing reports of insolvencies and bankruptcies posing an urgent need for transfer strategies and second chance entrepreneurs.³ Finally, finance availability especially for startups has become even more challenging which alongside with the decreased demand implies poor chances of survival of startups.⁴

¹ Eurostat database (2014). Available at: <http://ec.europa.eu/eurostat/data/database>, Accessed on 15 December 2014 and Reynolds, P., J. Storey, J. D. and Westhead, P. (1994). "Cross-national Comparisons of the Variation in New Firm Formation Rates, Regional Studies", Vol. 28:4, pp. 443-456.

² Fairlie, W., R., (2013). "Entrepreneurship, Economic Conditions, and the Great Recession", *Journal of Economics & Management Strategy*, Volume 22, pp. 207-231.

³ Calogirou et al. (2010) *Business Dynamics: Start-ups, Business Transfers and Bankruptcy*, PLANET S.A., CCIP, DTI and GFA, Published by the European Commission, DG Enterprise and Industry.

⁴ Vetter, S., Köhler, J. (2014). *Business demographics and dynamics in Europe*, Deutscher Bank Research, 2014.

Graph 1 Identified Risks for starting the business in EU-27, 2010

Source: Flash Eurobarometer 283, May cited Calogirou et al, *Business dynamics: start-ups, business transfers and bankruptcies*, European commission 2010: p.120.

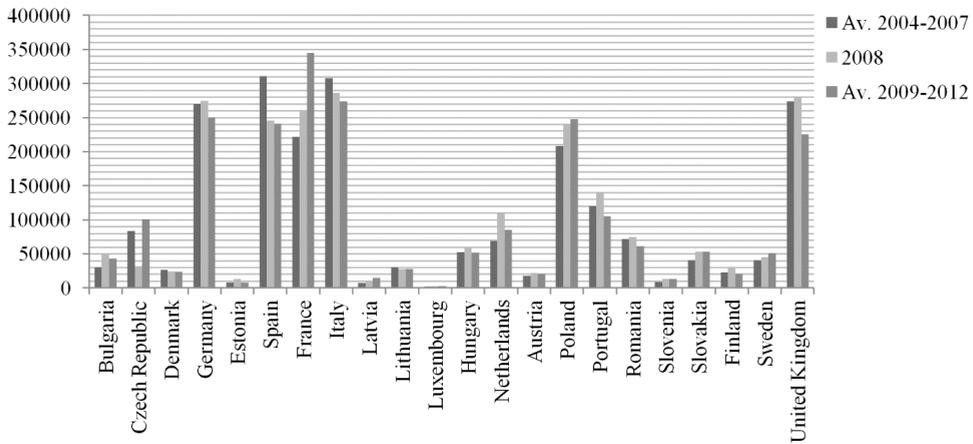
EC conducted a survey two years after the hit of the FC (Graph 1). The fears presented confirm the negative effect the crisis has exerted upon entrepreneurship perception. Although low opportunity costs and high unemployment have initiated start-up activity, the prevailing unstable environment has resulted in high risk adversity among potential entrepreneurs.

Observing the fluctuations of start-up activity during a recessive period can shed light on the effect of the FC on entrepreneurs' behavior. Given that start-ups commercialize innovative ideas and contribute significantly in the job creation, observing trends of start-up activity in terms of number of enterprises' births provides valuable information for both, policy makers and researchers.

The next graph provides information on start-up activity in the member countries and compare pre and post-crisis levels by taking the average values of 2004-2007 and 2009-2012. The year 2008 is taken as critical year when the crisis hit. Note that data from Austria, Denmark and Finland was lacking for year 2007, 2008 and 2012 respectively. In these cases, the missing value was calculated as the mean of the previous and following year.⁵ Graph 2 highlights the uneven distribution of the crisis' effects on start-up activity among the countries.

⁵ E.g. Denmark 2008 was calculated by dividing the sum of 2007 and 2009 values by 2.

Graph 2 Number of new start ups in EU-22 in the period 2004-2012



Source: Eurostat: <http://ec.europa.eu/eurostat/web/structural-business-statistics/entrepreneurship/business-demography>, Accessed on 15 September 2016.

Entrepreneurs in Germany, Hungary, Netherlands, Poland, Portugal and the UK have been most resilient at the actual hit of the crisis (2008), but most of them have experienced drops in start-up activity in the post-crisis period. Czech, France, Poland, Lithuania, Slovakia and Sweden were the only members which managed to regain pre-crisis levels of start-up or even report a positive increase in the period of 2009-2012. Overall, the situation reflects a very slow and fragile recovery. According to the EC the weak internal demand from public and private consumption is partly responsible for the slow recovery. Even established SMEs rely more on the domestic market for achieving success rather than on international sales.⁶ The latest Annual Report on SMEs identified 60% of micro and 70% of medium sized SMEs as low-export oriented firms.⁷ Member countries still struggle to retain public deficits at low level, at the same aiming for growth and competitiveness through increased domestic demand.

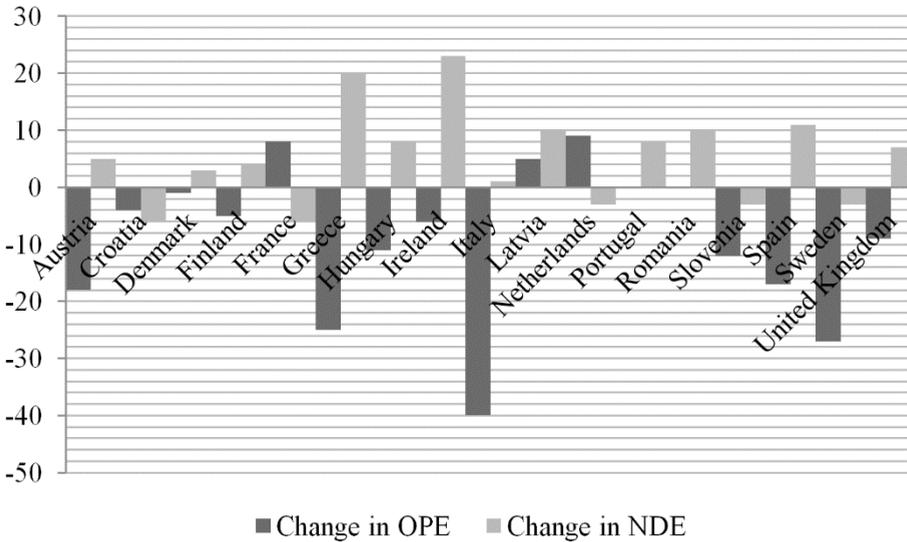
⁶ Ibid

⁷ Gagliardi, et. al. 2014. "A Partial and Fragile Recovery", Annual Report on European SMEs, European commission, 2013/2014.

Finally, we look into the types of entrepreneurs the crisis has produced and their motives for engaging with start-up activity. For that reason we analyzed the change in opportunity driven entrepreneurs (OPE) and necessity driven entrepreneurs (NDE) prior and after the crisis comparing data from 2012 and 2007.

The data from the graph implies that startups out of necessity have increased at the expense of opportunity seeking entrepreneurs, with the exception of Netherlands, France and Latvia where OPE has risen, while NDE have remained low.

Graph 3 Change in start-up motives, opportunity VS necessity, 2007-2012



Source: GEM: <http://www.gemconsortium.org/data>, Accessed on 15 September 2016

Conclusively, after the crisis entrepreneurship has been seen as more of an imperative necessity, rather than an alluring opportunity. Note that necessity driven startups lack knowledge, experience and are less likely to pursue internationalization or high-growth strategies.⁸

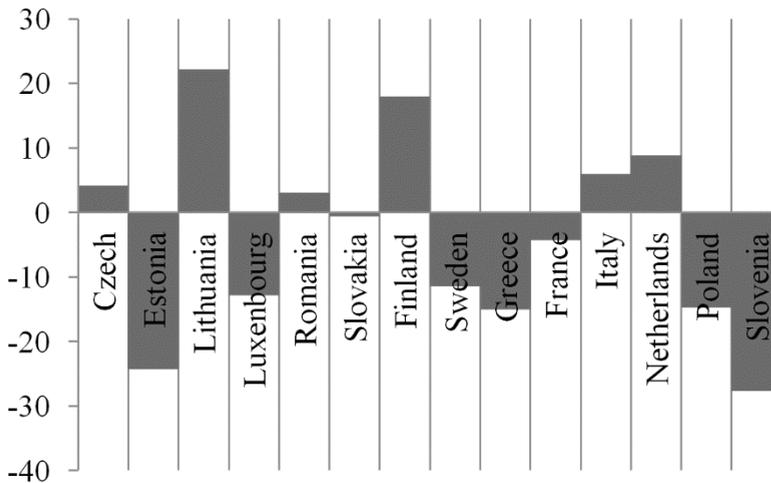
⁸ Poschke, M., (2012). “Entrepreneurs out of necessity: a snapshot”, *Applied Economics Letters*, Vol. 20, pp. 658–663

2. EXAMINING THE SURVIVAL RATE OF STARTUPS IN THE PRE AND POST-CRISIS ENVIRONMENT

The success of startups is of major importance for entrepreneurship activity for two main reasons. Primarily, startups facilitate the increase in competitiveness, innovation and economic growth. Second, more successful launches of startups send a positive message to the remaining potential entrepreneurs and increase self-efficacy. However, statistics show that most SMEs do not reach their fifth year of existence and the first year from their establishment appears as most critical for survival.⁹

Many of the listed reasons have characterized the business environment in the EU during and after the hit of the crisis. Moreover, startups founded in crisis years have 4% point higher probability of going bankrupt before the end of the 2nd year.¹⁰ Graph 4 illustrates the change in average survival rates from 2008-2010 in comparison to data from 2005-2007. Unfortunately the data was limited on these fourteen member countries.

Graph 4 Change in average survival rates from 2005-2007 and 2008-2010



Source: Marzocchi et al, SMEs demography, European commission, 2013

⁹ Marzocchi et. al (2013). Brief on SMEs demography, Manchester Institute of Innovation Research, Research MBS, the University of Manchester. UK, European commission.

¹⁰ Vanacker, T., Deloof, M. (2013) The financial and real effects of credit availability for startup firms.

The data presented in Graph 4 indicates low survival rates in Estonia, Sweden, Poland and Slovenia, regardless of their increase in start-up activity in the period of 2008-2010. Poland for instance has reported growth of 12% in startups but with decreasing survival rates of the same by 14% points. This implies that the net result of the startup activity may even have adverse effects on entrepreneurship.

3. FINANCING OPPORTUNITIES AND PROCESS OF REVIVING STARTUPS AFTER THE CRISIS

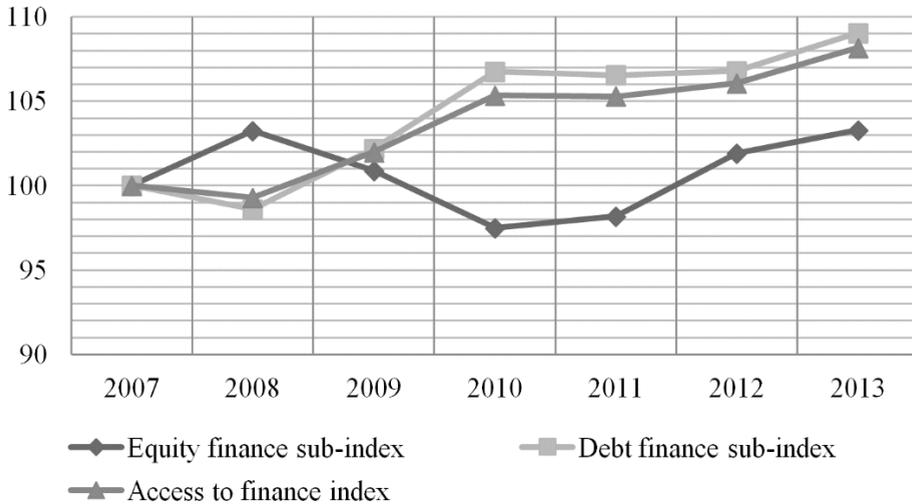
After the hit of the crisis, banks had to focus on strengthening capital bases and rebuilding profitability. Banks become more rigorous in their approaches for credit analysis applying stringent collateral requirements. Additionally, the stricter regulations on capital holdings implied by Basel III made banks highly risk adverse.¹¹ This translated into higher financing obstacles for SMEs. Rejection of loan applications together with receiving only partial funding have been major obstacles identified by SMEs. According to survey covering 25 000 SMEs across the EU, Bulgaria (36%), Ireland (27%) and Latvia (26%) had highest unsuccessful applications rates in 2010. Bulgaria also had the highest drop in success rate of loan applications from 87% in 2010 to 43% in 2007, followed by Ireland, Denmark and Lithuania. Overall, the percentage of successful loan applications dropped across the member states comparing the two years. In contrast, highest success rates had Finland, Poland and France.¹²

Another indicator of the capital availability for SMES is the index on SME Access to Finance (SMAF) developed by the EC (Graph 5).

¹¹ IFF (2013). Restoring financing and growth to Europe's SMEs, Bain & Company, Inc. and the Institute of International Finance, Indinvest (2013). Venture capital in France and Europe.

¹² European commission (2013). "A recovery on the horizon?", " Final Report, Annual report on European SMEs 2012/2013

Graph 5 Index on SMEs Access to Finance, EU-28, 2007 - 2013



Source: Adapted data from EC: http://ec.europa.eu/enterprise/policies/finance/data/enterprise-finance-index/index_en.htm#, Accessed on 15 September, 2016

The index consists of two sub indexes: access to debt finance (ADF) and access to equity finance (AEF). The year of 2007 is taken as basis for comparison since it reflects the time prior the financial turmoil. Graph 5 presents the fluctuations of SMAF together with the two sub indexes. Not surprisingly, the SMAF index hit its lowest point in 2008 at the very outbreak of the FC. The two sub-indexes have had divergent patterns. AEF index reached its peak in 2008 which emphasizes the importance equity financing during the hardest period of credit tightening. However, the index dropped significantly in 2009 before regaining strength in 2010 after which reported a constant incline. In contrast, the ADF index was stagnant from 2009 to 2011 but still at higher level in comparison to the AEF index.¹³

Finally, the hit of the crisis has not only caused tightening of financial supply but has also resulted in weak financial demand from the private sector. Namely, the contracting conditions on the market and the high rejection share of credit applications by SMEs discouraged majority of potential entrepreneurs to pursue their innovative ideas. Chances for financing start-ups with no history of payments, significant collateral or proven profitability of the business were even less optimistic. Furthermore, entrepreneurs'

¹³ Ibid.

avoided going further into debt and postponed the realization of their innovative ideas. The final outcome of the risk reluctant environment was underutilized use of resources which hinders entrepreneurial activity and economic growth.

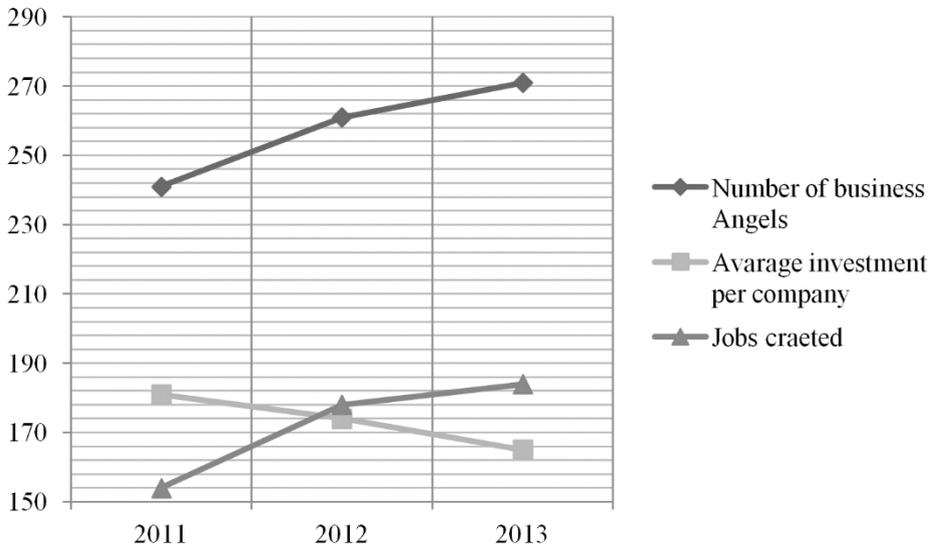
Private equity in the form of BA and VC has been identified as crucial for enabling start-ups access to finance. After the 2008 financial crisis and the tightening of credit availability their importance for start-up financing has amplified. This section provides an overview of the investments made in the early stages of financing on the VC market and BA specifically.

Although, there have been increasing efforts on EU level for directing venture capital investments into new businesses with focus on innovative start-ups, the venture capital market reported an overall decrease of 50% in investments. However, the seed and start-up stage financing held-up better than later-stage financing. Regardless, the early stage financing did not manage to regain pre-crisis level.¹⁴ The reason frequently mentioned has been higher risk aversion by investors in the post crisis environment.

The second source of equity capital we mentioned is BAs. The European Trade Association for Business Angels, Seed Funds, and other Early Stage Market Players (EBAN) provides annual data on BA activity and investment of BA within the network in the European region. According to their latest report the overall BA European Investment market increased 8.7% in 2013. BA investments dominated the early stage of financing with 73% share investing 7.5 billion Euros annually in Europe.

¹⁴ WEF (2014). *Enhancing Europe's Competitiveness Fostering Innovation-driven Entrepreneurship in Europe*, World economic Forum 2014.

Graph 6 BAs activity, EU, 2011-2013



Source: *Statistics Compendium, EBAN, 2014a: p.3.*

The graph shows that while the numbers of BAN has increased in 2013 in comparison with 2011, the average amount invested per company has decreased over the same period. IT has been recognized as financially best performing sector, while the media sector has presented to have biggest employment capacity. However, the data presented refers only to the visible part of the BA market which according to EBAN is only 10%. Note that individual BA outside the European networks also play crucial role in the startup stage and the job creation process, but data on the subject is unavailable. Individual investors often prefer to remain anonymous.

Finally, the distribution of BA investments and their effects in the real economy are not equally distributed across the member countries. UK and Germany which have reported an increase of 24% and 26% respectively in 2013, in comparison with 2012. In *Belgium*, most of SMEs, even startups are financed by bank credits. However, after the crisis there was a decrease of 26.8% in the amount of credit for startups. *Ireland* has established several funds to provide seed and startup capital for companies at their early stage of development such as “The AIB Seed Capital Fund, “The AIB Start-Up Accelerator Fund, “Bank of Ireland MedTech Accelerator Fund and “Enterprise Ireland Fund”. VC investments were concentrated in regions acting as innovation hubs. One example is Berlin in *Germany*,

where venture capital contributed to an increase of 7500 startups in 2012 in comparison to previous year. However, on the long term the volume of the venture capital in both, the early stage and expansion phase has dropped for more than 50% since 2007.¹⁵

In *France*, young innovative startups are exempted from social security taxes as an incentive for entrepreneurship. In addition France has worked towards enhancing university spin-offs from their top engineering schools. Incubators provide students and alumni access to available aid in terms of loans, connections with investors etc.¹⁶

Finally, in *Spain* and *Italy*, fewer businesses were started in 2013 than in 2008 which only confirm these economies have not recovered from the effects of the financial crisis. The Nordic region has been focused on international expansion of their startups encouraging entrepreneurship in the digital economy. The successful stories of Skype and Spotify are expected to draw a wave of investments in similar startups.

In conclusion, the EU, especially the venture market has not yet recovered from the 2008 FC. Member countries have put extensive efforts in support of the private sector with focus on start-ups, but investment amounts have stayed below pre-crisis levels.

Conclusions

The paper at hand gave an overview of the effects of the 2008 FC in the business sector with focus on start-ups. The interconnectedness of the financial crisis was highlighted as the number one reason for the fast spread of the crisis on a wide geographical spread in every field. Star-up activity, as one strategy for decreasing unemployment rates and revival of the economy after the crisis has been analyzed in more details, particularly the hurdles start-ups faced in the recessive economy.

The data presented in the paper indicated that in the addition to the lack of capital, entrepreneurs had high risk aversion which unless compelled to open a business, postponed their innovative ideas for future more stable market conditions. This decreased the start-up activity pro-

¹⁵ Ibid.

¹⁶ IFF (2013). Restoring financing and growth to Europe's SMEs, Bain & Company, Inc. and the Institute of International Finance, Indinvest (2013). Venture capital in France and Europe.

ducing more necessity driven entrepreneurs in contrast to opportunity seeking start-ups. According to Robinson and Grayson's contextual approach the decision for opening a start-up is a complex process which is under the influence of global events, especially how such phenomenon are perceived by potential entrepreneurs. For that reason future research must take into account, not only the general conditions in the environment, but also the cognition process of decision making by entrepreneurs.

The further analysis of sources of financial capital indicated that despite the tightening of the credit availability, bank credits and loans remained dominant financial source, especially in the years after the financial crisis. This indicates that despite the many benefits of alternative financing options, they have not exploited enough by entrepreneurs. The reason may be the lack of networks between start-ups and potential investors in the venture capital market. This requires further research in the area of linkages and their formation. Namely, start-ups often lack of information even in the case of existence of many support programs. Moreover, there is an increasing need for improvement of financial literacy for both entrepreneurs and investors. Both, entrepreneurs and investors should be better informed and educated about the financing and investment opportunities, respectively. Moreover, trainings for business and presentations skills can help future entrepreneurs to deliver sound business propositions in front of potential investors. This would increase their chances for alternative funding from venture capitalist, business angels and crowd-funding organizations.

Finally, the focus should not be only on fostering more start-ups, but linking them with customers, suppliers and other actors in the ecosystem which can provide resources. The aim of future research and policy actions should be in the direction of improving the general picture of business formation, empower entrepreneurs with better business skills and improve the perception of financing opportunities for BA and VC resulting in a better cooperation between all actors in the entrepreneurial environment

References:

1. Baily, M. N., Litan, R. E., & Johnson, M. S. (2008). *The origins of the financial crisis*. Initiative on Business and Public Policy at Brookings.
2. Barringer, R., B., Ireland, D., R. (2012). *Entrepreneurship*, Pearson, 4th edition.

3. Bloomberg, (2014). "Bill Clinton's drive to increase homeownership went way too far", Available at: http://www.businessweek.com/the_thread/hotproperty/archives/2008/02/clintons_drive.html, Accessed on: 05 August 2014
4. BMWI (2014). German Mittelstand: Engine of the German economy, Available at: <http://www.bmwi.de/English/Redaktion/Pdf/factbook-german-mittelstand,property=pdf,bereich=bmwi2012,sprache=en,rwb=true.pdf>, Accessed on 15 december 2014
5. Calogirou, C., Fragozidis, K., Houdard-Duval, E., Perrin-Bouillon, H. (2010) Business Dynamics: Start-ups, Business Transfers and Bankruptcy, PLANET S.A., CCIP, DTI and GFA, Published by the European Commission, DG Enterprise and Industry.
6. Cecchetti, S. G. (2008). Monetary policy and the financial crisis of 2007-2008. *CEPR Policy Insight, 21*.
7. Crotty, J. (2009). Structural causes of the global financial crisis: a critical assessment of the 'new financial architecture'. *Cambridge Journal of Economics, 33*(4), 563-580.
8. EBAN, (2014a). Statistics Compendium, EBAN.
9. EBAN (2014b). "Early Stage Investing Explained", Available at: <http://www.eban.org/about-angel-investment/early-stage-investing-explained/>, Accessed on 20 December 2014.
10. EBAN (2012). European Angel Investment Overview, EBAN.
11. European commission (2013). "A RECOVERY ON THE HORIZON?", Final Report, ANNUAL REPORT ON EUROPEAN SMEs 2012/2013, Gagliardi, D., Muller P., Glossop E., Caliendo, C., Fritsch M., Brtkova G., Bohn U., N., Klitou D., Avigdor G., Marzocchi C., Ramlogan R.,
12. European Commission Report (2010-2014). Statistical annex of European economy [online]. Directorate general ECFIN economic and financial affairs. Available from: http://ec.europa.eu/economy_finance/publications/european_economy/2010/pdf/statistical_annex_spring2010_en.pdf, Accessed 5 August 2014.
13. Eurostat database (2014). Available at: <http://ec.europa.eu/eurostat/data/database>, Accessed on 15 December 2014

14. EVCA (2014). “European Private Equity Activity Data 2007-2013”, Available at: <http://www.evca.eu/research/activity-data/annual-activity-statistics/>, Accessed on 22 December 2014.
15. Fairlie, W., R., (2013). “Entrepreneurship, Economic Conditions, and the Great Recession”, *Journal of Economics & Management Strategy*, Volume 22, pp. 207–231.
16. Gagliardi, D., Muller, P., Caliendo, C., Bohn, N., Klitou, D. 2014. “A Partial and Fragile Recovery”, Annual Report on European SMEs, European commission, 2013/2014.
17. IFF (2013). Restoring financing and growth to Europe’s SMEs, Bain & Company, Inc. and the Institute of International Finance, 2013
18. Indinvest (2013). VENTURE CAPITAL IN FRANCE AND EUROPE, Available at:
19. http://www.idinvest.com/Etude-sur-le-capital-risque-en-France-et-en-Europe-publications_12.pdf, Accessed on 20 December
20. Icrisis of 2008. *Journal of Financial economics*, 97(3), 319-338.
21. Marzocchi, C., Ramlogan, R., Gagliardi., D. (2013). Brief on SMEs demography, Manchester Institute of Innovation Research, Research MBS, the University of Manchester. UK, European commission.
22. Mian, A., Sufi, A. (2008). *The consequences of mortgage credit expansion: Evidence from the 2007 mortgage default crisis* (No. w13936). National Bureau of Economic Research.
23. Poschke, M., (2012). “Entrepreneurs out of necessity: a snapshot”, *Applied Economics Letters*, Vol. 20, pp. 658–663
24. Reynolds, P., J. Storey, J. D. and Westhead, P. (1994). “Cross-national Comparisons of the Variation in New Firm Formation Rates, Regional Studies”, Vol. 28:4, pp. 443-456
25. Shuklev, B. (2006). Management of small business, Faculty of Economics, Skopje, 4th edition.
26. Suetin, A. (2009). Causes of the current financial crisis. *Problems of Economic Transition*, 52(3),
27. Taylor, J., B., (2009). *The financial crisis and the policy responses: An empirical analysis of what went wrong* (No. w14631). National Bureau of Economic Research.

28. Vanacker, T., Deloof, M. () The financial and real effects of credit availability for startup firms: Evidence from the recent financial crisis, Available at: http://www.efmaefm.org/0EFMAMEETINGS/EFMA%20ANNUAL%20MEETINGS/2014-Rome/papers/EFMA2014_0231_fullpaper.pdf, Accessed on 20 December 2014.
29. Vetter, S., Köhler, J. (2014). Business demographics and dynamics in Europe, Deutsch Bank Research, 2014.
30. WEF (2014). Enhancing Europe's Competitiveness Fostering Innovation-driven Entrepreneurship in Europe, World economic Forum 2014.

VASIL POPOVSKI*
SLOBODAN LEVKOVSKI**
LJUBISHA NIKOLOVSKI***

**SELF EMPLOYMENT PROGRAM VIA CREDITING AS
AN INCENTIVE FOR INCREASING ENTREPRENEURIAL
ACTIVITY IN REPUBLIC OF MACEDONIA**

Abstract

In recent years, entrepreneurial activity has been the focus of the governments of the world's advanced economies. Policy makers increasingly recognize the importance of the presence of entrepreneurs in economies that open new markets, innovate products, services, technologies and organizational processes, thereby spreading consumer choice, deepen consumer possibilities and improve their well being. Therefore, there are numerous activities undertaken by the governments for stimulating new and potential entrepreneurs to enter the markets and take advantage of their entrepreneurial capabilities.

Self employment program via crediting is one of the activities undertaken by the government of the Republic of Macedonia which would facilitate market entry for the new entrepreneurs in the economy. The purpose of this paper is to present the research which was conducted on users of the self employment program via crediting and also to prove the effectiveness of this program in the creation of new entrepreneurial capital, which is the

* PhD, "Ss. Cyril and Methodius University" in Skopje, Institute of Economics –Skopje, Republic of Macedonia, e-mail: popovski@ek-inst.ukim.edu.mk

** MSc, TDA TREJD, 1000, Skopje, Republic of Macedonia, e-mail: bobilevkovski@gmail.com

*** PhD, st."Korushka" 24, 1000, Skopje, Republic of Macedonia, e-mail: nikolovski.ljubisa@gmail.com

paper hypothesis. The survey results confirm the hypothesis and suggest that self employment program via crediting is an incentive for potential entrepreneurs to enter Republic of Macedonia's markets.

Key words: self-employment program via crediting, entrepreneurship, business venture, innovation, entrepreneurial capital

JEL Classification: L 26, O, O3.

Introduction

Entrepreneurship enters the domain of the most actual fields of economy, business and social life because entrepreneurs through their creativity, innovation, imagination, fantasies, aspirations and willingness to enter into risky ventures, are changing the world we live in. Worldwide, the entrepreneurs are everyday starting a new enterprise. By exploiting their knowledge, talents and skills, entrepreneurs are trying to make profit, to achieve their vision and mission or to change the society they live in. Therefore, entrepreneurship is associated with small and medium sized enterprises, which represent a way of articulating ideas, vision and mission of the entrepreneurs.

There are numerous examples of entrepreneurs worldwide, who have influenced social life with their innovations, in a way of expanding people's choice and their opportunities. A major challenge in modern capitalistic societies is the creation of conditions for easier articulation of the ideas and aspirations of potential entrepreneurs. Difficult access to the markets for new entrepreneurs who wants to run their innovative ventures is caused by the lack of resources and by the fact that markets are well developed and occupied by the competitors. Therefore, the focus of the governments is to create appropriate policies which would ease market entry of new entrepreneurs, and thus will increase entrepreneurial capital in the economy.

There are many potential entrepreneurs in the Republic of Macedonia who have knowledge, skills and ideas, but they cannot find a way to put them in the markets because they face limited resources, needed for starting a new business venture. It is very important to support those

entrepreneurs because with each lost idea, the economy is losing entrepreneurial capital which is important for increasing the value of the economy.

Self employment programs are one of the measures implemented by the Government of the Republic of Macedonia as a part of the plan to reduce unemployment in the country, but also to give incentive for new entrepreneurs to enter markets through forming small enterprise. It is important to note that there are two self employment programs - self employment program via receiving grant and self employment via crediting. This paper will analyze the influence of self employment program via crediting on new entrepreneurs to form small enterprises and enter in markets and the extent of entrepreneurial capital they form with their presence. Not all small enterprises are entrepreneurial-minded and hence the need to measure the influence of the program on the creation of entrepreneurial capital.

1. ENTREPRENEURSHIP AND SMALL AND MEDIUM SIZED ENTERPRISES

The term entrepreneurship is becoming more popular in modern societies. Entrepreneur originates from the French word “ENTREPRENEUR”, meaning something to be done or be undertaken. Therefore, entrepreneurs are defined as people who create innovative ventures with a dose of risk and uncertainty in order to make profit by exploiting perceived opportunities and efficient utilization of resources required. Thus, they create additional value in the societies.

The concept of entrepreneurship is known since the twelfth century, but its academic learning begins in the eighteenth century with french economist Richard Cantillon. In his essay “Essay on the nature of trade in general” published in 1755, the term entrepreneurship was mentioned for the first time. Cantillon sees entrepreneurs as risk takers through the purchase of goods at a predetermined price and then selling them at a price that is uncertain.

Another significant author is Frenchman Nicolas Baudeau who inherited the position of Cantillon that taking risk is primary feature of entrepreneur and that he must be an innovator to reduce the levels of risk. His idea refers to the entrepreneur who finds and uses new technologies in order to cut operating costs and make more profit.

Furthermore, the European theorist Jean-Baptist Say describes entrepreneurs as people who possess scientific knowledge which they link

with consumer needs, taking into account the cost of production. English theorist's like Adam Smith, David Ricardo and John Stuart Mill see entrepreneurs as capitalists whose main objective is to maximize profit.

Joseph Alois Schumpeter is an American theorist despite his Austrian origin. He is considered to be the greatest theorist of entrepreneurial thought in the twentieth century. His entrepreneur is an innovator who brings change through implementing new technological processes and products. Entrepreneur is a dynamic force that undermines economic "status quo" by taking innovative actions as implementing new products or services that require new raw materials, which can get operative by using new organization methods. Schumpeter is the first theorist who made a distinction between entrepreneur, manager and business owner.

While American theorists base their concepts on the Schumpeter theory, prominent university professors like Kirzner sees the entrepreneur as a creative person who has to imagine the opportunities. Uncertain and asymmetric information create opportunities for some individuals to imagine possibilities for profit. He considered that only entrepreneurs are capable of recognizing the opportunities quickly and adequately and to react appropriately to them.

All these aspects of economic theories from various schools defined the concept of entrepreneurship. These definitions can set the framework and assess whether participants in the self employment program via crediting possess part of the listed characteristics of entrepreneurs.

Because entrepreneurs are related to small and medium sized enterprises, this section provides a brief overview of the situation of SME's in Republic of Macedonia

Defining small business in the Republic of Macedonia started in transitional years with implementing the "Law of accounting" in 1993, which differed only small and large companies through one characteristic – number of employees in an enterprise. Thus, enterprises employing up to 250 persons were classified as small, and those with over 250 persons were classified as large enterprises. This definition remained until 2004 when the "Law of business ventures" was adopted. The law accepted European criteria for definition of enterprises by number of employees, annual turnover and value of operating asset.

In 2015, in Republic of Macedonia were registered 70.139 enterprises, of which 63.590 were micro enterprises, 4.979 were small ventures, 1.339 were medium sized, and 231 were large companies. Almost

99.7% of the Macedonian economy consist small and medium sized businesses. This figures show the importance of small and medium sized enterprises for the creation of value in the economy and opening new job opportunities.

Small and medium sized enterprises represent a pillar of the economy because of their ability to innovate, to increase market competition and expand product range, and thus, producing economic growth. They represent a form of expression of entrepreneurs. Therefore there must be incentives and proper policies for supporting small and medium sized enterprises.

2. SELF-EMPLOYMENT PROGRAM VIA CREDITING

Self employment program via crediting is project of the government of the Republic of Macedonia whose implementation started in 2008. The purpose of this project is to enable favorable loans to interested unemployed persons who wish to legalize their informal business or to start their own business, which will create new jobs through self employment. Participants in the program receive 3.000 euros for each new created job position. The program determinates funding projects up to 15.000 euros and 5 new job positions. In 2014, the program has changed in order to provide better conditions for young people up to 29 years. Thus, for one newly opened job position the loan is up to 7.000 euros, and for each additional job position the loan is up to 4.000 euros (maximum financing 5 job positions). This means that program could fund projects up to 23.000 euros.

As terms specified for credit approval are:

- Repayment of the loan to be in 3 years time period;
- Annual interest rate of 1%;
- Grace period of 1 year;
- Owners assets of at least 25% of the total project value (in the form of equipment, items or money)
- User must provide a guarantee of return on assets in ratio 1:1 via mortgage, with approved credit or warranty with at least one guarantor
- Additional 1.000 euros for employment of persons declared redundant, unemployed on the basis of bankruptcy and liquidation or persons unemployed more than 3 years.

In order to achieve program objectives and measures, the project contains dozen activities. The program starts when the Employment Agency of the Republic of Macedonia publishes public announcement, calling target groups to apply and participate in the program. Users apply to the program and the application includes sample application for granting the loan and mini business plan, which must be filled and submitted by each applicant to over 30 employment centers in the country. In order to move to the next phase, applicants must meet certain criteria. One loan application means establishing one start-up business. Once the participants undergo to the process of registration of the business, they will be deleted from the records of unemployed persons in the Employment Agency. If the participant shut down his business, he cannot be registered as unemployed until he fully repay the loan.

The selection of candidates is carried out in several phases according to predetermined criteria by Project Steering Committee. In the first phase, the applications are reviewed, evaluated and distributed through developed software in terms of target groups selecting. Secondly, Commission of the Employment agency assesses actual situation regarding the completed mini business plan. If the assessment is positive, the Agency of promotion of entrepreneurship of the Republic of Macedonia evaluates and ranks the business according to its preferences which are consisted in the mini business plan. The Central Committee summarizes evaluation of the business ideas and is consisted of nine members, who submit them to the board for final approval. The Managing Board is composed of five members and makes the final decision for business that will be financially supported.

3. METHODOLOGY OF RESEARCH

In order to determine the importance of self employment program via crediting for entrepreneurship development in the Republic of Macedonia, a research was conducted on users of funds from the self employment program via crediting in 2008 in the region of the city of Skopje. Applicant's group from 2008 is particularly interesting to be analyzed because of elapsed time of minimum 5 years of granting loan. The results were obtained between the period of 2013-2016, thus there is enough elapsed time to recognize the effects of the program and the creation of entrepreneurial capital of each applicant of the program. The research was

completed by conducting a questionnaire consisting of 24 questions and is structured in two parts:

- Questions related to self employment program via crediting
- Questions related to entrepreneurial activity

In order to complete the research, contact details of 90 applicants in the self employment program via crediting from 2008 were obtained from the Employment Agency of Republic of Macedonia. Of these 90 contacted applicants, 47 weren't available for interview and 5 applicants denied to answer the questionnaire. Thus a number of 38 applicants gave their response to the questionnaire. The survey was conducted through telephone calls and interview with applicants of the program. Most of the respondents were man or 73.7%, while 26.3% were woman. The majority of respondents (71%) were with secondary vocational education and 73% were aged 40-60, while 21% were aged 20-40. The selected group consisted of members of different ethnic groups, but most of the participants were Macedonians 86%, while 10% were Albanians.

4. ANALYSIS OF SURVEY RESULTS

Results from the questionnaire confirm that self employment program via crediting is a significant incentive in the creation of new entrepreneurial capital. Presentation of questions that were crucial to form the conclusions which confirm the influence of self-employment program via crediting for enhancing entrepreneurial activity in the Republic of Macedonia will follow in the text bellow. Before the presentation, general information about realization and success of the program will follow.

During 2008, 2009, 2010 and 2011, 8.129 applications were filed for employment of 9.599 persons, out of which 5.217 applications for employment of 6.177 persons were approved. There were 4.716 contracts for employment of 5.514 persons which were signed and sent to the banks. In this period for 3.653 applicants was approved a credit for employment of 4.257 persons. The average of 1.16 persons were employed in the newly formed enterprises or every 6th enterprise consisted of 2 employees who were partners in the enterprise.

Of the total of 3.653 credit approvals from the program in the Republic of Macedonia, 3.573 applicants have registered activity in the following fields:

- 45% - agriculture, forestry and fisheries
- 20% - wholesale and retail
- 11% - industry of processing
- 8% - accomodation and food services
- 6% - transport and storage
- 3% - construction
- 1% - financial and insurance activities

Out of total 3.573 newly formed enterprises, still active are 3.216 (90%), while 357 (10%) are inactive because of liquidation or bankruptcy.

In 2012, a total of 850 persons applied in the program for employment of 970 persons, and 179 applicants received credit approval and signed contract for employment of 225 persons.

In 2013, a total of 1.062 persons applied in the program, and 455 applicants received credit approval and signed contract for employment of 455 persons.

In 2014, a total of 1.936 persons submitted applications in the program of which 597 were young people up to 29 years. Approved applications for credit recieval were 917 for employment of 929 persons of which 284 were young people up to 29 years.

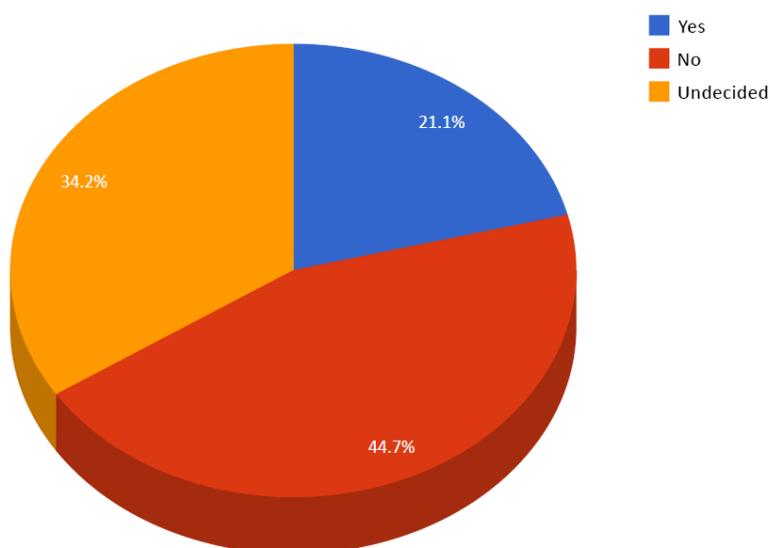
In 2015, a total of 1.723 persons submitted applications in the program of which 723 were young people up to 29 years. Approved applications for credit recieval were 1.058 for employment of 1.192 persons of which 555 were young people up to 29 years

Obtained results suggest that with the changes in the program in 2014, the number of applications for credit approval drastically increased (82% more than 2013). This increase is due to the increased number of young applicants up to 29 years because of the new measuers for this target group. Also, there is an increase in 2015 for 95% more young applicants up to 29 years than 2014. Thus, opportunities of young pepole who have new ideas, creativity and desire for success is increased for starting new entrepreneurial business ventures.

Regarding the question: Would you have started a small business venture without participating in self-employment program via crediting?, 44.7% of respondents said that they wouldn't have formed a start-up, 34.2% answered "I don't know" and 21.1% would've started a small business anyway. The large proportion of respondents who answered positively on this question indicates that the program is incentive for potential

entrepreneurs and unemployed persons to form small business enterprise. Respondents who were indecisive on this question cannot assess whether they would form a business without participating in this program, but also they didn't dispute the incentive which the program gave to them in forming their enterprise. As addition to this question, 84.2% of the respondents answered that the program completely or partly influenced to their decision on forming small business venture.

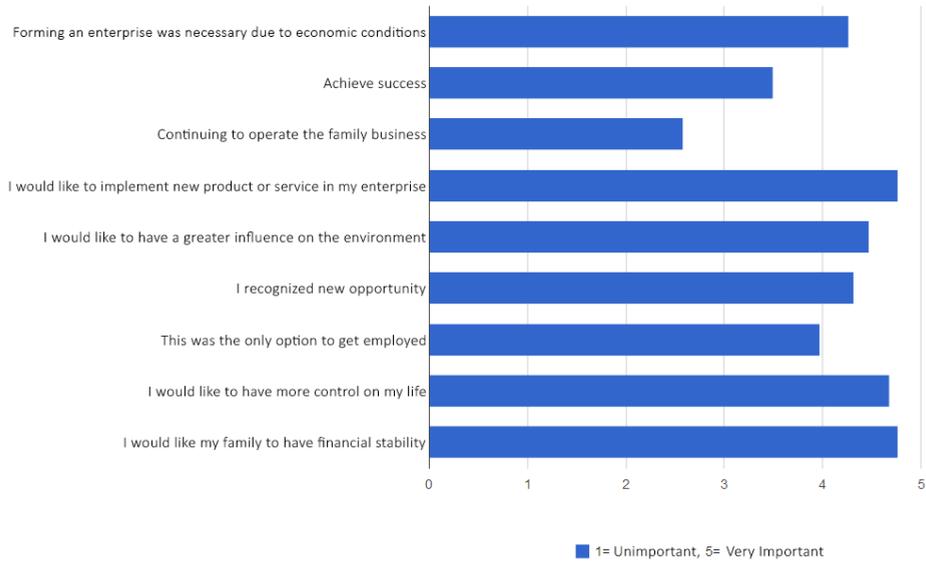
Chart 1: Would you have started a small business venture without participating in self-employment program via crediting?



Source: Authors research

Regarding the question: Which of below mentioned reasons were important for establishing the enterprise?, there were nine reasons listed for starting small business venture and for each reason the respondents gave a score from 1 to 5, where 1 is the smallest grade and 5 is the highest grade. Top rated reasons for establishing new business ventures were providing material security for the family and excitement to develop new idea for a product or service, with average score of 4.76. These results indicate the existence of entrepreneurial aspirations and reasons to form an enterprise, as, despite meeting of the needs of the family, a reason for market entry of applicants is utilization of skills and knowledge in order to make profit. Least favored reason is continuing family tradition with average grade of 2.57.

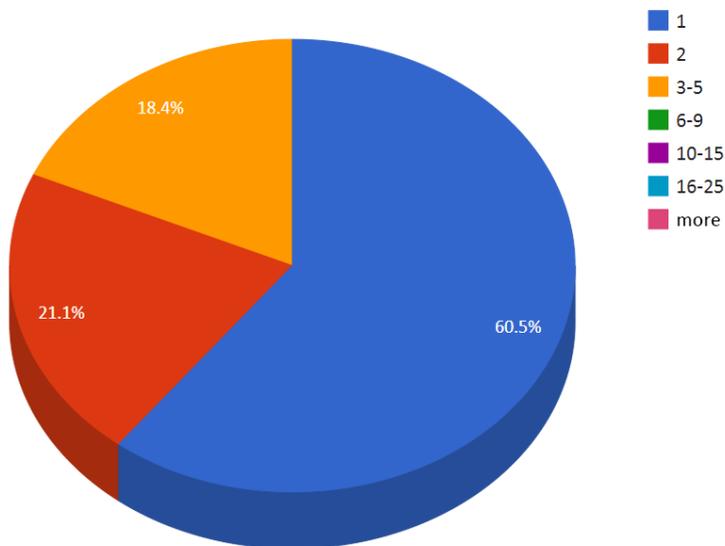
Chart 2: Which of below mentioned reasons were important for establishing the enterprise?



Source: Authors research

Regarding the question: How many employees are currently working in your enterprise?, 60.5% of the respondents have a total number of 1 employed staff in their enterprise, or they are self-employed and didn't made new employments. Those who employed extra worker, or the percentage of enterprises which have two employees is 21.1% and 18.4% of the enterprises have 3-5 employees. None of the respondents answered that they employed more than 5 workers in their enterprise.

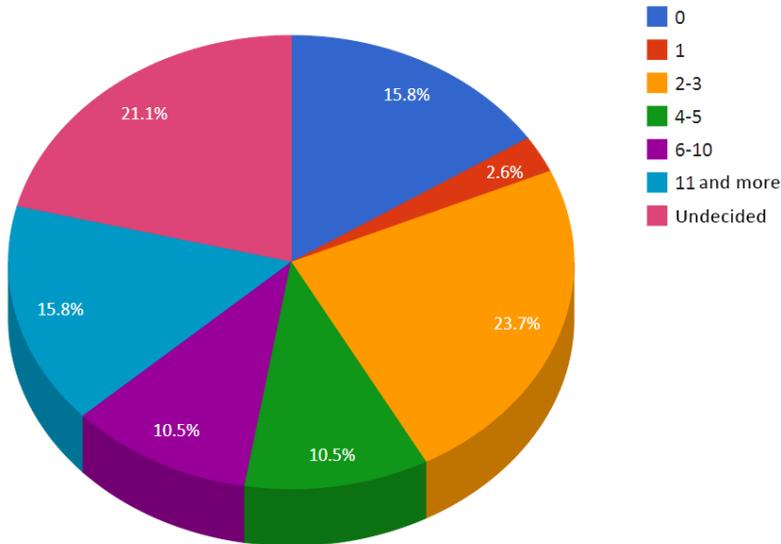
Chart 3: How many employees are currently working in your enterprise??



Source: Authors research

Regarding the question: How many new products or services have you implemented in your enterprise since its foundation?, there is no answer that prevails. The highest percentage of responses given is 23.7% and applies to entrepreneurs who have implemented 2-3 new products or services which are their innovation. Results indicate innovation of respondents as only 15.8% said that they have not introduced a product or service in the enterprise they formed. This percent is equal to the result of 15.8% of respondents who said that they have launched 11 new products or services in their enterprises. The percentage of those who do not know how many products or services they launched in their business is 21.1%, but is important to note that these are people who have launched new products or services but can't determine their exact number. Therefore, we can draw a conclusion that users of funds of this program do not have only skills and knowledge to operate their enterprise, but are sufficiently creative to produce their own ideas, which they launch in the market in form of new products or services.

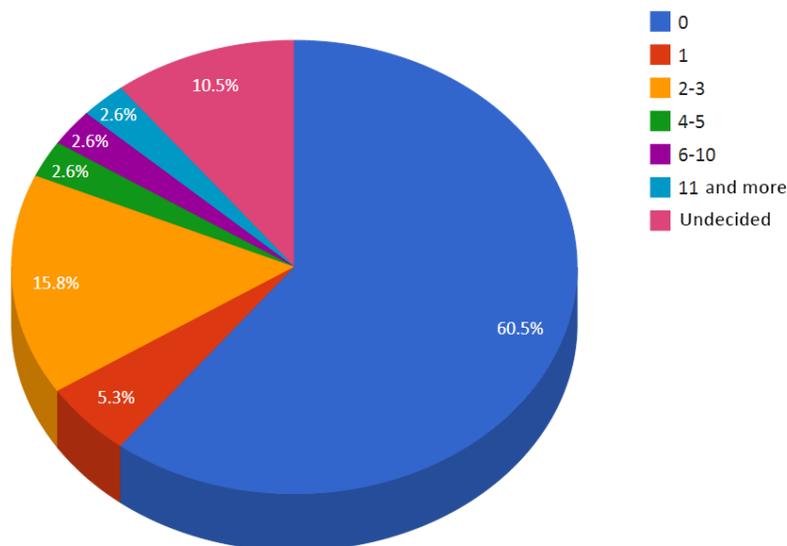
Chart 4: How many new products or services have you implemented in your enterprise since its foundation?



Source: Authors research

Regarding the question: **How many new technological solutions have you introduced in your enterprise?**, the results that have been obtained were expected, but also surprising. About 60.5% of the entrepreneurs said that they have never applied new technological solution. The result was expected because micro enterprises rarely have the resources to apply new technological solution. However, 15.8% of the entrepreneurs said that they introduced 2-3 new technological solutions in their enterprise and 2.6% said that they introduced 4-5, 6-10 and 11 or more new technological solutions.. Most prevalent technological solutions are knowledge transfer, technological solutions related to manufacturing processes and modification of equipment. Entrepreneurs who applied this solutions regularly attend conferences, business fairs and workshops in the country and abroad in order to perceive the new technological solutions in their fields and put a lot of effort to implement them in their enterprises.

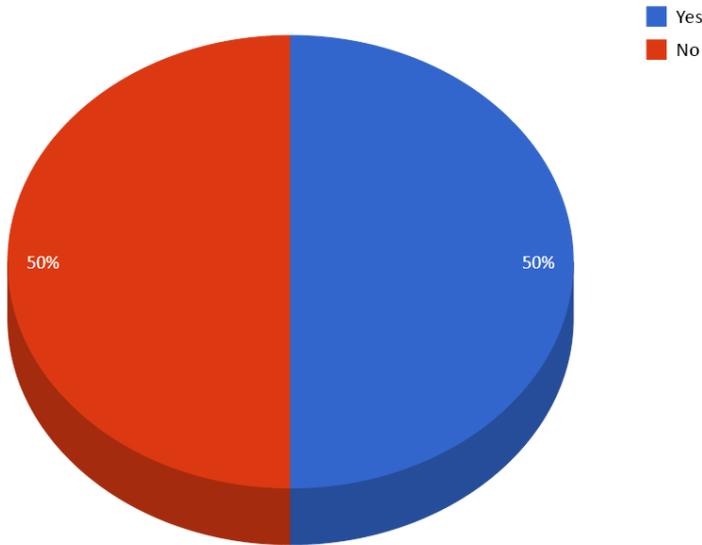
Chart 5: How many new technological solutions have you introduced in your enterprise?



Source: Authors research

Regarding the question: **Have you made new investments during the operation of the enterprise?**, the obtained results are half divided, 50% of the entrepreneurs made new investments and 50% didn't made new investments in their enterprise. Despite the difficulties they faced, entrepreneurs found strength and resources to expand their business venture. The most common type of investments are investments in new equipment, new capital investments and modernizing the premises of the enterprises. This results are indicator that gives us a picture of the faith that entrepreneurs have in their ventures, as well as their ambition and perseverance to succeed.

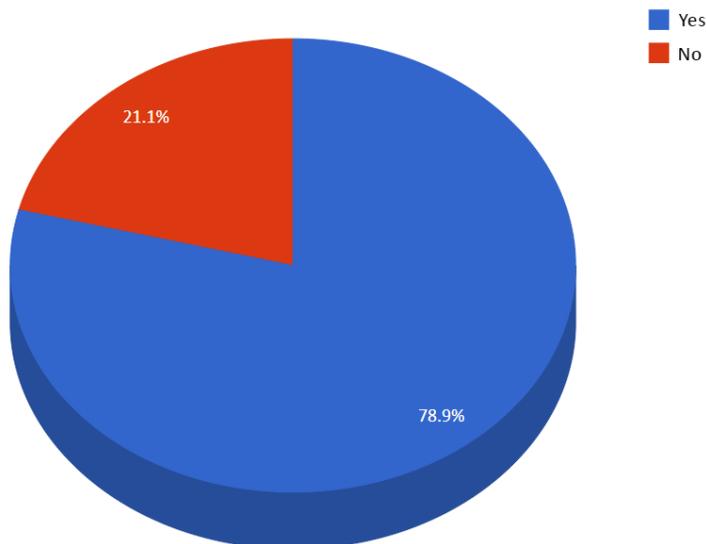
Chart 6: Have you made new investments during the operation of the enterprise?



Source: Authors research

Regarding the question: **Do you recommend to the unemployed persons who have ideas and desire to form their own business venture to participate in the program of “self employment via crediting”?** 78.9% of the entrepreneurs recommend to the ambitious people who have ideas and desire to form their own ventures to participate in the program. Yet, they also recommended to carefully asses their business ideas, to analyze the market, to calculate the risk and to form their enterprise only if they have faith in their abilities. A small proportion of 21.1% of the respondents didn't recommended taking part in this program. The results indicate that although respondents confront many problems, they appreciate the program, have entrepreneurial mind set and are willing to confront new challenges.

Chart 7: Do you recommend to the unemployed persons who have ideas and desire to form their own business venture to participate in the program of “self employment via crediting”?



Source: Authors research

According to the obtained results, self employment program via crediting increases the number of forming new business ventures of unemployed persons who have entrepreneurial aspirations in the markets of Republic of Macedonia, and their actions increase the entrepreneurial capital in the Macedonian economy.

5. RECOMMENDATIONS FOR IMPROVING “SELF-EMPLOYMENT PROGRAM VIA CREDITING” PROGRAM

In order to become more popular among unemployed persons and potential entrepreneurs, the future development of this program should consider following recommendations:

- Individuals who are granted funds under this program and that have formed business ventures through this program, in the first two years of operating to be free of charges to the state. This change

would give the opportunity to the potential entrepreneurs to develop their business ventures and to pay back the loan every month regularly. Two years period is enough to make their business ventures strong. After this period they will start to pay their obligations to the state.

- In order to improve the performances of the newly formed business ventures, it is necessary to establish a continuous contact between the Agency for employment of the Republic of Macedonia as the main institution which implements this government policies and program applicants. It is useful to carry out surveys to assess the performances of the newly formed business ventures, and with maintaining contact on regular basis the Agency for employment will be aware of the problems and challenges that newly formed business ventures face. Analyzing those problems will obtain proposed measures that have to be undertaken by the newly formed enterprises in order to solve their problems.
- Every business venture needs continuous support. Additional support could be received in various forms. Organizing workshops with business consultants could give an answer to entrepreneurs on their questions for finding new financial resources, or how to operate more efficiently, how to expand their brand products on different markets, and other questions that are concerned with their business venture. Networking is also needed by entrepreneurs and can be achieved through these workshops.

Conclusion

Considering the obtained results from the survey, self-employment program via crediting is becoming frequently used source of funds by the potential entrepreneurs in order to start their new business ventures in the markets of Republic of Macedonia. At a time when one of the biggest obstacles for starting innovative ventures, especially for young entrepreneurs, is lack of investment funds, participation in the self-employment program via crediting represents a way of overcoming this obstacle. As program changes in 2014, the number of young people up to 29 years who take participation in the program and use the funds in order to start their business ventures, have more than doubled. The high rate of survival of enterprises suggest high validity of the ideas, their differentiation, suc-

cessfully recognizing opportunities and taking risk that is calculated by the applicants of this program, thus presenting the entrepreneurial characteristic of their business ventures.

Survey results indicate entrepreneurial activity of the newly formed enterprises. Although these enterprises are micro enterprises, entrepreneurs who run them are innovating products, services, organizational processes, communication methods with their customers and distributors, marketing activities and new investment activities. Their ambitions produce exploring spirit and attending on trainings of different business fields in this country and abroad, as well as monitoring new trends in their fields of operating. Thus, entrepreneurs enhance their knowledge and skills which represent the basis for creation of competitive advantage and efficiently running business operations. Also, part of the respondents through the newly gained knowledge, introduce significant new technologies in their ventures which are important for better positioning on the markets they operate. Entrepreneurial activity is confirmed by the new investments of the entrepreneurs which are reflecting their quest for more, taking calculated risk, identification of new opportunities, opening new job positions and success of their products and services.

Certainly, the terms in the self employment program via crediting should keep modifying according to the needs of potential entrepreneurs. Still, with the actual terms, the program represents huge incentive in the creation of new entrepreneurial capital in the Macedonian economy. The approval and positive experience of the participators in the program confirm this hypothesis.

References

1. Taki F., Hadzi Vasileva-Markovska V., Bejtmen M. *Pretpriemnistvo*, Ekonomski fakultet Skopje, 2007,
2. Avlijas R., *Preduzetnistvo*, Univerzitet Singidunum, Beograd, 2010,
3. Dobre R., *Poduzetnistvo*, Zadar, 2006,
4. Deakins D., Freel M., *Entrepreneurship and small firms*, McGraw Hill, Breksire, 2002,
5. State Statistical office of Republic of Macedonia, *Broj na aktivni delovni subjekti*, number: 6.1.16.23, 2016,
6. Agencija za vrabotuvanje na Republika Makedonija, *Godisni izvestai za rabotata na Agencijata za vrabotuvanje na Republika Makedonija za period od 2006 - 2015 godina*.

NEDA PETROSKA-ANGELOVSKA*
MARIJA ACKOVSKA**

**FINANCIAL RATIOS FOR ASSESSMENT OF OPERATIONS
SUCCESS IN ENTERPRISES OF MACEDONIAN HOSPITALITY
INDUSTRY**

Abstract

This article is focused on issues related to operating efficiency and effectiveness of hospitality industry in the Republic of Macedonia. For that purpose, financial ratios for assessment of operations success in hospitality industry will be analyzed.

Financial ratios are measures of operating efficiency in the use of funds of enterprises. They show whether the available capacity of enterprises is properly utilized and whether assets are effectively managed. Indicators of efficiency of operation bind the income statement and balance sheet and associate relationship workload of the enterprise and the necessary funds for its maintenance. Higher values of these ratios indicates that operation of the enterprise is more efficient. The trend of these factors can serve as a guideline for planning of the increased workload or additional capital investment. In contrast, the trend of declining indicators of turnover of assets indicates that enterprises had not sufficiently exploit their facilities, or has a lower efficiency of use of funds, leading to a drop in profits.

The results of research in this paper show real trend of financial ratios in hospitality industry in the Republic of Macedonia for the analyzed period, due to different factors. For better operating results of those enterprises there are measures that should be undertaken in the forthcoming period on micro (enterprise) level as well as on macro (industry and national) level.

* Ph.D, associate professor, Institute of economics-Skopje, University "St. Cyril and Methodius", e-mail:neda@ek-nst.ukim.edu.mk

** Ph.D, associate professor, Institute of economics-Skopje, University "St. Cyril and Methodius", e-mail:marija@ek-nst.ukim.edu.mk

Key words: financial ratios, hospitality industry, financial statements, enterprises, Republic of Macedonia.

JEL Classification: M21; M41; Z3

Introduction

The financial analysis is mainly focused on analysis of data in intra-statements and official financial statements of enterprises. Number of indicators used can be different for different enterprises and depends on the analyst, the methodology applied, and the type of industry that enterprise belongs to.

That means that in enterprises that belongs to hospitality industry, also record all activities and transactions in financial statements, which are then used in decision-making of different parts as: managers, owners, government, banks and other financial institutions, business partners, competitors and other stakeholders. Depending on the nature of the user it is distinguished: internal and external accounting. Internal accounting relates primarily to internal users in hotels and restaurants, that first serve managers and it is called management accounting, and second one is external accounting that refers to external users or so called financial accounting.

However, there are evident shortcomings in making business decisions in hospitality industry based solely on the financial analysis. Major weaknesses are related to: the use of only historical data, overlooked market value of assets in the balance sheet, high level of use of figurative accounting, neglect of important economic information on micro and macro level and the like.

1. GOALS AND NEEDS OF ANALYSIS OF FINANCIAL STATEMENTS OF ENTERPRISES IN HOSPITALITY INDUSTRY

In order to obtain relevant data and information of financial condition of enterprise, analysts and users of financial statements, in spite of analysis of financial statements, are using additional data. They may be related to: the activity of the enterprise, environment, business relations with other companies and the like. Analysis of financial reports should not be confined to the financial statements a year, but should apply for at least 5 years.

This means that the analysis should be extended to examination of trends of certain financial indicators for longer periods, comparing the financial performance of one enterprise with another, because only in this way can be made realistic assessments of operational situation in enterprises. Analysis of financial statements is part of the overall system of economic analysis and covers the area of utilization of financial statements to evaluate the company's performance.¹

In the literature financial analysis is defined as:

- “Research, quantification, description and assessment of the financial status and performance of the enterprise. “²
- “Permanent process of systematic testing, evaluation of results and internal sources for financing of reproduction and by way of comparison, a breakdown and generalization in order to working people to be informed about the possibilities for improving the financial function of the enterprise.”³

On the other hand, according to the consulted literature financial analysis includes analysis of:⁴

- cash flows of the company, or inflows and outflows of funds or analysis of the liquidity of the company;
- factors of liquidity, i.e. analysis of financial results, revenues and expenses;
- relationships between assets and liabilities and
- relationships between financial and other functions in an enterprise.

Purpose of analyzing the financial statements relating to:⁵

- Assessment of the reasons for deviations in operations (positive or

¹ Spasic Vesna, Cerovic Slobodan: *Ekonomsko –finansijska analiza poslovanja preduzeca u hotelijerstvu i turizmu*, Univerzitet Singidunum, Beograd, 2013, p.161-215.

² Stojiljkovic M. and Krstic J: *Finansiska analiza*, Ekonomski fakultet, Nis, 2000, p 12.

³ Dohchevikj Sima : *Finansiska analiza kako instrument upravljanja finansijama u preduzeca*, Beograd, 1979, p.23.

⁴ Stojanovikj Todor: *Analiza na rabotenjeto na pretprijatijata, Sijuz na smstkovodstvenite I finansiskite rabotnici na Makedonija*, 1990, p. 35-44.

⁵ Ibid.

- negative) in order to improve the future operations of enterprises by undertaken of adequate measures to promote the positives;
- Better management enterprise, because the appropriate analysis provides additional data that are necessary for making quality business decisions;
 - Better performance of other functions in the enterprise, especially the functions of planning;
 - The provision of appropriate information and conclusions about the needs of a wider range of users of financial statements, which contributes to making appropriate business decisions and so on.

What refers to enterprises in hospitality industry, the aim of financial analysis is the same as it is already mentioned, having in mind the specific of hospitality industry. It is especially important to mention that there are specific indicators that arise from the financial analysis of operating of hospitality industry that will be presented in this paper. They refer to liquidity, financial structure and safety and profitability of hospitality industry.

2. REVIEW OF KEY FINANCIAL RATIOS OF OPERATION SUCCESS IN ENTERPRISES OF HOSPITALITY INDUSTRY

Financial indicators are obtained as the ratio between the figures of two or more balance sheet items, based on the obtained certain result. Thus the result, because by itself does not provide useful information and cannot serve as an adequate analysis of financial statements, commonly are compared to appropriate standards in order to see what is the financial and operating status of the enterprise in relation to standards. As standards for comparison and proper interpretation can be used as follows:

- targeted performance of the enterprise in hospitality industry, as defined by management;
- indicators of enterprise in hospitality industry realized in previous years;
- indicators of leading enterprises or competitors that belongs to the same industry as analyzed enterprise;
- the average of the operation indicators of to the enterprise;

- the interpretation of financial indicators should always be careful because there are limitations on their use;
- lack of appropriate standards for comparison (benchmarks).

It should be noted that there are no pre-defined standards that could be used at any time and in any situation for financial analysis in hospitality industry. They change depending on the purpose of the analysis and the need for making different conclusions and decisions. For example, the high liquidity ratio for short-term lender is a good indicator, but for investors it can be inadequate management of working capital. Furthermore, attention should be paid to: the point in time of calculation of ratios, the impact of inflation on the balance sheet items, the possibility of negative numbers to be unnoticed, the use of different accounting methods for different companies and so on.

It should be notice that for the purpose of this paper liquidity ratios, financial structure and safety indicators and profitability indicators of hospitality industry will be taken into account.⁶

♣ *Liquidity ratios in hospitality industry*

Liquidity ratios indicate the ability of the company to settle its obligations at maturity. Maintaining liquidity is one of the primary tasks of management. Gaining of better liquidity status leads to confidence among financial institutions that can provide sources of funds through the capital market at low interest rates. Also, the benefit can be found by avoiding costs for late payment etc. The liquidity of the company, generally depends on the amount of current assets, their structure and funding. But not always an enterprise should attempt to keep large amounts of working capital because it could adversely affect the profitability of operations or the financial result. Commonly used indicators of liquidity of enterprises are as follows: current liquidity ratio, quick liquidity ratio, cash liquidity ratio, net-working capital, operating profit quality, net income quality, efficiency in collection of receivables (revenues quality).⁷

⁶ Spasic Vesna, Cerovic Slobodan: *Ekonomsko –finansijska analiza poslovanja preduzeca u hotelijerstvu i turizmu*, Univerzitet Singidunum, Beograd, 2013, p. 128-133.

⁷ Brigham F. Eugene, Daves R. Philip: *Intermediate financial management*, Gengage learning Company, (izdadero na makedonski jazik od ARS lamina 2014) 2010, p. 726-758.

The indicator of current liquidity is calculated as the ratio of current assets (cash, short-term securities, receivables and inventories) and current liabilities (trade payables, liabilities for short-term loans, taxes and supplies). The higher level of this indicator means better of liquidity and conversely, a lower ratio indicates that the company falls into insolvency, and requires the use of foreign funds. This is as a general attitude in the literature, but more appropriate for determining the level of this indicator should take into account several factors including the activity of enterprises, and then all other elements related to the functioning of the operating process.

The indicator of current liquidity excludes inventory from the calculation due to their least liquid form as current assets. The ratios of current liquidity and quick liquidity are based on transformation of inventories and accounts receivable into cash. Therefore, these factors should be analyzed together with other indicators of performance, especially with the turnover ratio of receivables, inventories and liabilities.

If we take into account accounts receivable and inventories in the calculation of liquidity indicators, as is the case with the previous two indicators, a problem of achieving real liquidity can arise. In fact, claims are a category of current assets that may be uncollectible, while the quantities to be obsolete and thus cannot achieve full liquidity operations. To overcome such anomalies in the application of these factors, in the literature another factor is known- cash ratio of liquidity.

Cash ratio is the most conservative indicator of liquidity because it takes into account only cash and securities the most liquid form of current assets. But despite this ratio exceeds the disadvantages enterprises faced with current and quick liquidity, weaknesses of all three factors, still remain.

Apart from the aforementioned liquidity indicators, is net working capital, which represents the difference between current assets and current liabilities. Ratio for this indicator is shown as follows:

$$\text{Net working capital} = \text{Current assets} - \text{Current liabilities}$$

In fact, a positive amount of this indicator suggests that the company has a certain degree of liquidity, i.e. that time can perform their duties.

The practice showed that the liquidity is not conditional on the static relationship between the individual elements of the balance sheet, but is closely linked and dependent on the cash inflows and cash outflows and their balance. The enterprises, that have a high level of current liquidity, while in current assets structure, levels of inventory and accounts receiv-

able that are difficult to convert into cash, dominate, may become illiquid if more obligations come to maturity. To avoid this drawback, it is necessary to analyze data from the statement of cash flows. In this regard, all significant inflows and outflows, especially should pay attention to the net inflow from operating activities. Based on these data can assess the quality of business profits, the quality of net income, earnings quality - efficiency in collection process.

$$\text{Business profit quality} = \frac{\text{net cashflow from operating activities}}{\text{business profit}}$$

The results of the calculations show how denars net cash flow from operating activities generated by a penny business profit (the lower the risk of insolvency is higher) . in practice, this is a significant indicator to detect different aspects of undercover accounting data such as shown higher revenues, lower costs and consequently shown a higher financial result. The risk is higher because it also displayed financial result is not usually accompanied by a stream of cash.

$$\text{Net income quality} = \frac{\text{net cashflow}}{\text{net income}}$$

Net income quality in its calculation takes into account cash flows from the activities and shows how the company draws money and generate free cash flow of investment, operational and financial activities.

$$\text{Efficiency in collection process} = \frac{\text{net cashflow}}{\text{operating revenues}}$$

Efficiency in collection of receivables (revenues quality) shows percentage of collected revenues from operating activities during the accounting period, ie how many of them remain outstanding. So, results from this indicator can also be used in the process of appreciating the degree of risk of insolvency of enterprises un hospitality industry.

♣ *Financial structure ratios in hospitality industry*

The ratio between own and borrowed sources of funds indicates the quality of the financial structure of enterprise and its financial security. These indicators, also belong to the group - solvency ratios, that can be

taken into consideration also as the ratio of cash inflows and outflows in the long term. As important indicators of the solvency of enterprises in hospitality industry in this paper are analyzed: the level of indebtedness, ratio of capital and financial leverage factor.

The indicator for the level of indebtedness of enterprises indicates the extent to which the company is financed by borrowed sources of funds, ie the share of liabilities in the financial structure. The lower level of this index indicates more solvent company.⁸

Capital ratio shows the level of financing by own capital of enterprise, i.e the share of own capital in total liabilities amount. This indicator, thereby indicates the financial risk or financial safety of enterprise.

Financial leverage factor indicator, also is used to measure financial risk of enterprise. The level of financial expenses arises from the level of financing through borrowed resources and shows the uncertainty of achieving a net income related to oscillations in operating profit.

The impact of financial leverage depends on the difference in the return on equity and average interest rate, as well as on the share of liabilities in total sources of financing. As much as these factors are on higher level, the positive effect of financial leverage on profitability of capital.⁹

♣ *Profitability ratios in hospitality industry*

Profitability as a principle for achieving maximum profit with less used assets, can be shown through the following indicators: indicator of business profit and net profit rate- as partial indicators, as well as through ROA (return on assets) and ROE (return of equity) indicators- as a synthetic one. Special system of analyzing the profitability of enterprises is through the Du Pont analysis system, where by disaggregating ROA and ROE on separate components, management is trying to perceive appropriate strategies for improving profitability of enterprise.

Business profit ratio shows the gross margin, ie how much denars of operating profit is generated by 100 denars operating income. Net profit rate is a result remaining after covering all expenses of the enterprise, income tax,

⁸ Brealey A. Richard, Myers C. Steward, Allen Franklin: Principles of Corporate Finance, The McGraw-Hill Companies, (izdadero na makedonski jazyk od ARS lamina 2015) 2011, p. 440-465.

⁹ Ibidem.

etc., or it shows the share of net profit in operating revenues. The meaning of this indicator comes to the fore if the results are compared with competing businesses in the same industry and is commonly used in practice.

ROA shows the profitability of total assets, ie the degree of growth of total operating assets involved in the enterprise. In fact, this indicator refers to the net profit and if it realizes unit engaged assets. Through this indicator data horizontal or trend analysis can be carried, or data might be compared with overall results of the industry, group of enterprises or separate competitive enterprise.

Operating income ratio can be divided, if it is already known that than ROA can be increased by increasing the operating income through higher sale prices, declining of number of employees etc, as well as by faster turnover of total assets over a shorter turnover of inventories and faster collection of receivables. The point is to put attention on management of turnover of total assets.

Closely related to ROA is ROE and it is showing the level of return on equity while taking into account the financial structure that shows the growth of equity at the end of the period compared to the beginning. The results of this indicator can be improved by better level of net income and faster turnover of capital.

3. IMPLEMENTATION OF KEY FINANCIAL RATIOS OF OPERATION SUCCESS IN ENTERPRISES OF MACEDONIAN HOSPITALITY INDUSTRY

Despite the theoretical approach for determining the operating performances of enterprises in hospitality industry, for the purpose of this paper quantitative research is conducted, too. Data that are further analyzed in the paper are derived through research conducted by questionnaire in period 2014/ 2015. The questionnaire was sent to 40 enterprises in hospitality industry in the Republic of Macedonia (selected at random), of which 32 enterprises have provided the answers to the questionnaire .

In Table 1 is shown an overview of the results obtained from the calculation of theoretical displayed indicators of surveyed enterprises for a period of 5 years.

Table 1: Financial ratios for operation success of enterprises in hospitality industry in the Republic of Macedonia

<i>Ratios</i>	2011	2012	2013	2014	2015
Liquidity ratios in hospitality industry					
<i>Current liquidity ratio</i>	5,76	1,26	4,41	4,31	4,7
<i>Quick liquidity ratio</i>	5,23	1,00	4,03	3,95	4,2
<i>Cash liquidity ratio</i>	4,10	0,42	1,32	1,2	2,14
<i>Net working capital (in million MKD denars)</i>	24.157	2.684	24.685	23.817	26.259
<i>Operating profit quality</i>	1,59	2,21	1,29	1,22	1,37
<i>Net income quality</i>	0,53	-1,04	0,17	0,16	1,17
<i>Efficiency in collection of receivables</i>	1,12	1,13	1,13	1,12	1,13
Financial structure ratios in hospitality industry					
<i>Level of indebtedness</i>	1,23%	2,52%	1,73%	1,72%	1,74%
<i>Own capital ratio</i>	98,08%	96,63%	97,27%	97,28%	97,26%
<i>Financial leverage</i>	1,02	0,95	1,04	1,04	1,04
Profitability ratios in hospitality industry					
<i>Business profit ratio</i>	14,53%	9,17%	16,56%	16,5%	16,58%
<i>Net profit rate</i>	14,31%	9,62%	15,98%	15,95%	15,99%
<i>ROA (Return on assets)</i>	2,16%	3,64%	6,52%	6,5%	6,55%
<i>ROE (Return on equity)</i>	2,16%	3,92%	6,49%	6,47%	6,49%

Source: Calculated ratios based on data in financial statements for appropriate years of surveyed enterprises in hospitality industry

According to data in the table 1 it can be considered that the index of current liquidity for the analyzed period was the highest in 2011, where the coverage of current liabilities with current assets is 5.76, while at the end of the period the amount is 4.7 (due to the synthetic character of current assets, the results cannot be taken as favorable one without depth analysis of current assets structure) . This indicator shows least favorable result in 2012, where coverage is at a level of 1.26 or every MKD denar of current liabilities of the analyzed enterprises is covered by 1.26 denars of current assets.

Reduced liquidity indicator or quick liquidity ratio shows that surveyed enterprises from hospitality industry in the Republic of Macedonia,

to settle 100 denars current liabilities have to use 523 denars in 2011, 100 denars, 403 denars, 395 denars, 420 denars liquid assets (cash and receivables) respectively per year. This indicator is most unfavorable in 2012, too. As we mention before this indicator doesn't take into consideration the level of uncollected receivables, which is one of the crucial problems in macedonian economy.

Results of cash ratio concerning coverage of current liabilities with cash, for the analyzed period in years, is as follows: 410 denars, 42 denars, 132 denars, 120 denars and 214 denars. As it can be seen the best coverage of current liabilities with cash there is in 2011, but it doesn't mean that this is optimal one. This means that the profitability of enterprises might be problematic issue. Liquidity ratios must be taken into consideration together with net working capital amount, that is on highest level in 2015 year which is positive indicator for the liquidity degree.

From the above table, it is evident that observed enterprises don't have significant level of indebtedness for all analyzed period. Business profit ratio and net profit rate data show that the highest level is generated in period 2013-2015, and the same conclusion for that period can be made for ROA and ROE indicator in hospitality industry in the Republic of Macedonia.

As we can see, in almost all indicators for operations success in hospitality industry it is evident improved substantially, over the last three years of the analyzed period. However, positive influence on this data has the process of gradually overcoming the economic crisis world while and on European continent. Consequently, indirect impact of economic crisis on Macedonian economy is lower. Also, the situation is a result of good policy making in recent period and measures that are undertaken toward special affirmation of tourism on international level.

Conclusion

The essence of financial analysis of operations of companies consists of using the results obtained by calculating the indicators of balance sheet items and their comparison with the standard, theoretical and empirical sizes. Conclusions from the analysis process are useful for internal and external, current and potential stakeholders in decision-making process.

That approach gives more reliable picture for the enterprise operation success. That means that it's possible to have more accurate amount of revenue and operating expenses of the enterprise as a whole and in parts, i.e. monitoring of profitability trends by units, which is very important element for successful management in enterprises of hospitality industry.

In order successfully to manage businesses in hospitality industry, it important and required according to the stated criteria periodically to compare performances among competitors in the same industry. In that way, hospitality industry enterprises will go on in better direction, through improvement of their offer and better cost - effectiveness.

References

1. Brealey A. Richard, Myers C. Steward, Allen Franklin: Principles of Corporate Finance, The McGraw-Hill Companies, (izdadero na makedonski jazik od ARS lamina 2015) 2011.
2. Brigham F. Eugene, Daves R. Philip: Intermediate financial management, Gengage learning Company, (izdadero na makedonski jazik od ARS lamina 2014) 2010.
3. Dohchevikj Sima: Finansiska analiza kako instrument upravljanja finansijama u preduzeca, Beograd, 1979.
4. Stojanovikj Todor: Analiza na rabotenjeto na pretprijatijata, Sijuz na smstkovodstvenite I finansiskite rabotnici na Makedonija, 1990.
5. Spasic Vesna, Cerovic Slobodan: Ekonomsko –finansijska analiza poslovanja preduzeca u hotelijerstvu i turizmu, Univerzitet Singidunum, Beograd, 2013.
6. Stojiljkovic M. and Krstic J: Finansiska analiza, Ekonomski fakultet, Nis, 2000. UDC 005.336.5:005.963.1(497.7)

IRINA MAJOVSKI*
ELENA DAVITKOVSKA**

DEVELOPING EMPLOYEE SKILLS IN CHALLENGING TIMES

Abstract

In the contemporary business context, the significance of employee skills and competences is widely acknowledged. Investments in formal and continuous training have become inevitable need both for employees and businesses. In challenging times, however investments in employee skill development are hindered by cost-cutting measures imposed by companies as a response to the rising impediments. Therefore, the primary aim of the paper is to assess recent developments in employee training policies in Macedonian businesses and the potential impact of the economic downturn on training investments. A research was conducted in 24 medium-sized companies in different industries in R. Macedonia covering employee training issues. The overall findings point to a reduction in training investments and companies' focus on in-house, job-specific employee training.

Keywords: employee skill development, economic downturn, training investments

JEL classification: M50

* PhD, Assistant Professor, Ss. Cyril and Methodius University, Institute of Economics – Skopje, e-mail: irina@ek-inst.ukim.edu.mk

** PhD, Assistant Professor, Ss. Cyril and Methodius University, Institute of Economics – Skopje, e-mail: elena@ek-inst.ukim.edu.mk

Introduction

Employee training and development have become essential element of human resource management. Businesses are facing rapid changes in market conditions and are becoming more dependent on employee skills and competences. In this context, formal and continuous training has become inevitable need both for employees and businesses.

Recent technological advances and the strive for competitive position in the market have led to the recognition of the impact of employees' skills and competence on organizational success, which subsequently resulted in increase of employee training investments. Moreover, the development of human resource management and the growing focus of companies on organizational commitment have highlighted the significance of employee training and development as well as organizational learning. The above has imposed employee training as a continuous activity in organizations in order to stay competitive, improve organizational performance and retain key employees.

The concept of knowledge-based economy has given central position to human capital and skills development in all societies. Investments in the development of human capital have become primary worldwide and are integral part of the European Commission strategic framework Education and Training 2020¹.

The commitment to developing employee skills faces major challenges during a period of economic downturn. Indeed, long-term economic downturn has proved to have negative impact on the overall training investments and employee skill development. While tackling financial challenges companies respond by cost-cutting measures that are imposed on training investments among other. Consequently, this hampers the recovery of businesses and deteriorates their competitive position.

1. THE GROWING IMPORTANCE OF EMPLOYEE TRAINING AND DEVELOPMENT

Training and development pertain to activities that improve employee skills and competences having direct impact on their performance.

¹ European Commission, Education and Training, Supporting education and training in Europe and beyond, [http://ec.europa.eu/education/policy/strategic-framework_en]

In general, training refers to improving skills and competences directly related to the work, while development refers to a broader learning of the individual and employee's career².

Training should not be taken as a series of interventions to upgrade employee's knowledge with immediate improvements in individual and organizational performance. In contemporary business context, this concept is too narrow to encompass employee training and development. In this regard, necessary skills and competences change rapidly hence creating a need for their continuous improvement. Employee training is about developing skills and competences that are not easily available in the labor market i.e. developing a set of tailor-made skills and competences that fit company's strategy and meet specific business needs. The strategic objective of employee training and development is improvement of organizational performance.

The growing interest in developing human capital and investments in employee skills and competences reflect the change in organizational approach to human resources and their deployment. Recent research supports this trend. The financial results of companies account for 50-70% of their market value while the rest is prescribed to intangibles as intellectual property and human capital³. Developing human capital is organizational prerequisite for increase of shareholder value.

Yet, the decision on investment in employee training, its type and intensity largely depend on various factors as culture, industry, state policies on education and training, company's strategy and objectives. Namely, training was found to be part of HRM strategy in companies in 10 European countries⁴. Generally, the report suggests that there has been an overall increase in training investments over the last decade, however, only in Sweden and France⁵ more than a quarter of surveyed companies

² Mullins, L. "Management and Organisational Behaviour" (9th Ed.) Prentice Hall, London, England, 2010, p.174

³ Ulrich, D. & Smallwood, N. "Human resources' new ROI: Return on intangibles" in Losey, M., Meisinger, S. & Ulrich, D. (Eds) "The Future of Human Resource Management: 64 Thought Leaders Explore the Critical HR Issues of Today and Tomorrow", John Wiley & Sons, Inc., NJ, 2005, p.229

⁴ Holden, L. & Livian, Y. "Does strategic training policy exist? Some evidence from ten European countries", *Personnel Review* 21(1), 1992, pp.12-23

⁵ Based on the French system of continuing education and training, companies that do not invest a minimum of 1.4% of their payroll budget are subject to a special tax.

invested more than 4% of the payroll budget in employee training and only 10% of the companies offered more than 10 days training annually.

Training for skills development is more often conducted for middle and top management as opposed to line management and employees⁶. In this regard, in the US, companies invest three to four times more in training on stress management and running effective meetings than skills development of employees that seek promotion⁷. There are several reasons why companies might choose to invest less in training than the optimal level. First, in most countries there are no regulations that would impose a minimum training for employees, and second, training costs are immediate while training benefits are indirect and delayed. Taking into account the above-said as well as organization's short-term budgets and higher profit pressure, many companies consider training a cost that is first to be cut.

Research on company's benefits from training confirms the significance of employee skills development. For example, formal training programs significantly increase workforce productivity. Formal training programs conducted in 495 companies⁸ showed an average of 17% increase of staff productivity in three consecutive years, making companies' productivity higher than that of competitors.

A research on the effects of training confirmed the positive relation between the level of training investments and company's profitability, whereas employee fluctuation was found not to affect training investment but it did have a negative impact on company's profitability⁹. The above might be due to the fact that the economic benefits of training outweigh the costs related to employee training and lost human capital in which was invested. Employee fluctuation is not a predominant factor affecting training investments. In this regard, the most important factors that determine the level of investments in training refer to company's management, training

⁶ Bratton, J. & Gold, J. "Human Resource Management: Theory and Practice" 4th Ed., Palgrave Macmillan, NY, 2007, p.275

⁷ Pfeffer, J. "Competitive Advantage Through People: Unleashing the Power of the Workforce", Harvard Business School Press, Boston, 1994, p.68

⁸ Bartel, A. P. "Productivity gains from the implementation of employee training programs", Working Paper No. 3893, National Bureau of Economic Research, Columbia University, MA, 1991 [<http://www.nber.org/papers/w3893.pdf>]

⁹ Hansson, B. "Company-based determinants of training and the impact of training on company performance: Results from an international HRM survey", *Personnel Review* 36(2), 2007, pp. 311-31

needs assessment, developed formal training policies and educational level of employees.

Training is closely related to the quality of output as well. A study on small production businesses in US showed that the increase in training hours results in 7% decrease of product scrap rate¹⁰. The effects of formal employee training on organizational performance are manifold, as it has positive impact on quality of products, product development, market share, sales increase and profit increase¹¹. Moreover, 1% point increase in work-related training results in 0.6% increase in employee productivity, measured by value added per hour, as reported by the survey conducted in 94 industries in Great Britain over a period of 14 years¹².

The benefits of employee training and development for overall organizational performance are recognized by Macedonian businesses as well. The research, conducted in Macedonian businesses in 2009, showed that businesses invest in employee training¹³. The majority of surveyed companies conduct formal training in soft skills as well as work-related training for about 30% of their employees. Work-related training prevails over other types of training (with over 30% of employees in surveyed companies having undergone such training) and generally encompasses employee skills development related to customer relations, technical skills and quality management. On the other hand, personal development trainings related to stress management, time management, teamwork, motivation and efficiency included less than 30% of the employees.

In this context, literature confirms that most organizations conduct training in work-related skills development customized for specific business needs as opposed to personal skills development that are easi-

¹⁰ Holzer, H., Block, R., Cheatham, M. & Knott, J. "Are training subsidies for firms effective? The Michigan experience", *Industrial and Labor Relations Review* 46(4), 1993 pp. 625-36

¹¹ Kalleberg, A.L. & Moody, J.W. "Human resource management and organizational performance", *American Behavioral Scientist* 7(37), 1994, pp. 948-62

¹² Dearden, L., Reed, H. & Van Reenen, J. "The impact of training on productivity and wages: Evidence from British panel data", *Oxford Bulletin of Economics and Statistics* 68(4), 2006, pp.397-421

¹³ Мајовски, И. "Влијанието на стратешкиот менаџмент на човечки ресурси врз организациските перформанси кај деловните субјекти во Република Македонија", докторска дисертација, Економски Институт-Скопје, 2010, стр.85

ly transferred to other organizations¹⁴. The work-related training directly affects the improvement of employee skills and competences in accomplishing their job activities hence making training benefits direct and more transparent both on individual and organizational level.

2. EMPLOYEE SKILL DEVELOPMENT DURING ECONOMIC DOWNTURN

Economic downturn occurs with little warning and deteriorates market performance thus imposing rapid response by companies and significant changes to organizational strategy. In such challenging times, investments in employee training and skill development are the first to feel the consequences of the reactive measures by companies. Companies are expected to cut training and development budgets over 10% in response to recession¹⁵. Businesses are generally reluctant to invest in training during deep downturn as they seek to reduce costs and solve acute financial challenges and training costs are considered to be additional burden to companies.

On the other hand, training in economic downturn is essentially important to overcome challenges that companies face and prepare the organization for post-recessionary period. In addition, during economic downturn major concern of employees has proven to be job security. In this regard, training and development programs can boost employee morale and organizational commitment as employees regard training as company's investment in them¹⁶. Companies that use more rigorous staffing and training outperform competitors, before and during a recessionary period and recover more quickly than those companies that do not use so rigorous practices¹⁷. Moreover, these human resource practices enhance both organizational and financial performance of businesses and differentiate the organization from competitors.

¹⁴ Beardwell, I., Holden, L. & Claydon, T. "Human Resource Management: A Contemporary Approach", 4th Edition, Pearson Education Limited, UK, 2004, p.343

¹⁵ Noe, R. "Employee training and development", (5th Ed.), New York: McGraw-Hill, 2010, p.11

¹⁶ Flannery, J. et al. "Experiencing training: the need for a detailed investigation", Working With Older People, 9 (1), 2005, pp. 13-16

¹⁷ Kim, Y. & Ployhart, R.E. "The effects of staffing and training on firm productivity and profit growth before, during, and after the great recession", Journal of Applied Psychology, Vol.99 No.3, 2014, pp.361-389

The 2008-09 recession has not affected the level of training investments considerably as major reductions in employee training were not reported. Companies have given priority to temporary and full-time employee layoffs over cutting back on employee training and using early retirement¹⁸. This is mainly because the cuts on employee training and development were least effective in the previous recession and had negative impact on employee commitment and consequently productivity. In this context, private sector employers in UK continued to invest in employee training, but primarily in ‘training floors’ that were essential for their operations¹⁹. Businesses, however, did seek alternative cost-effective ways to deliver training as in-house training, having regular employees as trainers, group training and increased e-learning. The above could be mainly due to the fact that businesses are obliged to sustain employee training despite the recession in order to comply with legal requirements and meet operational needs and customer demands²⁰.

Although, a large scale survey in central England²¹ reported some reduction in training investments among small and medium-sized enterprises as a result of the costs of training and managers’ belief that employees did not need training. Namely, around a quarter of the surveyed companies has never provided any training to the employees.

That the last recession did not affect considerably the commitment of businesses to employee training and development in Europe was also confirmed by Cranet’s latest research on HRM policies throughout Europe²². The EU average of training investments was reported to amount to 3.72% of the annual payroll budget whereas Europe non-EU average

¹⁸ Strack, R. et al. “Creating people advantage in times of crisis: how to address HR challenges in the recession”, Boston Consulting Group & European Association for People Management, 2009 [<http://www.thebostonconsultinggroup.es/documents/file15460.pdf>]

¹⁹ Felstead, A., Green, F. & Jewson, N. “Training in the Recession: The impact of the 2008-2009 recession on training at work”, UK Commission for Employment and Skills, Evidence Report 72, 2013, p. 64

²⁰ Ibid, p. 88

²¹ Green, A.E. & Martinez-Solano, L.E. “Leveraging training skills development in SMEs: An analysis of the West Midlands, England, UK”, OECD Local Economic and Employment Development Working Paper Series, 2011, p.27

²² Cranet Survey on Comparative Human Resource Management, International Executive Report 2011, Cranet 2011, [http://www.ef.uns.ac.rs/cranet/download/cranet_report_2012_280212.pdf]

was 4.73%. Comparing the findings with that of Cranet's survey in 2005²³, when the average investments in employee training accounted for 3% of the payroll budget and an average of 44% of employees was found to participate in formal training, it could be concluded that there is no dramatic impact of the recession on training investments.

The general observation is that recession has negative impact on employee training. When revenues shrink, cost-cutting measures are inevitable in companies, since they seek to reduce costs in order to overcome market challenges, hence reflecting on training budgets, among others, as well. However, the last recession proved that employers have recognized the value of employee training and seek to sustain the levels of training investments by balancing the high costs of training and training benefits through alternative methods of delivery of employee training. Companies that acknowledge training benefits, and focus on long-term strategy as well, may change the delivery of training to less expensive alternatives as taking training in-house, using experienced staff to train others or introduce e-learning. The reduction in training investments mainly refers to training on soft skills whereas training in job-specific skills, that are core to businesses, has kept the same levels of the pre-recession period.

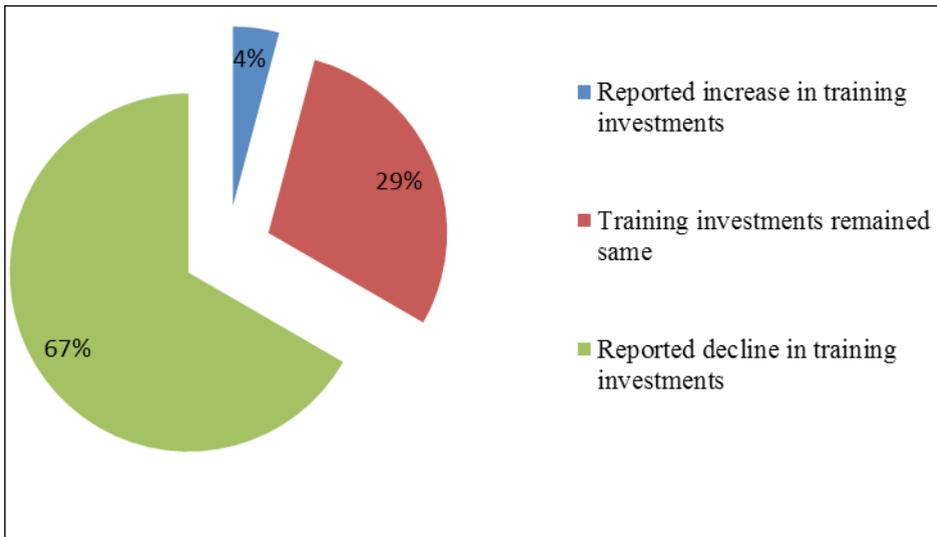
3. RECENT TRENDS IN EMPLOYEE SKILL DEVELOPMENT IN MACEDONIAN COMPANIES

Training investments reported by Macedonian businesses however, do not follow world trends in this area. Namely, in order to assess recent developments in employee training policies in Macedonian businesses and the potential impact of the economic downturn on training investments, a research was conducted in 24 medium-sized companies in different industries during spring 2016. A questionnaire pertaining to employee training aspects was distributed to the managers of the surveyed businesses and included issues related to the level of training investments, types of training conducted, methods used by companies to deliver employee training, as well as major limitations to training investments. The overall findings point to a significant reduction in training investments and companies' focus on in-house, job-specific employee training.

²³ Cranet Survey on Comparative Human Resource Management, International Executive Report 2005, Cranet 2006 [<http://www.ef.uns.ac.rs/cranet/download/internationalreport2005-1.pdf>]

The findings from the survey indicate that companies have introduced cost-cutting measures in practices that refer to employee training and development. Namely, the majority of surveyed businesses (67%) have reported a decline in investments in employee training, whereas almost 30% of the businesses have managed to remain the same level of investment in training in the last two years (Figure 1).

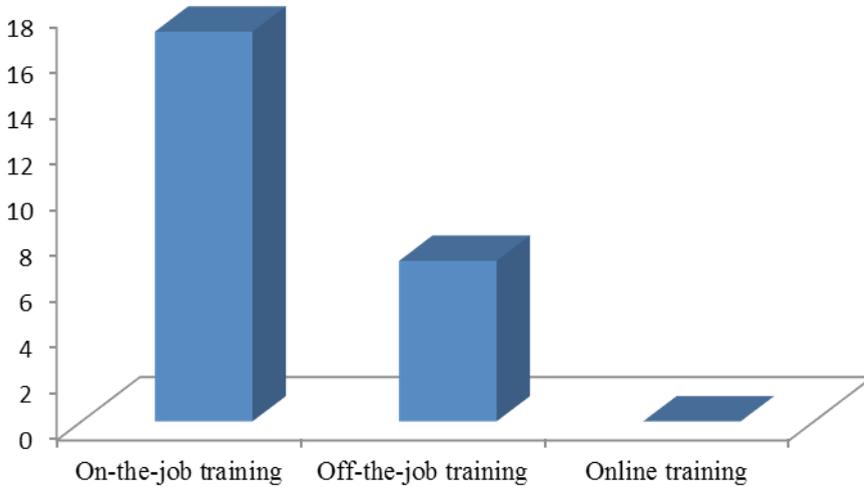
Figure 1. Level of investment in employee training in the last two years



Source: Authors' research

Businesses mainly deliver on-the-job training as about 70% of surveyed companies have conducted this method of employee training in the last two years (Figure 2). This finding does not come as a surprise since on-the-job training is more cost-effective as opposed to off-the-job training and, as it is closely related to job specifics, it meets individual business needs. Companies have not reported using online training which might be due to the lack of online training available in the market that meet their needs thus making companies reluctant to use this training delivery method.

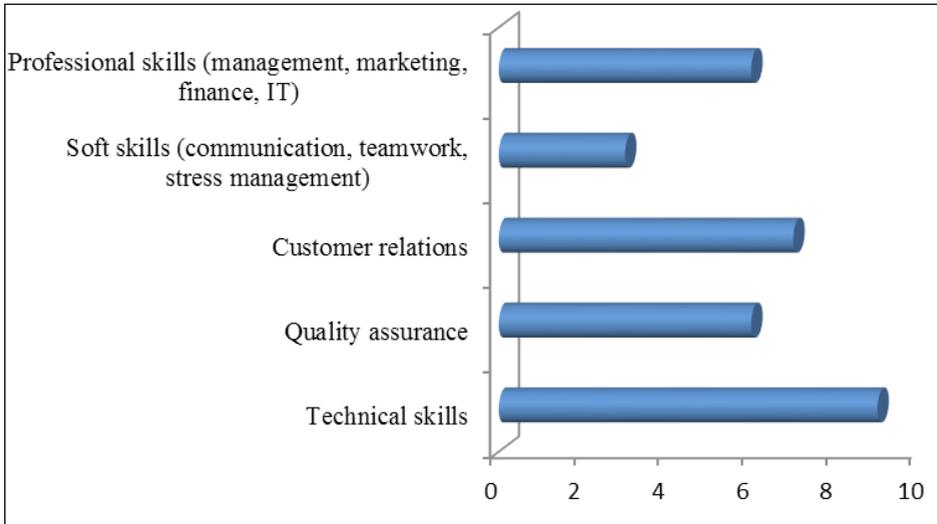
Figure 2. Training delivery methods used by businesses in the last two years



Source: Authors' research

Investments in training in the last two years reported by surveyed companies generally relate to upgrading and developing job-specific employee skills and competences. Businesses have focused on training programs that develop employee skills mainly pertaining to technical skills, customer relations and quality assurance (Figure 3). These types of skills are essential for the operational needs of companies and are hence of primary interest to the businesses. In this context, during economic downturn, companies focus on training that improves employee skills necessary to meet the immediate goals of businesses, effectively perform core activities and maintain current market position.

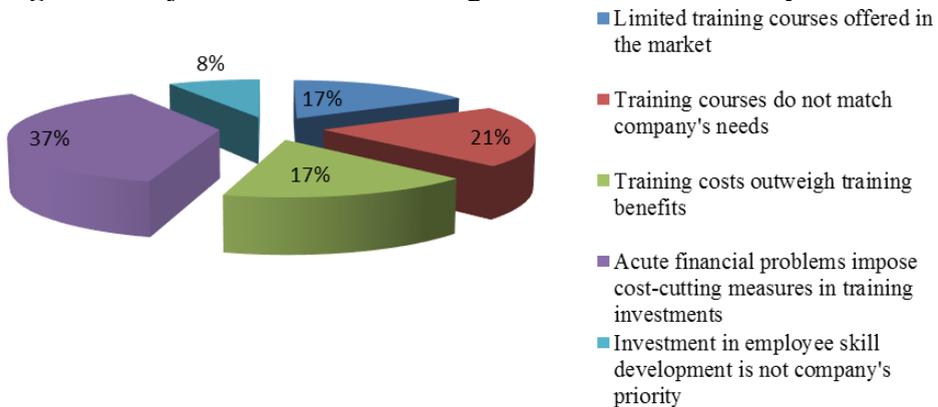
Figure 3. Type of employee training delivered in the last two years



Source: Authors' research

The reasons reported by surveyed companies for the barriers to training investments are various. However, acute financial problems that impose cost-cutting measures in training investments in companies is a predominant reason for the decline, reported by 37% of businesses (Figure 4).

Figure 4. Major limitations in training investments indicated by businesses



Source: Authors' research

Some of the surveyed companies reported that training courses offered in the market do not match company's needs. This could be due to the fact that most of the training programs offered in the market are oriented toward individual development, whereas what companies prefer to invest in is job-specific training, i.e. tailor-made courses that match the primary needs of the companies. In addition, the findings reveal lack of recognition of training benefits among Macedonian businesses. Some of the participants in the survey believe that costs related to employee training outweigh the benefits, which implies that the significance of employee skill development is not yet fully acknowledged by businesses.

Conclusion

Nowadays, the value of human capital to companies is widely accepted by most employers. In contemporary business settings, the unique set of specific skills and competences of employees significantly contributes to its competitive position in the market. In this regard, employee training and development have become an integral element of business strategies.

During economic downturn, however, companies pay insufficient attention to developing employees' skills and competences. Moreover, coping with various challenges, many companies insist on short-term cost-cutting measures among which investments in employee training. High costs related to investments in employee training and development are always a concern for management in difficult times and thus, many companies are reluctant to maintain the same level of investments. Coping with current challenges and reactive cost-cutting measures businesses can undermine the future competitiveness of the company.

The recent economic downturn has however presented the commitment of businesses to developing employee skills and competences as part of their long-term strategy. Many companies have managed to remain the level of training investments during economic downturn and, as they try to keep costs at low level as possible, they compensate through alternative methods of delivery of employee training as in-house training, group training and increased e-learning. Nevertheless, the research in Macedonian companies reveals overall reduction in the level of training investments and focus mainly on on-the-job training that is work-related and meets their immediate needs.

References:

1. Bartel, A. P. "Productivity gains from the implementation of employee training programs", Working Paper No. 3893, National Bureau of Economic Research, Columbia University, MA, 1991
2. Beardwell, I., Holden, L. & Claydon, T. "Human Resource Management: A Contemporary Approach", 4th Edition, Pearson Education Limited, UK, 2004
3. Bratton, J. & Gold, J. "Human Resource Management: Theory and Practice" 4th Ed., Palgrave Macmillan, NY, 2007
4. Cranet Survey on Comparative Human Resource Management, International Executive Report 2005, Cranet 2006 [<http://www.ef.uns.ac.rs/cranet/download/internationalreport2005-1.pdf>]
5. Cranet Survey on Comparative Human Resource Management, International Executive Report 2011, Cranet 2011, [http://www.ef.uns.ac.rs/cranet/download/cranet_report_2012_280212.pdf]
6. Dearden, L., Reed, H. & Van Reenen, J. "The impact of training on productivity and wages: Evidence from British panel data", *Oxford Bulletin of Economics and Statistics* 68(4), 2006, pp.397-421
7. Flannery, J., Stasi, K., Nolan, M., Davies, S., McKee, K. & Warnes, T. "Experiencing training: the need for a detailed investigation", *Working with Older People*, Vol. 9 (1), 2005, pp.13-16
8. Hansson, B. "Company-based determinants of training and the impact of training on company performance: Results from an international HRM survey", *Personnel Review* 36(2), 2007, pp. 311-31
9. Holden, L. & Livian, Y. "Does strategic training policy exist? Some evidence from ten European countries", *Personnel Review* 21(1), 1992, pp.12-23
10. Holzer, H., Block, R., Cheatham, M. & Knott, J. "Are training subsidies for firms effective? The Michigan experience", *Industrial and Labor Relations Review* 46(4), 1993, pp. 625-36
11. Kalleberg, A.L. & Moody, J.W. "Human resource management and organizational performance", *American Behavioral Scientist* 7(37), 1994, pp. 948-62
12. Kim, Y. & Ployhart, R.E. "The effects of staffing and training on

- firm productivity and profit growth before, during, and after the great recession”, *Journal of Applied Psychology*, Vol.99 No.3, 2014, pp.361-389
13. Мајовски, И. “Влијанието на стратешкиот менаџмент на човечки ресурси врз организациските перформанси кај деловните субјекти во Република Македонија“, докторска дисертација, Економски Институт-Скопје, 2010
 14. Mullins, L. “Management and Organisational Behaviour” (9th Ed.) Prentice Hall, London, England, 2010
 15. Noe, R. “Employee training and development” (5th Ed.) New York: McGraw–Hill, 2010
 16. Pfeffer, J. “Competitive Advantage Through People: Unleashing the Power of the Workforce”, Harvard Business School Press, Boston, 1994
 17. Strack, R., Caye, J.M., Thurner, R. & Haen, P. “*Creating people advantage in times of crisis: how to address HR challenges in the recession*”, Boston Consulting Group & European Association for People Management, 2009, [<http://www.thebostonconsultinggroup.es/documents/file15460.pdf>]
 18. Torrington, D., Hall, L. & Taylor, S. “Human Resource Management”, 6th Ed., Pearson Education Ltd., UK, 2005
 19. Ulrich, D. & Smallwood, N. “Human resources’ new ROI: Return on intangibles” in Losey, M., Meisinger, S. & Ulrich, D. (Eds) “The Future of Human Resource Management: 64 Thought Leaders Explore the Critical HR Issues of Today and Tomorrow”, John Wiley & Sons, Inc., NJ, 2005

NATASHA DANILOSKA*

INSURANCE IN AGRICULTURE- SITUATION IN THE REPUBLIC OF MACEDONIA

Abstract

Agricultural production faces many risks that makes agriculture a notoriously risky business. Issues of high price risk caused by potential price instability and production risk resulting from variations in the levels of production that primary producers can achieve from their current activities, are the main concerns to the agricultural sector. This is especially highlighted in developing countries where agricultural producers are severely exposed to uncertainties of the weather, prices, disease and socio-economic environment that makes them live in extreme uncertainty and on the line of survival. It is clear that risk management in agriculture is a crucial issue. In this sense, insurance, as a market based risk management instrument, is of great importance for agriculture, particularly in developing countries.

Objectives of this paper are to review and analyze conceptual framework of agricultural risk management and insurance, as a risk management strategy. Focus will be given to the situation with agricultural insurance in the Republic of Macedonia. At the end of the paper, conclusions and some recommendations will be drawn.

Key words: risk management in agriculture, agricultural insurance, Republic of Macedonia

JEL Classification: Q10, G22, G31, Q18, Q19

* Ph.D., Associate professor at the Institute of economics, University of "Ss Cyril and Methodius", Skopje, Republic of Macedonia, natasha.daniloska@ek-inst.ukim.edu.mk

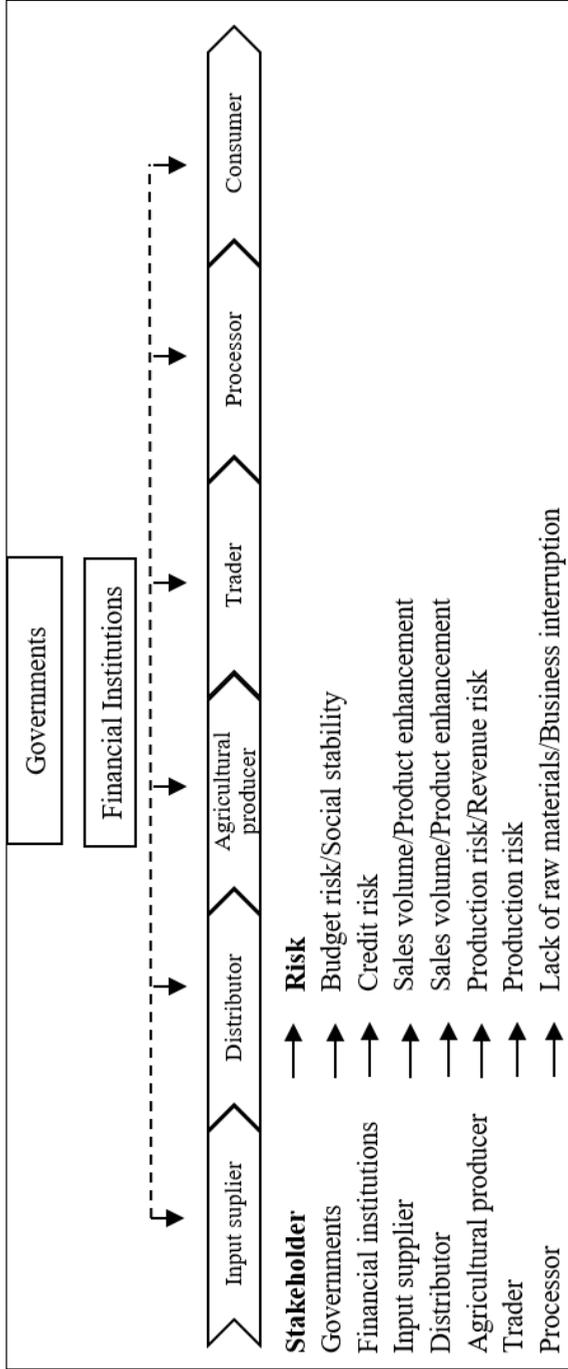
Introduction

Agricultural producers make decisions every day that affect their operations. Many of the factors that influence the decisions they make cannot be predicted with complete accuracy-this is risk. Agriculture as a production with biological characteristics and depended on the climate conditions, is predetermined to be risky, but its riskiness rise as it becomes more market-oriented. Nowadays, two major risks that concern agricultural sector are price risk due to liberalization of trade and production risk caused by the effects of climate change. In the modern dynamic environment, both in natural and socio-economic aspect, it is likely that these major risks will increase in the future.

As the agricultural production is subject to many uncertainties, thus it is typically associated with multiple potential outcomes with different probabilities. Weather, market developments and other events cannot be controlled by the agricultural producers but have a direct incidence on the returns of its activities. In this context, producers, although well known by their rigid live and management philosophy, have to manage agricultural risk as part of the general management of the agribusiness. Hazards and unforeseen events occur in all economic and business activities and are not specific to agriculture. However, agricultural risk and risk management instruments in the sector do have a certain number of specificities.

One of the main specifics of agricultural risks is their wide range of impact. Being that agriculture is complex activity, depended on many other sectors in the economy, agricultural risks have negative repercussion to the whole agribusiness value chain. Together with the agricultural producers, each of the participants along the supply chain, from the suppliers of inputs to the end consumer, are affected by these risks. In addition, as the interconnections between the participants are becoming more close and complex, negative risk effects tend to spread faster and easier. On Figure 1 we can see the conections and risks faced by each participant in the agricultural value chain.

Figure 1. Value chain and risks in agriculture



Source: Ramiro Iturrioz: Agricultural Insurance, Primer series on insurance, Issue 12, The World Bank, November 2009, p. 2.

Figure 1 clearly shows that the number of subject affected by the agricultural risks justify all resources and efforts invested into their management. Risk management strategies in agriculture are as complex and the sector itself. However, they all start with decisions of the agricultural producer: on the set of outputs to be produced, the allocation of land, the use of other inputs and techniques, including irrigation and the diversification of activities on and off-farm. Agricultural producers can also manage risk through market instruments which include insurance and futures markets. In this paper focus will be given to the agricultural insurance, both as agricultural policy instrument and a veritable tool that agricultural producers can potentially use to adapt and even mitigate the risks associated with adverse risk events.

1. TYPES OF RISK IN AGRICULTURE AND ATTITUDE OF AGRICULTURAL PRODUCERS TOWARDS THE RISK

Risk in agriculture is an everyday issue. Since the production is mostly carried out in the open air, and always entails the management of genetically variable living plants and animals, agriculture is especially exposed to risk. Risk affects production such as changes in the weather and the incidence of pests and diseases. Equipment breakdown can seriously endanger production and market price fluctuations can make it not economic. With sudden changes in interest rates, borrowing money can also be risky, as can high collateral demands. Risk also occurs as a result of changes in government policies. Such risks often have a major impact on the income from agricultural activity. Finally, there are risks related to the health and wellbeing of the agricultural producer and his family and the supply of labour, particularly regarding seasonal workers. Thus, risks and sources or risks that are relevant in agriculture have different characteristics, thus they can be classified in very different ways.

One of the basical classifications of agricultural risks is their categorization into 2 groups: systematic and unsystematic risks, as given in Table 1.

Table 1: Types of risks during agricultural production

Type of risk	Description
<i>Systematic agricultural risk</i>	
Production	Climatic aspects, plant and animal diseases
Market	Uncertainties about prices for both inputs and outputs
Institutional	Policy changes
Financial	Interest and exchange rate movement
<i>Unsystematic agricultural risk</i>	
Assets	Loss or damage of assets because of fire, accidents or theft
Operational	Uncertainties and risks related to health and personal

Source: Adaptation from: Danuletu Adina Elena, Danuletu Dan Constantib, Barna Flavia: Agricultural Insurance In Romania, Annals of Faculty of Economics, University of Oradea, Faculty of Economics, vol. 3(1), May, 2009, pp. 169-175

Systematic risks such as production, market, institutional or financial are unforeseeable and uncontrollable, while unsystematic risks like assets or operational happen randomly, have isolated effect and can be controllable. There are many other classifications of risks that can affect agriculture. Some scientific approaches prefer to stress more the specifics of agriculture and make differentiation between risks that are common to all businesses and risks that affect agriculture more specifically.² Another particular view on risk management in agriculture is the one that makes differences regarding developing countries. This approach includes non-agricultural specific risks in the classification and lists six different types of risks: natural, health, social, economic, political and environmental. When the assessment of this six types of risks is intended for developing countries, they need to be crossed with an additional dimension of systemic characteristics of different risks: Micro or idiosyncratic risk that affects the individual, Meso-risk affecting a whole community, and Macro or systemic risk affecting a whole region or country. As a result of the interaction of individual agricultural risk with certain systemic dimension, most of these risks eventually take the form of economic risk, implying that an individual agricultural producer may be facing very different risks at the same time.³

² Moschini, G., Hennessy, D. A.: Uncertainty, risk aversion, and risk management for agricultural producers. In Gardner, B. and G. Rausser (eds.) Handbook of Agricultural Economics vol. 1. Elsevier Science B.V, 2001, pp. 48-53.

³ World Bank Publications: Managing Agricultural Production Risks: Innovations in Developing Countries. World Bank, Agriculture and Rural Development Department,

Another specific related to the agricultural risks is that agricultural producers differ in the degree to which they accept the risk. Some agricultural producers are willing to accept more risk than others, and thus they may be divided into three types:⁴

- Risk-averse agricultural producers-they try to avoid taking risks and usually are more cautious individuals with preferences for less risky sources of income.
- Risk-takers agricultural producers-are people who are open to more risky business options and choose the alternative that gives some chance of a higher outcome, even though they may have to accept a lower outcome.
- Risk-neutral agricultural producers- lies between the risk-averse and risk-taking positions.

These differences in attitudes of agricultural producers towards risk are often related to their financial ability to accept a small gain or loss. It also determines their acceptance of insurance as a strategy to manage the risk.

2. INSURANCE AS A STRATEGY FOR RISK MANAGEMENT IN AGRICULTURE

Regardless of the approach that will be used to classify agricultural risks, general conclusion and notorious fact is that they exist and they are many so the most logical issue to discuss next is how the party (or parties) at risk can seek to manage that risk. Before we start this discussion, it is very important to point out that risk management in general, and particularly in agriculture, should be planned before realization of an event, that is on an

Report No. 32727. The World Bank. Washington, DC., 2015, pp. 72-78.

⁴ Bard, S.K., Barry, P.J.: Developing a scale for assessing risk attitudes of agricultural decision makers, *International Food and Agribusiness Management Review* 3:9-25, 2000, p. 11.

ex-ante basis. Namely, managing realized risks on an ex-post basis only is not considered to be risk management, after all, if something has already happened, it is no longer a risk, although a future reoccurrence might be. There is a great deal of literature on the subject of risk management and a surprisingly large amount of differing terminology in use. For the purposes of this paper on the issue of risk management in agriculture, we will use the terminology of World Bank, according to which three separate approaches to risk management are considered:⁵

- Mitigation is the lessening or limitation of the adverse impacts of hazards and related disasters. Risk mitigation options in agriculture are numerous and varied (for example, crop and livestock diversification, income diversification, soil drainage, mulching, use of resistant seeds, avoidance of risky practices, and crop calendars).
- Transfer refers to the transfer of the potential financial consequences of particular risks from one party to another. While insurance is the best-known form of risk transfer, in agricultural sectors in developing countries the use of informal risk transfer within families and communities is extremely important.
- Coping refers to improving the resilience to withstand and manage events, through ex-ante preparation and making use of informal and formal mechanisms in order to sustain agricultural production and livelihoods following an event. Although we have noted that coping is an ex-post activity, it is possible to plan and to prepare for coping activities on an ex-ante basis. This is often fiscally beneficial, as the ability to quickly respond to events often reduces losses.

At this point, we will mention that there is a fourth risk management approach, so called risk avoidance or risk prevention (that is rarely possible in agricultural production, especially in developing countries where there are very few alternative sources of nonfarm employment),⁶

⁵ World Bank Publications: Helping poor People Manage Risk, The World Bank. Washington, DC., 2005, p.32

⁶ Cafiero, C., F. Capitanio, A. Cioffi and A. Coppola: Risk and Crisis Management in the Reformed European Agricultural Policy, Canadian Journal of Agricultural Economics,

but as intended, in this paper focus will be given to insurance as a strategy for risk management in agriculture.

Agricultural insurance is a special line of property insurance applied to agricultural producers and it not limited only to crops, but also applies to livestock, bloodstock, forestry, aquaculture and greenhouses. There are several features of this type of insurance that makes it being treated as a special line of business. Most prominent reasons for this include difficulties in achieving adequate diversification because of the nature of the risk, asymmetries of information in underwriting, the geographical dispersion and complexity of agricultural production. Additionally, the cause-and-effect relationships in agriculture are not always easily observable. There are many variables that affect agricultural production, not all of which are insurable, so the agricultural insurer must be able to establish the link between a loss that is insurable and the cause of the loss. All this features validate that agricultural insurance requires skilled and expert underwriting. This special expertise is needed to understand the biological and technical processes not only to set premiums commensurate with the risk but also to assess the producers' own risk management practices and assist in improving them.

In recognition of the specialized nature of this type of insurance is the offer of insurance products. Agricultural insurance products can be classified into three main groups based on the method of determining how claims are calculated, as follows:⁷

- Indemnity Based Agricultural Insurance (insurance payouts based on the actual loss at the insured unit level)
- Index based Agricultural Insurance (insurance payouts based on an index measurement)
- Crop Revenue Insurance (insurance payouts based on yield measurement and crop prices)

Indemnity based agricultural insurance products determine claim payment based on the actual loss incurred by the policy holder. If an in-

N° 55: 419-441, 2007, p.433.

⁷ World Bank Publications: Managing Agricultural Production Risks: Innovations in Developing Countries. World Bank, Agriculture and Rural Development Department, Report No. 32727. The World Bank. Washington, DC., 2015, p. 49

sured event occurs, an assessment of the loss and a determination of the indemnity are made at the level of the insured party. The classification is often divided into two subclasses-*named peril* (damage-based products-provides indemnity against those adverse events that are explicitly listed in the policy) and *multiple peril* (yield based product-is a multiple peril crop insurance that provides insurance against all perils that affect production unless specific perils have been explicitly excluded in the contract of insurance) agricultural insurance. In named peril insurance contracts insurance claim is calculated by measuring the percentage of damage in the field soon after the damage occurs. Multiple peril insurance offers comprehensive cover to the producers but comes at significantly higher cost compared with named peril insurance.

Index based agricultural insurance products pay out based on the value of an „index”, not on losses measured in the field. The index is a variable that is highly correlated with losses and that cannot be influenced by the insured. Precondition for successful implementation of this subclass is that both parties to the contract have confidence in the objectivity and transparency of the index. Once the indexes have been created, further operational costs are low and this translates into lower premiums for insured parties. Typical application of this insurance product is trough Area yield index insurance-AYII, by which insurance contract defines an area referred to as the „insured unit”.

Crop revenue agricultural insurance products protect insured parties from the consequences of low yields, low prices or a combination of both. It is essentially multiple peril crop insurance cover with a price hedge. This is a relatively new sub-class and moves away from more traditional products where the insurable interest is the size of the crop to products where the interest is a revenue stream.

Having in mind the complexities of agricultural insurance, it is clear that design and development of suitable and affordable agricultural insurance programs require innovation and action from both the public and the private sectors.

Where governments choose to intervene, they may adopt different approaches but the most common mechanisms for public sector involvement in agricultural insurance markets are:⁸

⁸ Mahul, O & Stutley, CJ: Government support to agricultural insurance: challenges and options for developing countries, World Bank, Washington, D.C., 2010, p.67.

- Premium subsidies, as the most common type of public sector support to agricultural insurance.
- Investment in product research and development (R&D), training and information gathering.
- Agricultural insurance legislation as special legislation for crop and livestock insurance.
- Public sector reinsurance.
- Administration cost subsidies as a less common practice of public sector support to agricultural insurance.

Involvement of the public sector is critical to ensure that agriculture insurance programs meet the needs of small-scale farmers while ensuring the sustainability of financial providers. Namely, while agricultural insurance is essentially a commercial activity, it is, nevertheless, common to see governments playing a role in the industry. Governments have an interest from the perspective of maintaining productivity for the economy and safeguarding the wellbeing of the rural community. Government presence in the market fills a void left by the private sector which is sometimes reluctant to enter this market segment due to high start up costs, high distribution and administrative costs and a lack of capacity caused by difficulties in obtaining reinsurance.

3. AGRICULTURAL INSURANCE IN THE REPUBLIC OF MACEDONIA

Agriculture is one of the leading sectors in Macedonian economy. Data in the table below shows that big share of national territory is used for agricultural production. Also, big part of the population provides for live from agricultural activities.

Table 2. Basic indicators for Macedonian agriculture

Total area	25.713 km ² ; (41% of the total is agricultural area/ 1/3 is classified as farmland)
Share of the primary agriculture including the sectors of Hunting and Forestry in GDP	9, 40%
Workforce in the agricultural sector	167.992 (18%)

Number of agricultural holdings		170.885
Total share in international trade	Import	19%
	Export	13%

Source: State statistical office, 2015

In same time, to the notorious fact for agriculture being a risky business, we must add that in the last decades, Macedonia has been affected by the climatic changes. That has results in incensement of middle temperatures, decrease of humidity, as well as sudden and extreme weather changes (draught, hot flashes and forest fires, frosts). In order to help to the agricultural producers to manage this risks, in 2008 Government of the Republic of Macedonia, within the national agricultural policy, introduced insurance subsidies. Namely, as a preventive measure to reduce potential damage and loss to the agricultural producers, caused primarily from the impact of bad weather conditions, starting from 2008 onwards, Macedonian Government regularly provides financial support for co-financing the insurance policy. The insurance subsidy program started with 30%, but by 2013 arrived at 60% of the amount of the insurance premiums that any agricultural producer (holding) will purchase in order to protect its production from the negative impact of major risks. This subsidized percentage covers only defined crops and defined maximum area insured per user, that are as follows:⁹

- 10 hectares of vineand fruit plantations;
- 2 hectares of horticultural crops;
- 2 hectares of tobacco;
- up to 20 hectares of crops and
- up to 100 beehives.

The amount of subsidy cannot exceed 60% of the cost of the insurance premium for compensation of damage to the agricultural production occurred as a result of adverse climatic event, but not more than 200.000 MKD (3.253 EUR) per agricultural producer (household).¹⁰

⁹ Republic of Macedonia, Ministry of Agriculture, Forestry and Water Economy: National Strategy for agricultural and rural development 2013-2010, Skopje, December, 2014, p. 229.

¹⁰ Law on agriculture and rural development, Official Gazette of the Republic of

Beside insurance subsidies, for risk management Macedonian agricultural producers can apply for 50% of governmental co-financing on investment for protective equipment (hail nets and shading) and for efficient irrigation systems (drip, etc.).

Financial state support for subsidizing agricultural insurance premiums in Macedonia has been increased gradually, and so in 2013 was 568 000 EU and by 2016 it arrived at nearly 1.130.000 EU.¹¹

In its effort to support and foster agricultural insurance, Republic of Macedonia in 2012 joins to the regional programme created to address very low levels of catastrophe and weather risk insurance penetration in Southeastern Europe. Activities are managed by the Europa Reinsurance Facility Ltd. (Europa Re), a Swiss-based specialty property catastrophe reinsurance company owned by countries of Southeastern Europe (SEE). On 15 September, 2014, this Company presented the first Area Yield Index Insurance (AYII) product for protection of specific crops in the Macedonian agriculture sector. The AYII product became operational in 2015 and is sold by certified local insurance companies that participate in Europa Re programme. Europa Re provides appropriate expertise, technical support and quality reinsurance for all policies issued by local partner insurance companies. By providing an opportunity to agricultural producers to insure the expected yields of their crops, AYII aims to protect agricultural producers from all types of adverse weather risks, such as drought, floods, frost, torrential rains, hail and other risks, which affect wider areas (e.g. municipalities) and can significantly reduce crop yields.

In same time, Macedonian insurance industry can be described as small and underdeveloped, but with a high potential for further growth and development. The structure of the insurance system of the Republic of Macedonia rests on the Law on Insurance Supervision¹² complemented by other laws and bylaws that are harmonized with EU's insurance legislation.

In 2009, national Insurance Supervision Agency was established as an independent body whose competence and authorizations are in the field of guaranteeing lawful and efficient functioning of the insurance market

Macedonia, No. 49/2010; 53/2011, 126/2012, 15/2013 и 69/2013, Article 98

¹¹ National program for agricultural and rural development 2013-2017, Official Gazette of the Republic of Macedonia, No. 134/2012., p. 16.

¹² Law on Insurance Supervision, Official Gazette of the Republic of Macedonia, No. 27/2002, 98/02, 79/07, 88/08, 67/10, 44/11, 112/11, 188/13, 30/14, 43/14, 112/14, 153/15 и 92/15),

for the purpose of protecting policyholders' rights. Insurance Supervision Agency (ISA) is the key state regulatory body that controls the insurance market in Macedonia. Currently, on the insurance market in Republic of Macedonia are active 15 Insurance undertakings (11 non-life and 4 life), 30 Insurance brokerage companies, 10 Insurance agencies and 2 Banks which acts as insurance agency. Until to 2015, 6 out of 11 insurance companies for nonlife insurance perform business in agriculture insurance line of business. Namely, till 2013 only 4 insurance undertakings were offering products for agricultural insurance, and in 2014 two other companies began selling policies for agricultural insurance.¹³

Insurance products available to the Macedonian agricultural producers are crop insurance, livestock insurance and agriculture yield index insurance (AYII), are the Crop insurance covers basic risk (hail, fire and thunder) and additional risks (spring ice, flood and storm) and subject to the insurance contracts are:¹⁴

- crops and fruit,
- meadow grasses,
- herbs,
- ornamental plants,
- fruit,
- vine and forest seedlings,
- young orchards and vineyards before entering the race,
- young forest plants and
- plaiting willows and reeds vine yards.

Within the animal insurance, almost all domestic animals (equidae, cattle, pigs, sheep and goats, feathery animals, cats and dogs), bees, fish and exotic animals) can be insured against following risks:¹⁵

¹³ INSURANCE SUPERVISION AGENCY: 2015-Annual Report on the insurance market in the Republic of Macedonia, Skopje, 2016, p.12

¹⁴ National program for agricultural and rural development 2013-2017, Official Gazette of the Republic of Macedonia, No. 134/2012., p. 38.

¹⁵ Ibid, p. 42

- Death due to accident or illness;
- Emergency slaughter;
- Health care expenses (if agreed as an additional coverage);
- Emasculation.

Regarding the agriculture yield index insurance (AYII), as mentioned previously, it is a multiple-peril loss of crop yield policy that insures against all climatic, naturally occurring and biological perils-it is an „all risks” loss of yield policy. This insurance product, for Macedonian agricultural producers utilizes measurement of potential losses of their crops caused by adverse weather based on the index of the average yield at a municipal level for each particular crop. In this way, the insured agricultural producers receive compensation for damages if the realized average yield at the municipality level in a given year is lower than the contractually agreed reference level of crop yields which in turn is set based on the historic yield average for the index municipality.

Even when 60% of insurance premiums are covered by the Macedonian Government, and with couple of insurance companies involved, yet, agricultural insurance in the Republic of Macedonia is not at satisfactory level.

According to the ISA, some dynamism in agricultural insurance, as a part of non-live (property) insurance can be seen just in last 3 years. Namely, out of 70.000 registered agricultural producers, in 2013 were signed 2.559 agricultural insurance contracts, in 2014 were signed 3.704 contracts and 2015 concluded with 5.021 agricultural insurance contracts. Total participation of Gross written premiums (GWP) for the year 2014 was 114.52 million MKD and for 2015 GWP was 181, 83 million MKD. If we compare year 2014 and 2015 both in terms of signed contracts and GWP, we can see an increase of 58.78% in the realized GWP with growth of 35, 56% in the number of contracts. In the segment of property insurance, agricultural insurance has a share of 33, 21% and 211, 38 million MKD Gross paid claims total amount.¹⁶

Table 3. Share of agricultural insurance by peril in Gross written premium in Republic of Macedonia, for 2015

¹⁶ INSURANCE SUPERVISION AGENCY: 2015-Annual Report on the insurance market in the Republic of Macedonia, Skopje, 2016, pp.15-16.

	Share in GWP-property insurance	Share in total nonlife GWP
Crop insurance	5, 48%	1, 12%
Fire	0, 18%	0, 04%
Flood	0, 00%	0, 00%
Hail and frost	5, 30%	1, 09%
Other property insurance	22, 83%	4, 67%
Fire	14, 04%	2, 87%
Earthquake	4, 58%	0, 94%
Flood	2, 32%	0, 48%
Hail and frost	1, 89%	0, 39%

Source: ISA, 2015

On Table 3. are given shares of agricultural insurance by peril in Gross written premium in the Republic of Macedonia for 2015 and can be concluded that it is only 1.2 % in total insurance. Contracts are predominantly made against hail and frost, while in property insurance, fire is most insured peril. In the structure of agricultural insurance, dominant is fruit production with 350 ha. of vineyards and apple with 270 ha., followed by wheat on about 210 ha.¹⁷ This imply that the risks in agricultural production are very large, and the insurance companies are often reluctant to provide insurance of agricultural production, or if they do it, they do it with a high premium rates that affect dissimulating for individual farmers and legal entities engaged in agriculture to ensure their production. This entire situation indicates that insured agricultural area is relatively small in relation of total agricultural area, quantities of Macedonian agricultural production, number of agricultural producers and the opportunities afforded by the program for financial support in agriculture by subsidizing insurance premiums.

Conclusion

The sources of risk in agriculture are numerous and diverse and they expose agricultural producers, suppliers, distributors, financial institutions and governments to potential losses. Many approaches can be

¹⁷ Zoran Stojanovski: Agricultural insurance in Macedonia, Paper presented at the IIF 2015-Property Insurance in a Stormy Era, Munich, June, 2015.

used to manage agricultural risks. One of the possible risk management strategies is the risk transfer or agricultural insurance.

Regarding the situation in the Republic of Macedonia, unfortunately, despite governmental subsidy of 60% of insurance premiums, the insurance of agriculture is not giving satisfactory results. Although the agriculture in the structure of GDP of the Republic of Macedonia is 12%, still insurance in agriculture in the country in total premium paid for insurance in the Republic of Macedonia is only 1.2 %, suggesting that the risks in agricultural production are very large. With less than 1, 5% of insured agricultural producers in the country, we can say that they are still very vulnerable to weather risks, especially because the government has not created an effective system for protection from negative natural influences i.e. drought, flood, hail, fire etc. This makes the money spend for subsidizing agriculture not efficient since they are not sufficient to cover the damage. Existing insurance packages offered at the Macedonian insurance market are against hail, but not protection against drought or. Also, insurance companies either avoid dealing with agricultural insurance, or they carry a high premium rates that are quite unaffordable and thus dissimulating for agricultural producers.

In order to increase the interest of Macedonian agricultural producers for insuring their production, it is necessary to educate and inform them about the positive aspects of insurance, especially for agriculture yield index insurance (AYII). Spending from national budget should be in building modern infrastructure that can provide valued, accurate historical and forecasted data of weather and market, enhancing legal and regulatory system and providing educational programs to agricultural producers. In addition, insurance companies should consider lowering their premium rates and engage experts who would professionally assess the damages of the eventual natural disasters.

At the end, it must be pointed out that even when there are many institutional agricultural insurance systems and market products, insurance is not the universal solution to the risk and uncertainties that agricultural producers face. It can only address part of the losses resulting from some perils and most certainly not all risks that threats modern and global agriculture. In fact, it would even be wrong since it would be a linear approach considering only a specific source of risk, a specific strategy, or a specific policy measure, that is likely to result in inefficient choices. Risk management in agriculture should be analyzed as a system in which there is interaction be-

tween many elements and complemented the set of outputs to be produced and political measures and instruments to be employed, the allocation of land, the use of other inputs and techniques, including irrigation and the diversification of activities on and off-farm.

References:

1. Bard, S.K., Barry, P.J.: Developing a scale for assessing risk attitudes of agricultural decision makers, *International Food and Agribusiness Management Review* 3:9-25, 2000.
2. Cafiero, C., F. Capitanio, A. Cioffi and A. Coppola (2007), —Risk and Crisis Management in the Reformed European Agricultural Policy, *Canadian Journal of Agricultural Economics*, N° 55: 419-441.
3. Danuletu Adina Elena, Danuletu Dan Constantib, Barna Flavia: Agricultural Insurance In Romania, *Annals of Faculty of Economics, University of Oradea, Faculty of Economics*, vol. 3(1), May, 2009.
4. INSURANCE SUPERVISION AGENCY: 2015-Annual Report on the insurance market in the Republic of Macedonia, Skopje, 2016
5. Law on agriculture and rural development, *Official Gazette of the Republic of Macedonia*, No. 49/2010; 53/2011, 126/2012, 15/2013 и 69/2013
6. Law on Insurance Supervision, *Official Gazette of the Republic of Macedonia*, No. 27/2002, 98/02, 79/07, 88/08, 67/10, 44/11, 112/11, 188/13, 30/14, 43/14, 112/14, 153/15 и 92/15),
7. Mahul, O & Stutley, CJ: Government support to agricultural insurance: challenges and options for developing countries, *World Bank, Washington, D.C.*, 2010
8. Moschini, G., Hennessy, D. A.: Uncertainty, risk aversion, and risk management for agricultural producers. In Gardner, B. and G.

- Rausser (eds.) Handbook of Agricultural Economics vol. 1. Elsevier Science B.V, 2001
9. National program for agricultural and rural development 2013-2017, Official Gazette of the Republic of Macedonia, No. 134/2012.,
 10. Olivier Mahul: Agricultural Insurance for Developing Countries-The Role of Governments, Pluriagri conference on Insuring Agricultural Production, Paris, France December 18, 2012.
 11. Ramiro Iturrioz: Agricultural Insurance, Primer series on insurance, Issue 12, The World Bank, November 2009.
 12. Republic of Macedonia, Ministry of Agriculture, Forestry and Water Economy: National Strategy for agricultural and rural development 2013-2010, Skopje, December, 2014
 13. Trajan Dojchinovski: The situation with insurance of crop production in the Republic Macedonia and the EU Member States and the USA, IJISSET-International Journal of Innovative Science, Engineering & Technology, Vol. 1 Issue 10, December 2014. pp. 593-598.
 14. World Bank Publications: Helping poor People Manage Risk, The World Bank. Washington, DC., 2005.
 15. World Bank: Managing Agricultural Production Risks: Innovations in Developing Countries. World Bank, Agriculture and Rural Development Department, Report No. 32727. The World Bank. Washington, DC., 2015.
 16. Zoran Stojanovski: Agricultural insurance in Macedonia, Paper presented at the IIF 2015-Property Insurance in a Stormy Era, Munich, June, 2015.

ELIZABETA DJAMBASKA*
VLADIMIR PETKOVSKI**
ALEKSANDRA LOZANOSKA***

**CAPITAL MARKET AND THE DETERMINANTS OF
DEVELOPMENT IN THE REPUBLIC OF MACEDONIA**

Abstract

This paper considers the capital market in the Republic of Macedonia. The analysis identifies and explains whether capital market development is influenced by economic growth. The focus of the paper is to determine the effects of different factors on the capital market development in the Republic of Macedonia. For these purpose a multivariate linear regression is conducted using the data from 1997-2013. The analysis indicates that the capital market in the Republic of Macedonia is small and underdeveloped. Therefore the economic growth factors taken into consideration for the research have not shown considerable impact on the capital market due to its underdevelopment.

Key words: Capital Market, Market Capitalization, Calderon-Rossell model, regression, Republic of Macedonia

JEL classification: P340, G10, O16, C3

* Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: beti@ek-inst.ukim.edu.mk

** Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: vladimir@ek-inst.ukim.edu.mk

*** Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: sandra@ek-inst.ukim.edu.mk

Introduction

This paper considers the development of the capital market in the Republic of Macedonia with the attempt for estimating the impact of factors that have influence on its development. Economic development of the country is important factor and precondition for capital market development. Theoretical approach about the development of the capital market and the determination of the factors is the basis for determining their impact for the development of the capital market in the Republic of Macedonia. Therefore, the main goal of the research is to evaluate the influence of economic growth, development of the financial sector, macroeconomic stability, gross investments and gross savings on capital market development in the Republic of Macedonia.

1. LITERATURE REVIEW AND THEORETICAL FOUNDATION FOR THE STUDY

There are a lot of studies that analyze the development of the capital market. Very interesting segment for researchers are the determination of the factors that influence its growth. Every study takes in consideration different aspect of the analysis.

This fact is well acknowledged and a lot of studies that analyze this relationship confirm the existence of a positive and significant relationship between capital market development and economic growth and development. According to Bekaert G. and Harvey C.¹ economic growth in a modern economy hinges on an efficient financial sector that pools domestic savings and mobilizes foreign capital for productive investments. The findings from Caporale G., Howelts A. and Soliman M.² indicate that a well-developed stock market can foster economic growth in the long run through faster capital accumulation, similar to findings of King and Levine³ and Levine and Zervos.⁴

¹ Bekaert G., Harvey C. Emerging Equity Market Volatility, Journal of Financial Economics, Elsevier, 1997, No. 43. 29-77.

² Caporale M. Howells G. P., Soliman A.M., Stock Market Development and Economic Growth: The Causal Linkage, Journal of Economic development 33 Volume 29, Number 1, June 2004

³ King R. G., Levine, R., Finance and Growth: Schumpeter May Be Right, The Quarterly Journal of Economics, Volume 108, Issue 3, 1993p. 717-737.

⁴ Levine, R., Zevros, S., Stock Markets, Banks and Economic Growth, American Economic Review, Vol. 88, 1998 pp. 536-558.

A considerable amount of empirical research has been conducted on the effect of stock market on the level of economic growth (Atje and Jovanovic,⁵ Demirgüç-Kunt and Maksimovic,⁶ Levine and Zervos⁷). However according Fink G. Haiss P. and Sirma H.,⁸ previous literature on the finance growth has largely ignored the bond market despite it being an essential source of external finance.

The most empirical paper on finance growth considered the role of the banking sector in economic growth. Oya and Damar⁹ identify that previous studies focused mostly on the size of the financial sector as commercial bank deposits as a percentage of GDP, without making much inference on the role of the capital market as a major contributor to financial sector growth in the economy.

Different authors use different methods for calculating the impact of capital market development on economic development and vice versa, but there approaches often have common features. Usually the studies are focused on the relationship between stock prices and macroeconomic indicators in developed countries like USA, Japan or Italy (Plachý R., Rašovec T.,¹⁰). The common conclusion is that stock market in the developed countries has a very strong relationship with interest rates, both in short-term and long-term.

The majority of the studies that observe the determinant of the capital market development, especially in the emerging economies, draw a common conclusion that the banking sector has dominant influence on the capital market development. In most of the studies the size, the level of development and scope of the banking sector have positive and signif-

⁵ Atje, R., Jovanovic, B., Stock Markets and Development, *European Economic Review*, 37 (2/3), 1993

⁶ Demirgüç-Kunt, A. Maksimovic, V. Stock Market Development and Financial Choices Of Firms, *The World Bank Economic Review*, Volume 10, Issue 2, 1996, p. 341-369.

⁷ Op. Cit. Levine, R., Zevros, S.

⁸ Fink G. Haiss P., Sirma H., Credit, Bonds, Stocks and Growth in Seven Large Economies, *EI Working Paper No. 70*, 2006

⁹ Oya P. A., Damar H.E., Financial Sector Depending and Economic Growth: Evidence for Turkey, *MPRA Paper No. 4077*, 2006 (posted 15 July 2007)

¹⁰ Plachý R., Rašovec T., Impact of economic indicators on development of capital market, *International Journal E+M*, 102 - 3, XVIII, 2015

ificant impact. (Yartey, ¹¹Kemboi J.K., Tarus, D.K., ¹²). But, in the literature there are evidence that the development of the banking sector, the activities of the Central Bank and other financial institutions interacted negatively with market capitalization which implies that the activities of those institutions deterred the development of the capital market.¹³

In the study of Yartey, ¹⁴ the author exams macroeconomic and institutional indicator using a panel data of 42 emerging economies for the period 1990 to 2004. The findings from this paper are that macroeconomic factors such as income level, gross domestic investment, banking sector development, private capital flows, and stock market liquidity are important determinants of capital market development in emerging market countries. The results also show that political risk, law and order, and bureaucratic quality are important determinants because they enhance the viability of external finance.

The capital market development in Republic of Macedonia and the factors that affect it have been the subject of research in the several studies.

In the study of the Hadzi-Mishev R., ¹⁵ is constructed a model for the macroeconomic determinants of the trends of the Macedonia Stock Exchange. The study covers and analyses empirical literature and formulates a standard regression equation in which the dependent value that reflects the development of the capital market is the value of MBI-10 and the independent variables that are taken into consideration are inflation, interest rates, industrial production and money supply. The results of empirical analysis confirm the expected positive relation between the value of MBI-10 and the level of industrial production and money supply on one hand, and the inverse relationship between interest rates and inflation, on the other.

¹¹ Yartey, C.A., The Determinants of Stock Market Development in Emerging Economies: Is South Africa Different?, IMF Working Paper, WP/08/32, 2008

¹² Kemboi J.K., Tarus, D.K., Macroeconomic Determinants of Stock Market Development in Emerging Markets: Evidence from Kenya, Research Journal of Finance and Accounting, ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online), Vol 3, No 5, 2012

¹³ Idowu, A., Babatunde, M.A., Effect of Financial Reforms on Capital Market Development in Nigeria, Asian Journal of Business and Management Sciences, Vol. 1 No. 8, 2012, p. 44-52.

¹⁴ Op. Cit. Yartey, C.A.

¹⁵ Hadzi-Mishev R., Limit of effective portfolios of the Macedonian Stock Exchange, website of the Macedonian Stock Exchange, 2011

Eliskovski M.¹⁶ (2012), in his study analyses the development of the capital market in Republic of Macedonia, through its size and depth, with the effects of the GDP, investment, development of the banking sector and macroeconomic stability. „The results for the first specification indicate that in Republic of Macedonia the gross investment and macroeconomic stability have a major impact on the size of the capital market. It is interesting to emphasize that the development of the banking sector have complementary and not substitutable effect.”¹⁷

The challenge is to attain a sustainable capital market in an emerging economy like Republic of Macedonia, which would lead to a sustainable growth and development. Previously mentioned papers were taken into consideration as a basis for preparing empirical analysis in this paper, considering the macroeconomic indicators that influence and determine the capital market development.

2. DETERMINANTS OF THE DEVELOPMENT OF THE CAPITAL MARKET IN THE REPUBLIC OF MACEDONIA (DATA, METHODOLOGY AND RESULTS FROM THE EMPIRICAL ANALYSIS)

The estimation of the development of capital market usually used Calderon-Rossell behavioral structural model. The basic model considers that the development of the capital market is the function of the GDP per capita and Turnover Ratio. The equitation model is:

$$\text{Market capitalization} = f(\text{GDP, per capita, Turover Ratio})$$

The determination of macroeconomic factors that influence the development of the capital market in this paper is done with the extended Calderon-Rossell model. The extended model includes more variables that have influence on the capital market. These variables reflect the relationship among economic growth, national savings and the available capital for investment, macroeconomic stability, development of the financial sector and the capital market. This modification of the model is done in order to get a better specifications and more comprehensive model which

¹⁶ Eliskovski M., Macroeconomic determinants of development of the capital market in the Republic of Macedonia, 2012

¹⁷ Ibid, p. 23

determines the intensity of the influence of the previously stated variables on the development of capital market.

Development of the capital market in the Republic of Macedonia is influenced by the impact of several factors.

Economic growth is considered to be the main precondition for the development of the capital market. The expansion of the economic activity increased GDP. This has positive impact on the company's profits and consequently leads to increase of their value on the capital market. In the long term, the increase in gross domestic product - creates the need for new financial instruments for economic agents in order to fertilize their income at a given level of risk. The variable rate of economic growth used in the regression, represents the economic development in the Republic of Macedonia.

Higher economic growth leads to increased levels of national saving and investments. Increased savings also increases the potential for investment. The increased volume of saving and investment can be channeled through capital market into profitable projects and can have positive influence on the capital market. Empirical models usually evaluate the impact of national savings as % of GDP or gross investment as % of GDP on market capitalization. The regression in this paper estimates the impact of savings and investment on market capitalization using the variable gross savings as % of GDP.

The development of financial sector especially banking sector is very important for the development of capital market. Usually, the indicators of the financial sector development that are used in models are: volume of credits, deposits and monetary aggregates. Banking sector in Republic of Macedonia is considered as dominant part in the financial sector, so it is reasonable that the analysis include these indicators. The developed financial sector allows a wider and diversified range of financial instruments for investment of economic entities. Consequently there is an opportunity for higher diversification risk. Therefore, the development of the financial sector, especially the banking sector has positive impact on development of the capital market. These sectors are complementary and supplement each other. Sometimes the opposite situation is present, so the development of financial sector can have negative implications on capital market as a results of increased competition. The both sectors compete with each other for the prize of mobilizing the free capital of economic entities. In that case they represents substitutes.

In this study the financial sector and his influence on the capital market development is represent by the variable deposits interest rate. As was previously stated the banking sector is considered to be the dominant part in the financial sector in the Republic of Macedonia. Therefore, the deposits interest rate is the key factor that can influence the decision of the economic entities, whether to deposit their financial assets in the banks or to participate and invest in financial instruments in capital market. It can be assumed that the deposit interest rate will have negative impact on the development of the capital market, primarily due to the amount of the deposit interest rate and lower risk of investment in deposits.

Macroeconomic stability is present through the variable inflation rate or interest rate. The effects of macroeconomic stability on capital market development, using these variables can be determined as positive or negative. The inflation rate can be foreseen as appropriate indicator of macroeconomic stability, i.e. if the inflation rate is stabile it has positive influence on capital market development. On the other hand, the high inflation rate can create instability and high risk for the economic entities to participate and invest in the capital transactions. The other aspect is that high inflation rate encourages the speculative actions in trading with financial instruments. This activities can have positive influence on increasing the market capitalization and turnover ratio of the capital market.

These are the theoretically predictions about the expected influence of the variables on the market capitalization of the Macedonian Stock Exchange. After the applied statistical model the results for some of the variables confirm the theoretical prediction, but others defer from it. The conclusion and explanation are shown in the following section.

3. DATA, METHODOLOGY AND RESULTS FROM THE EMPIRICAL ANALYSIS

The development of the Macedonia Stock Exchange is estimates with multivariate linear regressions which determine and measures the influence of the several factors. The regressions are conducted using data from the World Bank for the period 1997-2012. The calculations of statistical parameters are obtained using the software package XLSTAT 2015.

The regression takes into consideration the market capitalization as dependent variable that is the indicator of the size of the Macedonia capital market, expressed as a percentage of GDP. Independent

variables that explain the depended variable taken into consideration in this model are:

- Y - Market capitalization (as % of GDP)
- X_1 – Gross savings (as % of GDP)
- X_2 – Deposit interest rate
- X_3 - Inflation Rate (Consumer Price Index)
- X_4 - GDP growth;
- β_0 – Free article;

The model is transformed into lin-log linear model and the mathematical equation has the following expression:

$$\ln Y = \beta_0 + \beta_1 \ln(X_1) + \beta_2 \ln(X_2) + \beta_3 \ln(X_3) + \beta_4 \ln(X_4)$$

The estimation of the parameters of statistical analysis in the model is done using the method of least squares. Significant assumption that is considered in the interpretation of the regression parameters are multicollinearity, heteroscedasticity and autocorrelation statistical errors.

Table 1 Results from the regression

Independent variables - X	(1)
X_1 – Gross savings (as % of GDP)	-1, 612 (-1, 306)*
X_2 – Deposit interest rate	-5, 769 (-6, 259)***
X_3 - Inflation Rate (Consumer Price Index)	0, 080 (0, 338)
X_4 - GDP growth;	-0, 663 (-1, 111)*
Number of observations (n)	16
R^2	0, 873
Adjusted R^2	0, 801
Durbin - Watson	1, 669

*-10% level of confidence; ** - 5% level of confidence and *** - 1% level of confidence
Source: own calculations using the software package XLSTAT, 2015

The method of least squares shows that $R^2 = 0,873$ which is considered an acceptable criterion for correctness of the model. The diagram of distribution of residuals shows no presence of heteroscedasticity. (Annex number 1). The equation has the following form:

$$\ln Y = 18,13 - 1,61\ln(X_1) - 5,77\ln(X_2) + 0,080\ln(X_3) - 0,66\ln(X_4)$$

The evaluation of the model by the method of least squares R^2 shows that about 87 % (0, 873) of the variation in the dependent variable can be explained by variations of all independent variables included in the model. They have successfully determined the relative dependence of capital market development in the Republic of Macedonia. The results from the criteria for evaluation of the model, correlation matrix, and test for the multicollinearity and the estimated value for the parameters are presented in the annex number 2. The variables considered in the regression analysis passed the p-test for $p < 5\%$ with the exception of the variable which presents the inflation rate, thus it can be deducted that there isn't any degree of randomization in the link between the four variables and that the bond between them is consistent. Also the regression model between passed the F-test for F-4.93, where the critical value of the F-test was determined to 3.35. The significance of the F-test is 1.59% for F-test significance critical value 5% and thus the bond between the four variables can be determined as significant. All the data presented above showed that there is a significant link between the variables taken into consideration which present the economic development and the capital market development in Republic of Macedonia. This is obvious because the economic growth determinates can directly influence on the development of the capital market. The regression analysis showed that there is a significance link between the variables of economic development and the development of the Macedonia Stock Exchange. Conclusion is confirmed with the consideration that the regression has passed the t-test, for t-test critical value 0.96 and t-test success probability -0.96 to + 0.96.

Gross savings variable, realizes inverse relation with the dependent variable, with the high statistical significance (-1, 306). Therefore, the level of gross savings in the country as a percent of real GDP is of particular importance for capital market development in the Republic of Macedonia. However the relation is with the reverse impact, which means that every increase of the gross savings in the Republic of Macedonia doesn't contribute to the capitalization of the stock market. This is due to the small amount of the transactions that take place on the Macedonia Stock Exchange. It discourage the entities that are interested for investing in financial instrument on the capital market. They rather channel the savings in the banking sector in the form of deposits or in insurance com-

panies and investment funds to diversify the possible risk. This result is not unfamiliar for the emerging economies. The same conclusion was found in the study of the Idowu A. and Babatunde, M.A.¹⁸ which analyzes the effect of the financial reforms on capital market development in Nigeria. The main conclusion about the effect of gross saving on the capital market development in the Republic of Macedonia is that they are very important, but the financial reforms should be toward development of financial instrument that will be considered more attractive for entities and it will encourage them to invest their savings into the stock market, rather than in deposits in the banks.

Another unexpected result is the statistical parameters that reflect the influence of the economic growth. The statistical parameters show statistically significant impact on market capitalization (-1, 111) with the 10 % significance level of confidence, but with negative sign. This means that the trend of the economic growth does not follow the trend line of the market capitalization and stock traded value in the Macedonian Stock Exchange. Appropriate explanation is that the economic growth in the Republic of Macedonia must be sustainable and continuous to reach every sector of the economy, especially the financial sector. The similar result was received in the study of Eliskovski M.¹⁹ Therefore, it is absurd to conclude that economic growth has negative and opposite impact on capital market development in the Republic of Macedonia. This can lead to the conclusion that real economic growth in the Republic of Macedonia is not sufficient for capital market development. Therefore, the recommendations are to stimulate policies measures for higher and more sustainable economic growth. „The quality of growth needs structural reforms and strategies to increase productivity in the economy and thus to facilitate quality economic growth. This parallel should be accompanied by a policy to educate the economic agents in order to realize uses of securities as a means of long-term earnings and dispersion of risk. Thus in the future, this could contribute to alter the negative effect of GDP on development of the capital market in the country.”²⁰

The most important factor with the 1% of statistical evidence is the variable that presents the deposit interest rate. The result from the regres-

¹⁸ Op. Cit. Idowu, A., Babatunde, M.A.

¹⁹ Op. Cit. Eliskovski, M.

²⁰ Ibid, p. 23

sion is -6, 259, that confirm the theoretical statement that deposit interest rate is in inversed relation with the indicators of capital market. So, the 1 % percent increase of the deposit interest rate, decrease the market capitalization of the Macedonia Stock Exchange for 6 (percentage point). The higher deposit rates adversely affect on the interest of economic entities to invest in the capital market. With the higher deposit rates investors could reach higher profit with less risk. This will lead to mobilizing the available assets in the bank in the form of deposits, rather than in stocks, bonds and other financial instruments.

In this context Macedonia Stock Exchange needs to develop new financial instruments and follow the world trends in stock exchange operations to attract more subjects to participate in the stock market. „Also, it is important to state that for the development of liquidity of the capital market, the banking sector should exhibit a more active role in the stock market. The banks in Macedonia should create attractive products with competitive prices that will encourage companies to participate in the stock market.”²¹

Inflation rate that was considered as independent variable in the statistical model did not evident statistical significance for the market capitalization in the Republic of Macedonia.

Conclusion

The development of the capital market is conditioned by the economic development of a country. This paper deals with the dependence of the capital market in Republic of Macedonia of the economic development of the country. For the purpose of the research a regression analysis was conducted introducing and measuring the impact of series of variables on the capitol market in Republic of Macedonia. The independent variables chosen for the purpose of the research are closely connected and/or influence the economic development as well. Independent variables taken into consideration for the research in this paper are: GDP growth of the country, deposits interest rate, inflation and gross savings as a percentage of the GDP. The purpose of these variables taken into consideration is to determine and explain the dependent variable that represents the develop-

²¹ Ibid, p. 23-24

ment of the stock market in the case of this research market capitalization as a percentage of GDP. The research showed that the variables can explain and have impact on the development of Macedonian capital market. However the link between the variables and their effect on the capital market development in Republic of Macedonia differ from some previous findings in this area. This is mainly due to the small and unsustainable economic development of the country, seen by the difference in the trend lines of the GDP and market capitalization growth. Other factors complement this statement such as underdeveloped capital market, dominating banking sector, insufficient offer of products on the stock market etc.

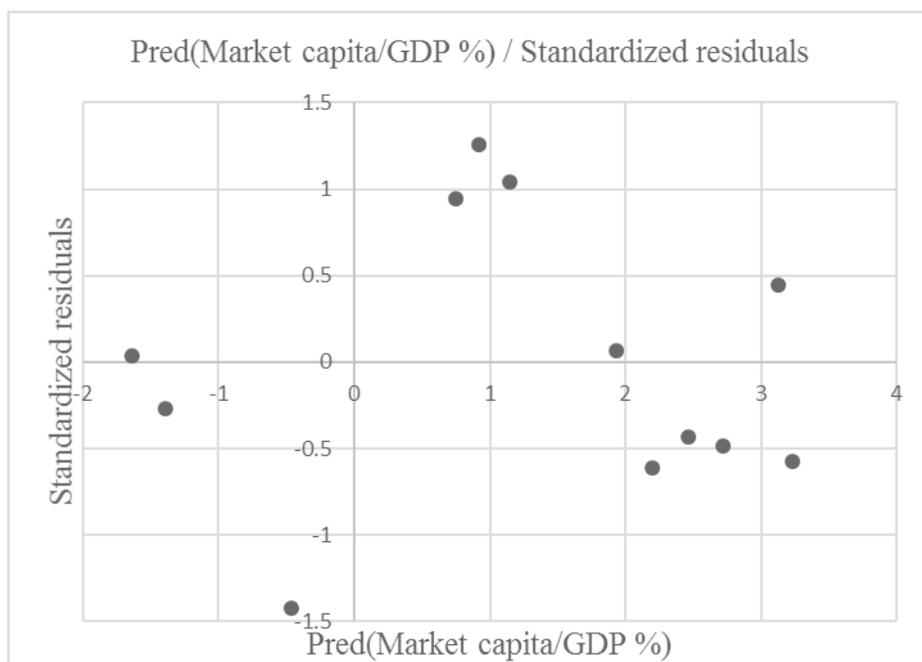
References:

1. Atje, R., Jovanovic, B., Stock Markets and Development, *European Economic Review*, 37 (2/3), 1993
2. Bekaert G. and Harvey C., Emerging Equity Market Volatility, *Journal of Financial Economics*, Elsevier, No. 43. 29-77, 1997
3. Caporale M. Howells G. P., Soliman A.M., Stock Market Development and Economic Growth: The Causal Linkage, *Journal of Economic development* 33 Volume 29, Number 1, June 2004
4. Demirgüç-Kunt, A. Maksimovic, V., Stock Market Development and Financial Choices Of Firms, *The World Bank Economic Review*, Volume 10, Issue 2, 1996
5. Eliskovski M., Macroeconomic determinants of development of the capital market in the Republic of Macedonia, 2012
6. Idowu, A., Babatunde, M.A., Effect of Financial Reforms on Capital Market Development in Nigeria, *Asian Journal of Business and Management Sciences*, Vol. 1 No. 8, 2012
7. Fink G. Haiss P., Sirma H., Credit, Bonds, Stocks and Growth in Seven Large Economies, *EI Working Paper No. 70*, 2006
8. Hadzi-Mishev R. Limit of effective portfolios of the Macedonian Stock Exchange, website of the Macedonian Stock Exchange, 2011
9. Kemboi J.K., Tarus, D.K., Macroeconomic Determinants of Stock Market Development in Emerging Markets: Evidence from Kenya, *Research Journal of Finance and Accounting*, ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online), Vol 3, No 5, 2012
10. King R. G., Levine, R., Finance and Growth: Schumpeter May Be Right, *The Quarterly Journal of Economics*, Volume 108, Issue 3, 1993

11. Levine, R., Zevros, S., Stock Markets, Banks and Economic Growth, American Economic Review, Vol. 88, 1998
12. Oya P. A., Damar H.E., Financial Sector Depending and Economic Growth: Evidence for Turkey, MPRA Paper No. 4077, 2006 (posted 15 July 2007)
13. National Bank of the Republic of Macedonia, Financial Stability Report for the Republic of Macedonia in 2014, October 2015
14. Plachý R., Rašovec T., Impact of economic indicators on development of capital market, International Journal E+M, 102 - 3, XVIII, 2015
15. Yartey, C.A., The Determinants of Stock Market Development in Emerging Economies: Is South Africa Different?, IMF Working Paper, WP/08/32, 2008
16. World Bank, <http://data.worldbank.org/indicator> (accessed 12.2.2016)

Annex 1

Figure 1 Test for heteroskedasticity of residual versus predicted values of the dependent variable Y



Source: own calculations XLSTAT 2015

Annex 2

Table 1 Criteria for evaluation of the model

DF	7,0000
R ²	0,8734
Adjusted R ²	0,8011
MSE	0,6435
RMSE	0,8022
DW	1,6695

Source: own calculations XLSTAT 2015

Table 2 Correlation matrix

Variables	Gross savings/% of GDP	Deposits interest rate	Inflation consumer price index	GDP Growth	Market capita/GDP %
Gross savings/% of GDP	1,0000	-0,3988	0,2488	0,3467	0,1822
Deposits interest rate	-0,3988	1,0000	-0,0473	-0,6019	-0,9013
Inflation consumer price index	0,2488	-0,0473	1,0000	0,0922	0,0316
GDP Growth	0,3467	-0,6019	0,0922	1,0000	0,4034
Market capita/GDP %	0,1822	-0,9013	0,0316	0,4034	1,0000

Source: own calculations XLSTAT 2015

Table 3 Multicollinearity statistics

Statistic	Gross savings/% of GDP	Deposits interest rate	Inflation consumer price index	GDP Growth
Tolerance	0,7746	0,5934	0,9330	0,6229
VIF	1,2909	1,6851	1,0718	1,6054

Source: own calculations XLSTAT 2015

Table 4 Model parameters

Source	Value	Standard error	t	Pr > t	Lower bound (95%)	Upper bound (95%)
Intercept	18,1305	4,5398	3,9936	0,0052	7,3881	28,8728
Gross savings/% of GDP	-1,6117	1,2342	-1,3059	0,2328	-4,5321	1,3086
Deposits interest rate	-5,7690	0,9217	-6,2590	0,0004	-7,9500	-3,5880
Inflation consumer price index	0,0797	0,2360	0,3379	0,7454	-0,4787	0,6382
GDP Growth	-0,6630	0,5965	-1,1114	0,3031	-2,0746	0,7486

Source: own calculations XLSTAT 2015

UDC 339.13.012.42(510)
338.121:339.13.012.42(510)
Original scientific paper

ISKRA STANCEVA-GIGOV*

THE BENEFITS OF TRADE LIBERALIZATION AND ITS CONTRIBUTION TO ECONOMIC GROWTH

Abstract

Nowadays trade liberalization is the most popular economic policy of developed and developing countries. Usually, high and sustainable economic growth, combined with a greater opening of international trade is the main goal of economic policy in almost every country regardless of its degree of development. Therefore the paper perceive existing benefits of trade liberalization and its effects on economic growth in the world and particularly in a developing country like China.

The paper concludes that trade liberalization promotes economic growth and produces a number of potential benefits (efficient use of resources, encourage competition, facilitating and increasing the flow of ideas, knowledge and technology, etc.) through a number of channels. Trade liberalization significantly encourages foreign trade and cross-border financial flows, a greater volume of output and specialization, which ultimately leads to higher economic growth. The paper also indicates that most of the effects of trade liberalization are positive, but that they are influenced by many individual factors of each country and its other macroeconomic policies and conditions.

Key words: trade liberalization, economic growth, foreign trade, FDI, world output

JEL classification: F13, F30, F43, F21

* Ph.D., Institute of Economics - Skopje, Republic of Macedonia, e-mail: iskra@ek-inst.ukim.edu.mk

Introduction

Historical development of foreign trade policies in a global economy is characterized by two trends: liberalism and protectionism. These two type of policies are typical for certain periods of development of particular countries. They formulate them depending on the objectives that they want to achieve and the specific conditions in the international economic and political system.

In spite of different choice of foreign trade policies in the countries, in this process throughout history are noticed two features. First, the protectionism is characterized for the early stages of industrialization, and was present in both developed (XIX century) and developing countries¹ (the period after the Second World War). Second, over the last thirty years have seen a strong trend of leaving the rigid protectionism and increasing liberalization of foreign trade policies of most countries in the world.² Policymakers and scientists in that period, began to discuss the benefit of liberalization and outward-oriented policies, explaining that open policies increasingly contribute to accelerated growth, then inward-oriented or closed protectionist policies.

After the Second World War are made continuous efforts to liberalize world trade. The first negotiations were made under the General Agreement on Tariffs and Trade (GATT). From 1947 onwards, eight, often difficult, negotiation rounds resulted in gradual reduction tariffs. Seventh, the Uruguay Round (1986-1994), expanded trade liberalization in new areas such as intellectual property rights, services, capital and agriculture. In addition, during this round it was agreed the creation of the World Trade Organization (WTO). While GATT is a set of trade rules, the WTO is an international organization that oversees global trade and promote its further liberalization. The negotiations in Doha³ are the first multilateral trade

¹ After the widespread adoption of policies of import substitution in the 1950s and 1960s, most developing countries since the early 1980s shifted towards more open trade policies. The reasons for this change are varied and include sluggish performance of the policies of import substitution (Kruger, 1997).

² Toseva, G., *Efekti od liberalizacijata na nadvoresno-trgovskata politika na Republika Makedonija*, doktorski trud, Ekonomski institut – Skopje, Skopje, 2011, p. 24

³ Doha Development Agenda initially covers 12 areas (agriculture, industrial products, services, intellectual property, investment, competition, government procurement, trade facilitation, anti-dumping, subsidies, regional trade agreements and trade and environment).

round since the WTO was established. It was lunched in Doha, Qatar, in November 2001 and has not yet been completed. Its main objective is to integrate developing countries into the world trading system. In the center of the negotiation are three issues: a) reduction of agricultural tariffs in EU, b) reduction of agricultural subsidies in the USA and c) improve access of industrial goods and services on the main developing countries' markets. All this confirms the growing orientation towards the liberalization of the international trading system.

Taking into account the intensive process of liberalization in recent decades, this paper will consider the benefits of liberalization and its contribution to higher economic growth in the world.

1. THE EFFECTS OF TRADE LIBERALIZATION ON ECONOMIC GROWTH

With the globalization of world economies, almost all countries in the world are actively involved in reducing trade barriers between their trading partners. The main goal of moving towards free trade is to achieve macroeconomic objectives of their economies and higher economic growth.

Despite numerous debate, economists largely agree that trade liberalization brings significant benefits for each county. It is expected that trade liberalization would promote economic growth through more efficient use of resources, encourage competition, and by increasing the flow of knowledge and ideas across national borders.

The notion that trade liberalization inevitably leads to export increasing, and hence to economic growth is accepted by all multilateral institutions, primarily the WTO and the World Bank, IMF, OECD etc. In the context of this consideration, the latest two decades, many developing countries liberalize their trade regimes. Moreover, some of these liberalizations are implemented voluntarily, while most of them are actually implemented at the request of most important financial institutions, primarily the World Bank and IMF. They directly connected their credit arrangements with the trade liberalization as one of the important conditions for obtaining loans. The main role of the WTO, as a global trade

regulator, is to provide as easy as possible and faster flow of goods and services across national borders and thus stimulate economic growth and facilitate economic development of countries and regions in the world. WTO achieves this through the formulation and implementation of several principles that are the base of multilateral trading system, and supporting the principle of liberalization. These are:⁴

- Trade without discrimination (Most-favoured-nation (MFN): treating other people equally and National treatment: Treating foreigners and locals equally).
- Freer trade: gradually, through negotiation.
- Predictability: through binding and transparency.
- Promoting fair competition.
- Encouraging development and economic reform.

These principles have certainly contributed to greater trade liberalization in the world.

In the field of liberalization the GATT and the WTO recorded impressive success. Although GATT was conceived as a temporary document⁵ with a limited field of action, yet his success during 47 years in promoting and providing the world trade liberalization is indisputable. Within the GATT, negotiations to reduce customs duties were held in eight successive rounds. Actually, the first five of these rounds were completely committed to reducing tariffs. The next three had a broader agenda, but negotiations on customs reduction remained an important item on the agenda of these rounds.

⁴ https://www.wto.org/english/thewto_e/whatis_e/tif_e/fact2_e.htm, accessed on 28 July, 2016

⁵ On October 30, 1947 has been agreed the content and scope of the General Agreement on Tariffs and Trade (GATT) as a temporary document which is supposed to regulate international trade until the overcoming of the problems with the ratification of the Havana Charter and the establishment of the International Trade Organization. But the International Trade Organization and the Havana Charter never realized so that the "temporary" GATT remained in force as the only international instrument in trade until the end of the Uruguay Round of negotiations and the creation of the WTO in 1995.

Table 1. MFN tariff reduction of industrial countries for industrial products, excluding petroleum

Implementation Round covered period		Weighted tariff reduction of all duties
1948–63	First five GATT rounds (1947–62) ^a	–36
1968–72	Kennedy Round (1964–67) ^b	–37
1980–87	Tokyo Round (1973–1979) ^c	–33
1995–99	Uruguay Round (1986–94) ^d	–38

Source: http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/22fact_e.htm#tariffcuts, accessed on 15 July, 2016

Note:

- a. Tariff reductions for the first five trade rounds refer to US only.
- b. refers to four markets: US, Japan, EC(6), and UK.
- c. refers to eight markets: US, EU(9), Japan, Austria, Finland, Norway, Sweden, Switzerland.
- d. refers to eight markets: US, EU(12), Japan, Austria, Finland, Norway, Sweden, Switzerland

The data presented in Table 1 show that the eight rounds of trade negotiations in GATT have been very successful in reducing customs duties. In addition to the previous statement is the fact that in the late 1940s, the average tariff on industrial products imposed by developed countries was about 40 per cent ad valorem, and as a result of eight GATT rounds since the mid-1990s the average tariff on industrial products fell gradually to 3, 9 per cent ad valorem.⁶

In period of application of the GATT and through eight rounds is achieved not only significant liberalization, but also the expansion of international trade. The continued reductions in tariffs helped encourage very high rates of growth of world trade. That is shown in Table 2. In 1948, the world export of goods amounted to 58 billion dollars, and in

⁶ Van den Bossche Peter, *The Law and Policy of the World Trade Organization: Text, Cases and Materials*, Cambridge University Press, Aug 21, 2008, p. 409

Table 2. World trade and output, Selected Indicators, 1948-98

	1948	1950	1973	1990	1998	Average annual change			
						1948-73	1973-98	1948-98	1990-98
World merchandise exports									
Billion current \$	58	61	579	3,438	5,235	9.7	9.2	9.4	5.4
Billion constant 1990\$	304	376	1797	3,438	5,683	7.4	4.7	6.0	6.5
World output (Indices, 1990=100)									
Commodity output	17	19	65	100	116	5.5	2.4	3.9	1.9
Manufacturing output	11	13	60	100	117	7.1	2.7	4.9	2.0
GDP (Billion, 1990\$)	3,935	4,285	13,408	22,490	27,615	4.9	2.9	4.0	2.6
GDP per capita (1990\$)	1,591	1,700	3,420	4,217	4,623	2.9	0.4	2.2	-1.4
Exports of goods and services, to GDP, at constant 1987 prices	...	8.0	14.9	19.7	26.4

Source: http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/22fact_e.htm#tariffcu, accessed on 15 July, 2016

This is confirmed by the fact that in this period commodity production registered growth of 3.9% annually, or 8 times more.

1998 it was increased to 5235 billion dollars. During that period world trade increased by 6%, or increased 18 times. Moreover, the dynamics of trade liberalization helped to ensure that trade growth continuously intensify production growth.

This is confirmed by the fact that in this period commodity production registered growth of 3, 9% annually, or 8 times more.

The share of global trade in goods and commercial services in the world's gross domestic product (GDP) is also a reliable measure of economic liberalization. In 1950, exports of goods and commercial services represented 8% of GDP, while in 1998, this share of exports in GDP is 26.4%.

Immediately after the international trade, foreign direct investment (FDI) is also an important aspect of economic globalization and liberalization. FDI inflows increased from 24 billion dollars in 1973 to 60 billion dollars in 1985 up to 645 billion dollars in 1998. That is, FDI inflows grew 27 times (or 14% per year) in the period between 1973 and 1998.⁷ These results largely due to the continuous improvement of the conditions for international trade, i.e. permanent evolution on multilateral trading system.

Despite the upward trend of international trade in the analyzed period, from the table can be seen a trend of increasing economic growth represented by GDP and GDP per capita in the world. It leads to the conclusion that the whole process of liberalization has a positive impact on growth in the world economy.

A number of other analyzes and evaluations indicate the positive contribution of liberalization on economic growth. Namely, the World Bank continues to support the view that trade liberalization encourages economic growth if are met other conditions - such as macroeconomic stability, good governance etc. It believes that the openness of markets could generate a further increase in growth of 1-1.5% annually.⁸

Another assessment is that of the OECD, according to which the economic benefits of the removal of remaining trade barriers will be considerable:

⁷ http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/22fact_e.htm#tariffcuts, accessed on 15 July, 2016

⁸ Spanu V., *Liberalization of the international trade and economic growth: implications for both developed and developing countries*, Harvard University, Cambridge, May, 2003, p. 13-14

- A 10% increase in trade is associated with a 4% rise in per capita income.
- «Open» climate for FDI can be expected to produce 0.75% increase in GDP per capita in the OECD area.
- Lower regulatory barriers to competition could result in a 2% to 3% increase in GDP per capita in the OECD.
- More efficient customs procedures could improve global welfare by \$ 100 billion.
- Full tariff liberalization in agricultural and industrial goods could boost global welfare for an additional 100 billion dollars.

In Europe also the reduction of trade barriers boosted economic performance: the EU's GDP is estimated to be almost 2 percent higher as a result of the creation of the single market. But the EU has much more to do in reducing barriers to trade with the rest of the world, especially in agriculture. Increased external openness is an integral part of the Lisbon agenda for promotion of economic reform within the EU.⁹

It is also important to add that despite the aforementioned analysis and estimates, the large number of empirical studies, regardless of advanced modern econometric techniques, show a positive relationship between trade liberalization and economic growth (Thomas et al. 1991; Joshi and Little, 1996; Helleiner, 1994; Bleaney, 1999; Ahmed, 2000).¹⁰

2. TRADE POLICY LIBERALIZATION AND ECONOMIC GROWTH – SUCCESS STORY OF CHINA

Although the impact of trade liberalization on export activity and economic growth is one of the most researched in recent decades, however, the existing experiences of countries, especially the developing countries that have implemented trade liberalization, are very different.

Certain Asian countries are perhaps the most spectacular example of economic success linked to export performance and trade liberalization. While other developing economies implemented a strategy of import-substitution industrialization and experienced relatively low rates

⁹ Dobre C., The relation between openness to trade and economic growth, 2008, p.241

¹⁰ Parikh A., Trade Liberalization, Growth, and Balance Of Payments in Developing Countries: An Econometric Study, The International Journal, Volume XX. No. 4, Winter 2006, p. 430

of economic growth, the East Asian “tigers”¹¹ have adopted more open trade policies and experienced staggering rates of economic growth. But in many cases the strategy for success was not based on full application of the principle of free trade.¹² While some of these countries were fully oriented towards free trade, others applied interventionist measures, such as South Korea. It is also concluded that there is no completely single East Asian model that can be applied to promoting economic growth. In that context, they were identified three policies that contributed to the success of these economies:

- Industrial policy which promoted the specific sectors in the economy in order to achieve strategic orientation of the industry as the main economic branch;
- Policy of state supervision of financial markets that reduce cost of capital and focuses on the direct lending of strategic sectors and
- Policy that promotes export and protecting the domestic industry at a certain time.

Generally it can be stated that there is no way in which any of these countries would grow faster if it was not applied in all cases the strategy for accelerated growth in exports.

When it comes to Asian countries, particularly interesting is the case of China, which after three decades of inward oriented trade has launched the so-called policy of “open doors” in 1978, and which is currently one of the top world exporters.¹³ Since then, its exports grow 15, 5% per year (on average), and the rate of GDP growth is around 10% (Figure 1).

¹¹ Group of countries consists of: South Korea, Singapore, Taiwan, Hong Kong.

¹² Obradovic S., *Uticaj integracije i liberalizacije na privredni rast – empiriska evidencija u korist integracija u EU*, Ekonomske teme br.1-2, Ekonomski fakultet, Nis, 2005, str. 155

¹³ UNCTAD, <http://knoema.com/pqaqfne/major-exporters>, accessed on 8 August, 2016

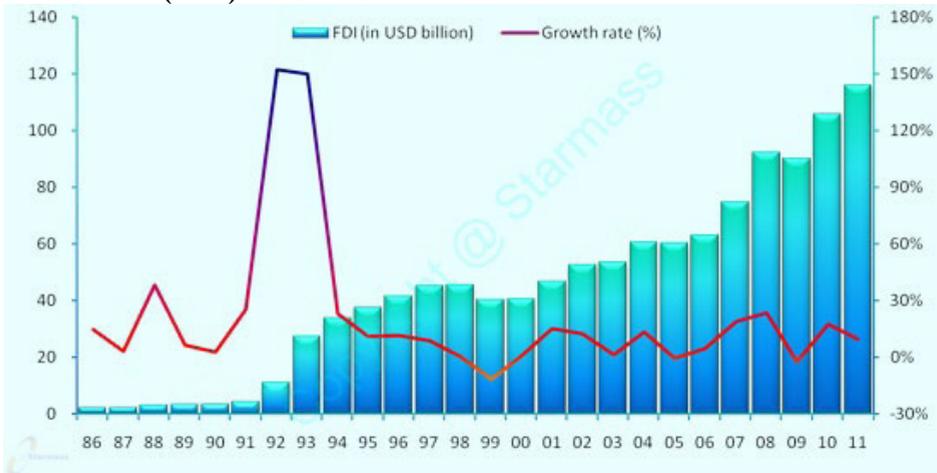
Figure 1. Annual average growth rate of export and GDP in China (1981-2014)



Source: Prepared by the author based on data from UNCTADStat

The driving force for this exceptional growth is the increasing openness of the economy, especially in trade and foreign direct investment. Actually, attracting FDI is pillar of the policy of opening to China. It is confirmed by the data about the volume and rate of growth of FDI in China that are shown in Figure 2. The role of FDI in promoting China's foreign trade focus on two aspects. First, the rapid increase in the volume of export and import of foreign investors has expand the scope of foreign trade of China. Second, FDI helped to upgrade the structure of export products of China.

Figure 2. Total amount and trends of foreign direct investment (FDI) used in China



Source: <http://www.starmass.com/china-review/foreign-investment/amount-FDI-used.htm>, accessed on 8 August, 2016

Foreign investors with their FDI in China introduced new technology, know-how, and international marketing opportunities and thus helped to change its comparative advantage. In the coming years, China will focus its investments in Research and Development centers, in new high-technology industries, advanced manufacturing and in sectors of energy saving and ecological adapted sectors. It is a classic example of export-oriented economic growth promoted by the government through the establishment of special economic zones and open cities, which are a magnet for investment. In all export-oriented economies, typical initiatives for exporters include: investment subsidies and allowances; exemption from taxes and duties on inputs for exported goods, favorable treatment of foreign investments, etc.

Conclusion

Generally, it can be concluded that trade liberalization promotes economic growth and produces a number of potential benefits (efficient

use of resources, encourage competition, facilitating and increasing the flow of ideas, knowledge and technology, etc.) realized through various channels. Trade liberalization leads to increased volume of trade and volume of output, encourages investment and greater specialization and technology transfer, and it certainly leads to greater economic growth.

The existing experiences of countries (especially the developing countries) about the impact of trade liberalization on export activity and economic growth are very different. Thus, China is an example of country with positive experience from the application of trade liberalization policy. After three decades of inward oriented trade it has launched the so-called policy of “open doors” in 1978, and it is currently one of the top world exporters. It has experienced significant progress not only in trade, but also in FDI. Attracting FDI is pillar of the policy of opening to China. The volume of export and import of foreign investors has expand the scope of foreign trade of China and FDI helped to upgrade the structure of export products of China.

Therefore it is important, each country in the implementation of trade liberalization to take into account its own characteristics - national legislation, foreign trade partners, export-oriented sectors, the share of primary exports in total exports, the rate of trade in GDP and how it is sensitive to foreign trade. Every country has the right to choose their own development priorities and its institutions and should be protected from external pressure.

It is also important to know that for the success of trade liberalization and its positive effects is not only important act of liberalization, but a wider range of economic policies and measures, and some other factors, such as natural and infrastructural barriers. In that regard trade liberalization is conditional in its impact on economic growth. In most cases economists highlight the need for a stable and non-discriminatory foreign exchange system, sound monetary and fiscal policies, corruption-free administration, the minimum required for trade liberalization in the long term.

References:

1. Dava Emilio, Trade liberalization and economic growth in the SADC: a difference-in-difference analysis, Paper presented at IESE's III Conference, September, 2012
2. Dobre C., The relation between openness to trade and economic growth, 2008
3. Obradovic S., Uticaj integracije i liberalizacije na privredni rast – empiriska evidencija u korist integracija u EU, *Ekonomске teme* br.1-2, Ekonomski fakultet, Nis, 2005
4. OECD, "The Impact of Trade Liberalisation on Jobs and Growth: Technical Note", OECD Trade Policy Working Papers, No. 107, OECD Publishing, 2011
5. Parikh A., Trade Liberalization, Growth, and Balance Of Payments in Developing Countries: An Econometric Study, *The International Journal*, Volume XX. No. 4, Winter 2006
6. Spanu V., Liberalization of the international trade and economic growth: implications for both developed and developing countries, Harvard University, Cambridge, May, 2003
7. UNCTADStat, <http://unctadstat.unctad.org>
8. UNCTAD, <http://knoema.com/pqaqfne/major-exporters>
9. Van den Bossche Peter, *The Law and Policy of the World Trade Organization: Text, Cases and Materials*, Cambridge University Press, Aug 21, 2008
10. https://www.wto.org/english/thewto_e/whatis_e/tif_e/fact2_e.htm
11. http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/22fact_e.htm#tariffcuts
12. http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/22fact_e.htm#tariffcuts
13. <http://www.starmass.com/china-review/foreign-investment/amount-FDI-used.htm>

VLADIMIR PETKOVSKI*
ELIZABETA DJAMBASKA**
SNEZANA KOSTADINOSKA MILOSESKA***

THE FUNDAMENTAL CONSIDERATIONS OF THE PUBLIC DEBT

Abstract

Recent financial and economic crises in 2010 produce serious negative consequences for the fiscal stability and economic sovereignty in the most of the countries in the world. The most intimidating are the increased public debts. The paper explains some of the fundamentals considerations of the public debt, with the focus on the determination and definition of the public debt. Especially important contribution of this paper is the elaboration of the methodology of calculation and estimation of the level and state of the public debt and distinguishing of the main differences among the applied methodology.

Key words: Public debt, Methodology, EFF methodology, ESA 95 methodology, ESA 2010 methodology

JEL classification: H60, H630, E62,

Introduction

There is no generally accepted stance on budget deficit, although the presence of the public debt is evident. The debate among the scientist

* Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: vladimir@ek-inst.ukim.edu.mk

** Ph.D., Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: beti@ek-inst.ukim.edu.mk

*** Ph.D. Ss. Cyril and Methodius University in Skopje, Institute of Economics – Skopje, Republic of Macedonia, e-mail: snezana@ek-inst.ukim.edu.mk

according to this problem considers and elaborates how big the problem is and should the balancing of the government budget be the main priority.

Most of the world countries are faced with the problem of high deficit and increasing public debt. Statistical evidence confirms that the level of public debt is above the highest register after the Second World War. Thus, in Japan, the USA and several European countries (Greece, Portugal, and Ireland) the debt exceeds the 100% of the GDP¹.

Economies faced with the situation of low economic growth rates, budget deficits, increased expenditures arising from aging population, and unstable financial sector represent additional pressure on the sustainability of public finances. Such concerns reflect the ratings of the economies and raise borrowing costs. Therefore, achieving fiscal balance and reducing the public debt are targets with the highest priorities.

The importance of this paper is seen thru the systematic review of the public debt methodology. First of all determination of total amount of the public debt in the economy is an objective that has to be fulfilled, because it presents the basis for preparing the appropriate policies and measures for managing public debt. These activities are crucial for solving the problem of public debt. Therefore the knowledge of the methodology for calculating and allocating the public debt and different modes and scope of the calculating methods give a clearer view of the debt burden.

1. PUBLIC DEBT CONCEPT AND METHODOLOGY

Economic and financial crisis in 2010 caused a serious distortion on economic sovereignty and a large fiscal burden of countries in Europe and worldwide. State borrowing measured by the public debt-to-GDP ratio increased sharply due to economic contraction and acyclic fiscal measures. The increased level of public borrowing in the world caused an increase in financial costs to governments borrowing. Increased borrowing caused further financial problems for countries that decreased economic activity, economic growth and crowding out effect of the private sector. Also, the increased borrowing of states causes a reduction in their liquidity and solvency off the capital market.

¹ World Economic and Financial Surveys, World Economic Outlook, Coping with Hight Debt and Sluggish Growth, IMF, October 2012

The State borrows as a result of previous fiscal deficits or when state expenditure exceeds state revenue. But the relationship between public debt and budget deficit is far more complex and is influenced by many other factors, such as additional requirements and criteria for borrowing, the difference between the nominal and market value of debt, adjustment of debt in convertible currencies and other statistical adjustments and methodology for calculating the public debt.

Public debt can be represented as nominal value of total public debt, debt per capita and the ratio between public debt and GDP. The ratio public debt/ GDP in fact represent the size of public debt in the relation of the size of economic activity. This is a key factor in determining the capacity of the economy for servicing the public debt. The indicator shows whether the capacity for tax collection is sufficient to service the debt.

The ratio between public debt and deficit (as the ratio public debt/ GDP) can be represented by the following:

$$\frac{D_t - D_{t-1}}{GDP_t} = \frac{EXP_t - REV_t}{GDP_t} + \frac{DDA_t}{GDP_t}$$

In equation D_{t-1} denotes the debt in period t-1, which together with the difference between budget expenditures EXP_t budget revenues REV_t and indicator adjustment of debt and deficit DDA_t representing cumulative public debt (D_t) at the end of period t.

Public debt with the high level and with the increasing trend changes the nominal and real interest rate. Further increase in public debt leads to increase of the debt servicing cost, primarily costs for interest. Despite the opportunity cost and crowding out effect of the private sector, debt may contribute to creating a snowball effect. The effect assumes that the increase in public debt causes an increase in the cost of interest and is financed by additional borrowing that decline the sustainability of public finances. This causes increase in interest rates. Due to the limited supply of money, borrowing from the private bank reduces the possibility of financing the private sector. This restriction causes the increased expenses for cash and loans that banks are issuing to private sector. Reduced possibility of lending to the private sector leads to a reduction in investment and consumption in the private sector. In some cases, high public indebtedness may cause capital outflow from the country, thereby causing a crisis in the banking sector or changes in exchange rates.

Appropriate methodology for public debt always should take into consideration the solvency of the government that borrows. The government is solvent when in the period t discounted value of all revenues is greater than the accumulated public debt and the discounted value of future budget deficits. However the state should be able to service its debt timely, in order not to fall in indebtedness. Government can service existing and future public debt by setting higher taxes to boost budget revenues, sale of assets that are owned or reduction of state expenditures. However the provision of funds for servicing the public debt through one of the ways previously shown can be accompanied by serious economic and political pressures. The increase in taxes could lead to a deepening crisis, by adding a larger tax burden and increased pressure for citizens.

Another criteria that is important for the selecting the method of calculation and analysis of public debt is the indicator of the liquidity of the state. Government that borrows is considered liquid for the period t , if all available funds and liquid assets of the state denominated in a particular currency can service all due liabilities for the same period t . Therefore, the knowledge of the assets and debt structure is crucial in managing and servicing the debt. The structure and liquidity of the government assets have great importance in determining the interest rate and debt cost.

The solvency and liquidity of the government in terms of public debt have a major impact on the sustainability of public finances and fiscal policy in the economy. Sustainability of the finances and debt considers the government's ability to manage debt through payment of liabilities arising from it and at the same time providing public facilities and services. So, the sustainability of the public debt should be seen through the liquidity indicator i.e. the ability of the governments to service the due debt timely. Long term sustainability of the public debt defines the solvency and the budgets constraints of the economy. Budget limit represents the difference between total public debts of the country with the discounted total future public expenditures and revenues. Increased public debt, assumes future increase of the revenues for debt servicing. The formula is as follows:

$$D_0 - \sum_{t=1}^{\infty} \frac{pb_t}{(1+r)^t} = 0$$

In the equation of budget constraint D_0 represents the public debt ratio to GDP at the beginning of time $t=0$, pb_t , t represents the budget bal-

ance in period t and r represents the differential gap between the nominal interest rate and the nominal growth rate of GDP.

The definition for the public debt in the European Union Countries and the most of the Europe countries takes into account the debt of the government sector.² Public debt includes the sum of all budget deficits. The most important for understanding the concept of public debt is to distinguish the main difference between the concept of public debt and budget deficit. The budget deficit represent flow and public debt state. Therefore, budget deficit is measured by changes over a period of time, while the total amount of the public debt is determined at one moment or on a certain day.³ The overall public debt (gross debt) in any period of time reflects the debt of all government liabilities, debt with the Central Bank, state agencies, social funds, private investors and other financial institutions. Government debt to private investors (except the debt with the central bank and government agencies) is net public debt.

The concept of calculation of public debt in the European Union is based on the methodology established in accordance with the Maastricht Treaty, so this method of calculation is called Maastricht debt. Maastricht debt is defined as gross public debt of the central government expressed in nominal value at the end of the fiscal year and consolidated debt of all level of central government. Maastricht debt consist of all government obligations in a currency including deposits, loans and securities (excluding shares). It excludes certain financial instruments precisely financial derivatives and trade credits. The methodology for the calculation of public debt is applied in the European Fiscal Framework (EFF). It is used for all fiscal procedural processes of calculation and determination of public debt in the European Union. Thus the estimated public debt is used for fiscal monitoring of countries in the European Union, in particular for overseeing the cri-

² The general government sector by convention includes all the public corporations that are not able to cover at least 50 percent of their costs by sales and, therefore, are considered non-market producers. The general government sector has four subsectors: central government, state government, local government and social security funds. In the European System of Accounts (ESA95), paragraph 2.68, the sector "general government" has been defined as containing: *"All institutional units which are other non-market producers whose output is intended for individual and collective consumption, and mainly financed by compulsory payments made by units belonging to other sectors and/or all institutional units principally engaged in the redistribution of national income and wealth."*

³ Atanasovski Zivko, Public Finances, Faculty of Economics – Skopje, 2004, p. 297

teria set by the European Union, public debt not exceeding 60% of GDP.⁴

The advantage of this methodology for the calculation of public debt is in the exemption of the effects related to prices, market changes, liquidity of government funds and changes in exchange rates. Applying the Maastricht debt indicator simplify the methodology of calculation of gross public debt and facilitate control, comparison and management of the public debt.

The second concept for the calculation of gross public debt is based on national accounts of the Member States of the European Union in accordance with the European System of Accounts (ESA 95), and are therefore called ESA debt. The concept of ESA public debt includes all obligations of the government in a given period of time in a particular currency. Despite further lease obligations and instruments which are included in the calculation of EFF debt, ESA methodology for calculating the public debt include other financial instruments, namely financial derivatives, due liabilities and insurance reserves. The additional difference between ESA and the EFF methodology for calculating the public debt is the proposition that according to ESA methodology public debt is calculated at market prices. Therefore, the estimated public debt reflects the impact of changes in market prices and exchange rates, as well as the liquidity of the assets of the central government.⁵

Starting from the 1 September 2014 the ESA 2010 are established as the new methodology for measurements the general government debt. In ESA 2010, the core equivalent concept is total financial liabilities, which involve a wider list of financial instruments than included in government debt. The relevant ESA 2010 paragraphs on valuation of government liabilities are:⁶

- 1.94: “Flows and stocks shall be measured according to their exchange value, i.e. the value at which flows and stocks are in fact, or could be exchanged for cash. Market prices are ESA’s basic reference for valuation.”

⁴ Publications Office of the European Union, “*Manuel on Government Deficit and Debt – Implementation of ESA 2010*”, Luxemburg, 2014, pg. 383

⁵ Ibid pg. 403

⁶ EUROSTAT, Manuals and guidelines, Manual on Government Deficit and Debt - Implementation of ESA 2010, 2014

- 7.33: “Assets and liabilities are valued at the market prices on the date to which the balance sheet relates”.
- The stock of government liabilities should be recorded in national accounts at their market value, at the end of the accounting period, in the closing balance sheet of the general government sector.

The main revenue of general government consists of taxes, social contributions, sales and property income. It is defined in ESA 2010 by reference to a list of categories: market output, output for own final use, payments for non-market output, taxes on production and imports, other subsidies on production, property income, current taxes on income, wealth, etc., net social contributions, other current transfers and capital transfers.

The main expenditure items consist of the compensation of (government) employees, social benefits (social benefits and social transfers in kind for market production purchased by general government and NPISHs), interest on the public debt, subsidies, and gross fixed capital formation. Total general government expenditure is defined in ESA 2010 by reference to a list of categories: intermediate consumption, gross capital formation, compensation of employees, other taxes on production, subsidies, property income, current taxes on income, wealth, etc., social benefits other than social transfers in kind, social transfers in kind - purchased market production, other current transfers, adjustments for the change in pension entitlements, capital transfers, and transactions in non-produced assets.

Table 1 Methodology for public debt

Sector	EFF methodology	ESA 95 methodology	ESA 2010 methodology
Gross concept	Central Government		
	Gross public debt		
Financial instruments	loans; deposits; other securities than shares	financial derivatives; liabilities from loans and other past due payments; insurance reserves	Currency and deposits (AF2), debt securities (AF.3), loans (AF.4)

Value	nominal price	market price	market price
Consolidation	Consolidated (Included sub-levels of the central government sector)	Dual consolidation (calculation include all levels of the central government and calculation only of the central government debt)	Dual consolidation (calculation include all levels of the central government and calculation only of the central government debt)
Advantages	<p>The calculations are on nominal prices and the impact of the market fluctuations is not included</p> <p>Simplicity of calculating the public debt (excluding all obligations that are difficult to measure in practice)</p> <p>The methodology allows direct application with the EU principles and comparison with EU countries</p>	<p>Comprehensive overview of government duties</p> <p>Calculation of net public debt of the central government at market prices</p> <p>Methodology that allows comparison with other countries of the world</p>	<p>Calculation of net public debt of the central government at market prices</p> <p>Methodology that allows comparison with other countries of the world</p>

Source: Dagmar Hartwig Lojsch, Marta Rodriguez-Vives and Michal Slavik, “The Size and Composition of Government debt in the Euro Area”, European central bank, Occasional paper series, October 2011, pg. 14

The European System of Accounts 1995 (the ESA 95), was published in 1996. The ESA 2010 methodology has the same structure as the ESA 95 publication for the first 13 chapters. But, it is expanded with the 11 new chapters elaborating aspects of the system which reflect develop-

ments in measuring modern economies. In order to establish a balance between data needs and data possibilities, the concepts in the ESA 2010 have several important characteristics. The characteristics are that the accounts are: (a) internationally compatible; (b) harmonized with other social and economic statistical systems; (c) consistent; (d) operational, meaning that they can be measured in practice; (e) different from most administrative concepts; (f) well-established and fixed over a long period; (g) focused on describing the economic process in monetary and readily observable terms and (h) capable of applying in different situations and for different purposes.

According to the ESA 2010 system, for the government deficit and debt it is important to depart several things:

- The classification of units: the government deficit and debt are primarily affected by units classified to the government sector. This is determined by considering whether or not a unit is controlled by government and whether it is a non-market or market (financed mainly by its own sales) unit. Privately controlled market institutional units are not included in the government sector.
- The timing of transactions: ESA 2010 records transactions on an accrual basis, i.e. when the economic activity takes place, rather than when the cash is paid. Such differences may be large, and therefore significant for the government deficit/surplus.
- The nature of a transaction: ESA 2010 distinguishes non-financial transactions such as consumption, wages and salary, subsidies or grants to cover losses, which directly affect the government deficit; and financial transactions as e.g. the acquisition of financial assets or the repayment of debts, which do not.

The introduction of ESA 2010 outweighs the negatives and the obstacles from the methodological aspect that contained EFF and ESA 95 methodology. The application of the ESA 2010 in the calculation of public debt over time will manifest failure, so, in the future will indicate what changes should be made.

2. THE CONCEPT OF PUBLIC DEBT IN THE REPUBLIC OF MACEDONIA

According to the Law on Public Debt of the Republic of Macedonia⁷ public and government debt are separate concepts and are separately defined. „Government debt is the sum of financial liabilities created by borrowing by the Republic of Macedonia, public institutions established by the Republic of Macedonia and the municipalities in the City and the City of Skopje, excluding the debt of public enterprises and companies being fully or predominantly owned by the state municipalities and the National Bank of the Republic of Macedonia.”⁸

The public debt „is the sum of government debt and the debt of public enterprises established by the state or the municipalities in the City and the City of Skopje, as well as companies being fully or a dominant ownership of the state or the municipalities in Skopje and Skopje for which the state has issued a state guarantee. The debt of the National Bank of the Republic of Macedonia is not a public debt.”⁹

Management of the public debt include set of activities and measurements that the Ministry of the Finance of the Republic of Macedonia is obligated to implement according to the specified competencies in the Law on Public Debt.

The main goals of the management of the public debt are:

- Financing the needs of the state apparatus with the lowest possible cost and sustainable risk, in the medium and long term;
- Identifying, monitoring and managing the risks to which the portfolio is subject to the public debt;
- Development and maintenance of efficient domestic financial market

⁷ Law on Public Debt (Official Gazette No. 165/2014), Act on Amendments of the Law of Public Debt, (Official Gazette no. 139/2014), Act on Amendments of the Law of Public Debt (Official Gazette No. 35/2011), Act on Amendments of the Law of Public Debt (Official Gazette No. 88/2008),), Decision of the Constitutional Court U.Br.49 / 2006-0-0 of 13.12.2006, (Official Gazette No.137/06) and the Unofficial Consolidation Law on Public Debt include: the Public Debt Law (Official Gazette no.62/05)

⁸ Law on Public Debt (Official Gazette No. 165/2014)

⁹ Ibid

Public debt policy management is determined for a period of three years and is part of the fiscal strategy of the Ministry of Finance in the Republic of Macedonia. It includes a set of activities among them are:

- determination of the public debt limit in the medium term;
- setting the amount of sovereign guarantees on average medium term;
- the maximum amount of new borrowing in the current year;
- the maximum amount of newly issued sovereign guarantees in the current year;

The most important question is to determine the public debt limit. Public debt limit in the Republic of Macedonia is determined based on the ratio of public debt and GDP in denars according to the average exchange rate at the official rate of the National Bank of the Republic of Macedonia valid on the date of calculation.

Public borrowing in the country may be accompanied in the following forms:

1. Borrowing by concluding loan
2. Borrowing by issuing government securities
3. Issuing state guarantees

The Republic of Macedonia accepted the ESA 2010 methodology for calculation of general government debt. Thus the calculations of government liabilities are made in accordance with the principles and criteria of the ESA 2010 and the Law on Public Debt of the Republic of Macedonia.

Conclusion

Public debt is present in both developed and developing countries. The most important relevant question for its management is the appropriate definition and scope of public debt.

Public debt is defined according to the different approaches about the structure and coverage of economic sectors, liabilities and assets of the country. The definition for the public debt in the European Union Countries

and the most of the Europe countries takes into account the debt of the government sector. Public debt includes the sum of all budget deficits.

The concept of calculation of public debt in the European Union is based on the methodology established in accordance with the Maastricht Treaty. The methodology for the calculation of public debt considered in this paper is the EFF methodology, ESA 95 and ESA 2010. All of them use the concept of gross debt. The difference among methodologies is in the proposition that according to ESA debt is calculated at market prices. Therefore, the estimated public debt with the ESA Methodology (95 and 2010) reflect the impact of changes in market prices and exchange rates, as well as the liquidity of the assets of the central government.

Also, there are differences in the scopes of the included financial instruments. The ESA methodology includes wider financial instruments than EFF methodology like, currency and deposits, debt securities, loans, insurance reserves, pensions and standardized guarantee schemes.

The main advantage of the ESA methodology is in the comprehensive overview of government duties and that allows comparison among the countries all over the world and not only among the EU countries.

The Republic of Macedonia accepted the ESA 2010 methodology for calculation of general government debt. Thus the calculations of government liabilities are made in accordance with the principles and criteria of the ESA 2010 and the Law on Public Debt of the Republic of Macedonia.

A methodology should not be considered right or wrong until each country evaluates its pros and cons. Thus, countries should classify debt in ways that reflect their perception of the associated risk, which would be related to their macroeconomic policies and perspectives for the future, as well as the difficulties involved in generating quality statistics based on the chosen criterion.

References:

1. Act on Amendments of the Law of Public Debt, (Official Gazette no. 139/2014);
2. Act on Amendments of the Law of Public Debt (Official Gazette No. 35/2011),
3. Act on Amendments of the Law of Public Debt (Official Gazette No. 88/2008),
4. Aline Dieguez B. de Meneses Silva Otavio Ladeira de Medeiros, Public Debt the Brazilian experience, World Bank Publications, Brazil, 2010;
5. Atanasovski Zivko, Public Finances, Faculty of Economics – Skopje, 2004;
6. Dagmar Hartwig Lojsch, Marta Rodriguez-Vives and Michal Slavik, „The Size and Composition of Government debt in the Euro Area”, European central bank, Occasional paper series, October 2011;
7. Decision of the Constitutional Court U.Br.49 / 2006-0-0 of 13.12.2006, (Official Gazette No.137/06)
8. EUROSTAT, European system of accounts ESA 2010, 2013;
9. EUROSTAT, Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016;
10. EUROSTAT, Manuals and guidelines, Manual on Government Deficit and Debt - Implementation of ESA 2010, 2014;
11. Law on Public Debt (Official Gazette No. 165/2014) and the Unofficial Consolidation Law on Public Debt include: the Public Debt Law (Official Gazette no.62/05)
12. Publications Office of the European Union, „Manuel on Government Deficit and Debt – Implementation of ESA 2010”, Luxembourg, 2014;
13. World Economic and Financial Surveys, World Economic Outlook, Coping with High Debt and Sluggish Growth, IMF, October 2012

KATERINA HADZI NAUMOVA-MIHAILOVSKA*

OPPORTUNITIES FOR TQM TRAINING IN ASSOCIATIONS OF ORGANIC PRODUCERS IN REPUBLIC OF MACEDONIA

Abstract

Organic agricultural production offers safe, healthy and high quality food for all. It's being produced by certain standards and approved by certificates that are issued by third party (certification body), which assures that organic standards are respected. It's an approach in which quality addresses all factors that participate in the production of organic food. The organic farming is a way of breeding and processing plants and livestock. The operation is follows one principle which is to create quality in all aspects. This triggered the research on the possibility of applying a managerial method on the creation of the idea that the quality is a liability and responsibility to everyone which is achieved with full commitment and a constant improvement in all aspects of the operation (TQM).

The implementation of TQM in the organization of work in associations of producers of organic products will improve the organization in general will achieve higher level of development and maintain itself on the market. The implementation of TQM in the operation of associations of producers of organic products should start by educating their presidency and then pass it on to all members and to change. The purpose of the paper is to explore the possibilities of implementing the training under the principles of TQM in the associations of producers of organic products in the country. Therefore, members of the associations of producers of organic products in Republic of Macedonia were surveyed on a previously prepared questionnaire.

Key words: organic production, TQM, training, associations, Republic of Macedonia

* PhD, Institute of economics – Skopje, University “Sc. Cyril and Methodius” – Skopje, e-mail: katerina@ek-inst.ukim.edu.mk

JEL classification: Q13; Q19

Introduction

It is doubtless that TQM is an important approach anchored in the belief that long-term success depends on unique commitment to quality in all departments of an organization. Quality has a special importance in agriculture because it is the only and main economic activity that produces and provides food for people, and providing quality food is a responsibility, and a challenge for every national economy. Production of quality food requires management that will continuously monitor the developments through adjusting to changes and improve their knowledge and skills with a full commitment to quality in all aspects of operations. A total improvement and enhancement of the quality of food contributes to the overall improvement of the quality of people's lives, which means: improvement of the living standards, environmental protection, health and safety.

Organic agriculture is an important segment in agriculture whose base is commitment to quality in each phase of working and production, therefore it's clear that TQM and organic production are linked by a very important factor – quality in all spheres/fields of life and work. Actually, TQM is present in each phase of growing plants and livestock products and their processing. It is doubtless that the Republic of Macedonia follows the world trends in organic production and it is a significant part of Macedonian agriculture, however, the producers of organic products and their association as highest form of organization in the Republic of Macedonia are facing problems, such as poor market organization and insufficient quantity of products for sale, therefore it's necessary that the concept of TQM is implanted in overall organization and work. The implementation of TQM in the organization of work will provide improvement for the organization and with that it will win and maintain on the market, thus achieving a recognizable brand, and a higher level of development. The implementation must begin in education and therefore a system of training is required that will enable associations to continuously learn and acquire new knowledge and skills, to be able to adjust to changes, and to develop and maintain on the market.

The main objective of the paper is to explore the trainings that are provided in the associations and based on it to see the possibility of designing

and implementing the training under the principles of TQM in the associations of producers of organic products in the country. For that purpose, the research in the paper is based on analysis of data obtained through interviews with the members of associations of producers of organic products in Republic of Macedonia on a previously prepared questionnaire.

1. DIMENSION, OBJECTIVES AND PRINCIPLES OF TQM IN AGRIBUSINESS

In agribusiness as business with many activities related to food production, quality has special meaning. Besides producing quality food, agribusiness constantly have to follow the requirements of customers or clients that are constantly increasing in terms of quality. These requirements restructure agribusiness so that it is more focused on continuous improvement of quality in the production process. This will entail greater cooperation of employees and creating teamwork, and thus employee satisfaction. This shows that the total quality management system should be present in agribusiness from several aspects:¹

- Continuous improvement of product quality.
- Continuous improvement of quality of work.
- Greater knowledge of the requirements of customers/consumers.
- Creating teamwork.
- Highlighting individual employees regarding their ideas and suggestions and thus creating a leadership.
- Creating employee satisfaction.

Those are the principles of TQM maintained in agribusiness. Based on them, the following tasks of TQM can be allocated³:

- Defining the objectives and strategy of the company or organization.
- Creating a model or structure to carry out activities.
- Choice of methods and techniques of TQM.

¹ Mitreva E., Chepjunoska V., Prodanovska V., "TQM strategy in the design of an quality system in the agribusiness", Научно-практическа конференция с международно участие, Свишов, 2009

- Optimizing the content, process and activities.
- Adoption and harmonization of relevant decisions and solutions activities.

According to Krieger and Schiffer, good agricultural practice (good agricultural practice - GAP), good hygienic practices (good hygienic practice - GHP), good manufacturing practice (good manufacturing practice - GMP) and good commercial practice (good trade practice - GTP) are a base for total quality management in agribusiness.² Together with HAC-CAP (Hazard Analysis Critical Control Point Systems) enable continuous improvement of product quality and quality of work.

Hence, the implementation of TQM in agribusiness is a systematic and complex process which primarily requires the application of the above practices and the use of standardized procedures in all processes, implementation of methods and techniques for better performance, optimizing the process and setting of good planned information system. To this, other activities should be added such as: creating business policy and culture, creating a dynamic structure of the company or organization, establishing a system of education and motivation of employees, optimizing the cost of quality, establishment of logistical support system and production of programs and projects for quality. TQM in agribusiness should be understood as a system of quality improvement in all areas of operation, starting with the idea or vision to produce high quality product which is expanding in all areas of operation and activity.

2. CHARACTERISTIC OF TRAINING UNDER THE PRINCIPLES OF TQM

The first and most significant step in the implementation of TQM is the education because it provides the necessary knowledge about the quality and the overall idea of TQM. Thereby, it is necessary to study all elements of quality, all the specifics of every function (department, sector) in the company or organization and all aspect of the problem (technological, economic, social, psychological, etc.). During the initial ap-

² Krieger S., Schiefer G., "Quality Management in Europe and Beyond", AFITA/WCCA JOINTCONGRESS ON IT IN AGRICULTURE, 2004, <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.200.1930&rep=rep1&type=pdf>, 2.10.2013

plication of the knowledge, they acquire new knowledge of the practice and further incorporated into education programs to employees. Once the system for quality is being introduced, a testing is done in order to determine whether the model is suitable. The testing is focused on the way the system applies the standard procedures for executing the tasks, the way it has applied the techniques and methods in the control checks, the expenses and other additional matters. In order for it to be carried out successfully, another research and additional education is required. At the end, when the system for quality is approved, during its application it is being developed and upgraded according to the increase in the knowledge that comes from the various activities of the system in every function of the operation of the organization or company. This shows that in fact, the education in the system of quality is demonstrated through PDCA circle (Plan-Do-Act-Check).

The purpose of education under the principles of TQM is to build knowledge and awareness among employees or members, to better and efficiently accomplish the tasks of quality, i.e. the activity of the company or organization. Top management has the task to take care of the education and training of employees, i.e. planning of the educational process for quality assurance. The plan is developed according to the needs of staff and in accordance with their qualifications and the tasks they perform in the company. The program should be based on humanitarian principles and its realization to be on the basis of clearly defined desire and interest of participants in the process of quality assurance, not under pressure and force. Therefore it should start to develop from the company and organization in collaboration with scientific experts - specialists and experts in various fields. Teaching should implement TQM experts of the highest scientific, professional and educational institutions on the one hand and the economy on the other.

Education and training of employees are conducted through various forms, such as:³

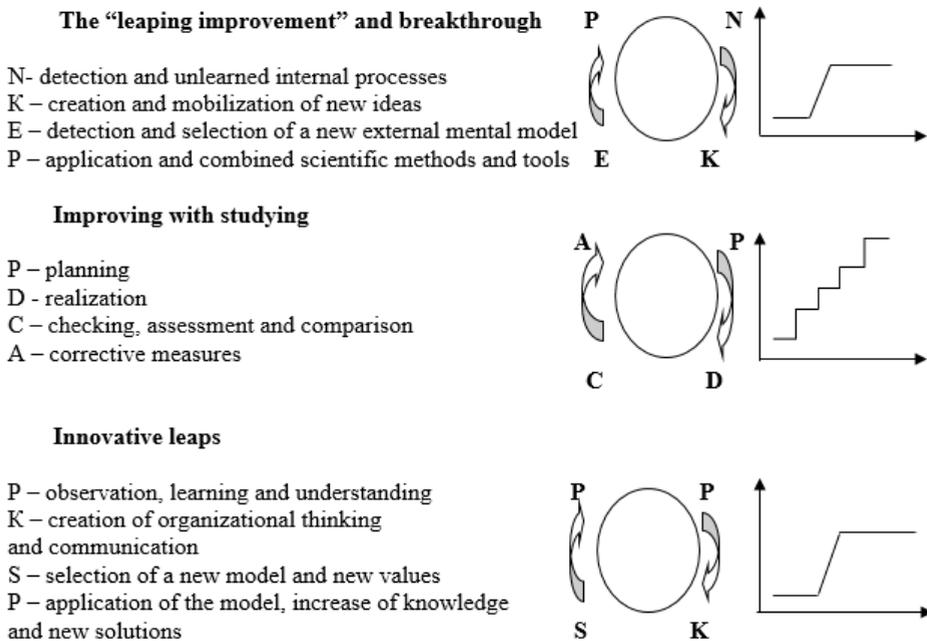
- Participation of individuals in seminars, conferences, symposia and conferences.

³ Badungodage V., Mendis M., Mudannayake M., & others, "TQM in HRM", University of Kelaniya, 2007

- School of quality at different levels (quality management, quality control, etc.).
- Seminars in the enterprise for various problems related to quality.
- Creative workshops of individual employees to perform tasks in order to improve performance and to improve quality.

According to Juran, “leaping improving” can radically improve performance with a visible lack of continuity with the existing situation and a breakthrough is a radical change, dynamic and resolutely move towards a higher level and better performance.⁴ (Figure 1)

Figure 1 Learning with approach of TQM



Source: Heleta M., “Menadžment kvaliteta”, Univerzitet Singudum, Beograd, 2008, p. 115

“Leaping improvement” and a breakthrough in associations aim to bring in a “learning organization” on short notice, which means a systematic ap-

⁴ Honapour A., Jusoh A., Nor K., “Knowledge management, TQM and Innovation: A New Look, <http://www.cielo.cl/pdf/jotmi/v7n3/art03.pdf> (16.04.2013)

proach to learning. A systematic approach to learning means the process of acquiring and understanding of knowledge and experiences can lead to improvements, changes and innovations involving more stakeholders and relevant parties such as advisory bodies, consultancy companies, institutions for education and research, Internet, producers individually and/or in the form of different associations.

Also, motivation and communication play a major role in the implementation of TQM because they include all stakeholders. It is an attraction for certain work resulting from factors such as: performing work to which there is affinity, vision and personal qualities of management, opportunity for advancement, the possibility of self-improvement and improvement in general, compactness and expertise of the team with highly developed work ethics and interpersonal relations, and more. In order to gain quality of work, it is necessary to motivate the staff which is not a simple task, as the factors for that vary from one person to another, between different periods of time and other conditions (environment) such the position they hold etc. Generally, the factors can be material and psychological. The important aim of motivational activities is for everyone to be familiar with the idea that quality is the goal for everyone. Motivation is essential to reach all the knowledge, the will to endure and overcome all the resistances that occur for everything that is unfamiliar, and new energy to overcome it. Communication encourages motivation, change of attitudes and allows people to gain deeper thoughts on various issues.

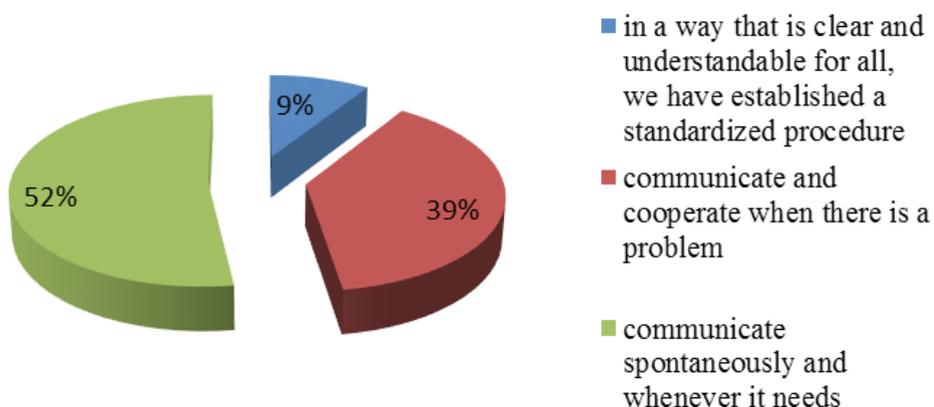
3. ANALYSES OF SITUATION REGARDING THE TRAINING AND EDUCATION IN ASSOCIATIONS OF ORGANIC PRODUCERS IN REPUBLIC OF MACEDONIA

Because the purpose of the paper is to explore training that is provided and to see the possibility of designing and implementing the training under the principles of TQM in the associations of producers of organic products in the country, the survey was raised among the associations members of Federation of Producers of organic products as highest form of organized associations in the country.⁵

⁵ The questionnaire was sent to the highest form of organized associations in the country - Federation of Producers of organic products which includes nine regional associations, of

On the question, “How is the cooperation and communication among members?”, thirty-four (34) respondents said they communicate spontaneously and whenever necessary, twenty-five (25) communicate and cooperate only when there is a problem and six (6) respondents answered that it is a way that is clear and understandable to all and have established a standardized procedure (Graph 1). This shows that the cooperation and communication among members takes place only if a need arises, i.e. if there is a problem pointing to the absence of clear and comprehensive cooperation with standardized procedure that is of great importance for successful implementation of TQM.

Graph 1 The cooperation and communication among members



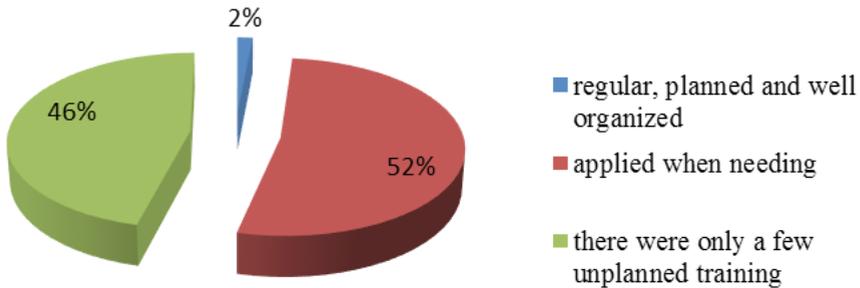
Source: Own research

On the question, “How is the situation with the training of members of the association?”, thirty-four (34) respondents said that they applied only where necessary, (30) that there were several unplanned trainings and one (1) replied that trainings regularly take place and are well organized (Graph 2). The responses showed that training courses are an important segment

which four (4) Associations ("Organik kaki" – Valandovo, "Aronia" - Gevgelija, "Ovcepoliski eko-proizvodi" - Sveti Nikole and "Eko-Sar" - Gostivar) and sixty-five (65) members - manufacturers responded to the questions in the period November 2012- March 2013

in the introduction of changes and new ways of working are implemented disorganized and in need, which in turn suggests that the willingness of associations for the introduction of TQM as a new way of work and organization is small and you need to examine the need for the introduction of continuous training to improve the work of associations.

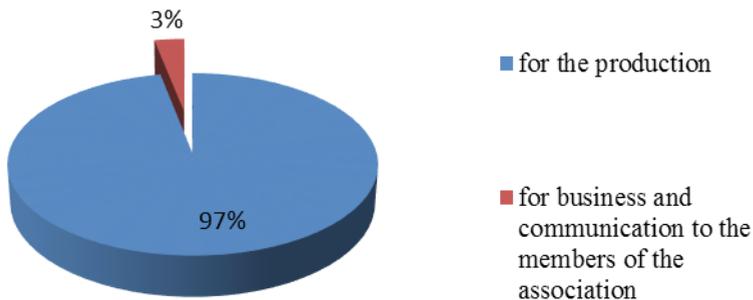
Graph 2 Condition with the training of members of the association



Source: Own research

To the question, “For what purpose are training usually organized?”, sixty-three (63) answered for production and two (2) for business operation association (Graph 3). It shows that the associations aim to improve production and less to work and communicate which also represents an important part in achieving quality production.

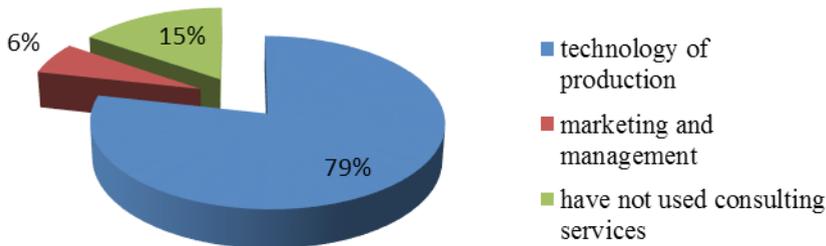
Graph 3 The purpose of training



Source: Own research

On the question, “Which areas you have used consulting services for?” Fifty-nine (51) respondents said that they have used consulting services for technology production, four for(4) marketing and management, and ten haven’t used any services (Graph 4). The responses show that the use of consulting services for improving the production, is reduced.

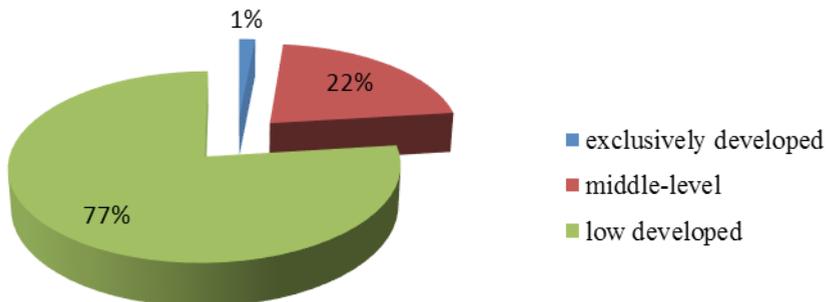
Graph 4 Areas of consulting services



Source: Own research

On the question, “What kind of cooperation do you have with scientific research, university and other educational institutions?”, fifty (50) said that it was developed at a low level, ten (10) don’t have any kind of cooperation, four (4) respondents said that they have developed an average level of cooperation, and one (1) replied that the cooperation was highly developed (Graph 5). Responses show that cooperation with foreign specialists, experts and trainers is not developed and that the associations are very concerned regarding communication with external associates.

Graph 5 Cooperation with scientific research, university and other educational institutions



Source: Own research

It can be concluded that the associations of producers of organic products use no or very little advice and consultation for production and for the operation of the organization. Also, the trainings take place unplanned and apply to one activity - production. Little attention is paid to permanent cooperation and communication among producers, hence it is logical that the main problem that the producers face is placement and market shares.

4. THE TRAINING UNDER THE PRINCIPLES OF TQM IN ASSOCIATIONS OF ORGANIC PRODUCERS IN REPUBLIC OF MACEDONIA

The implementation of TQM must start from training and therefore it is necessary to make a system that associations will constantly learn and acquire new knowledge and skills from, to be able to adjust to change, in order to develop and maintain on the market. Associations wishing to apply the system of TQM should use the approach of continuous improvement which consists of a combination of “leaping improvement” or a breakthrough to a new performance, application of learning - training learning (i.e. learning how to learn), improve the learning from their own experiences and use the knowledge of others and innovative jumps (Figure 1). The model of learning with associations of producers of organic products should be in a cycle of four stages: observation and understanding of knowledge and experience, specifically examining the formation of concept and enhance knowledge in the form of change and innovation.

Complex knowledge of TQM should start from the presidency of the association, the first task of the associations wishing to apply TQM is to ensure conditions for successful implementation of education primarily to the Presidency, and then to all members. It requires detailed elaboration, using the method of herringbone - to answer the questions, who, when, where and how the association should acquire the necessary knowledge for successful implementation of TQM through the application of quality circles. The process of education should take place in the form of cycle whose end result is to promote education and opportunity for promotion of all functions in the operation of the association (Figure 2). It should include the following steps:⁶

⁶ Ibid

1. Planning and determining the need for education - the presidency of the association determines the need for education, thus prepares a plan for the process of education members.

2. Preparation of educational program and selection of trainers (teachers, specialists, experts) - the stage which selects the method for training and trainers. Training can be carried out through work - external and internal. Internal methods for training can be: tutoring, shift between different work positions, a method of apprenticeship and planned active workers. The associations should use the method of tutoring because it implies a training under the supervision of a mentor who should be a properly qualified person who handles the problems in the organization, a member who has the knowledge and education for the area that requires training, an area where the causes of problems are identified alongside with the faults and defects. The external method of training is based on theory (lectures and tutorials) simulations and research on behalf of the universities and institutes. The lectures are held by specialists, experts and teachers, thus increasing the communication between the members, employees from different departments, universities and organizations is increased, and knowledge and experience is exchanged.

3. Selection of participants - associations select the participants for an activity based on the conducted survey and testing. In selecting participants they should make their development program for education and training as well as trainers.

4. Implementation of instruction - takes place in a specific place in certain conditions. The quality of training depends on several factors, primarily the interaction between trainers and participants arising from the knowledge and skills of trainers, the interest of the participants, literature, work conditions, responsibility and continuity.

5. Verification of knowledge - is testing the effectiveness of the lecturers, the capacity of the participants and the implementation of the program (training) through questions, discussions, tests and introducing the program into practice.

6. Correcting program and establishing a model of education - essentially an assessment of the success of the program is established on the

basis of evaluation of knowledge. Corrections can refer to the content of the program, the trainers, the interest for the course as well as working conditions. After the faults are identified, corrective measures are taken in order to eliminate them, or establish a model of education.

Thus realized, quality circles and associations are continuing their work toward continuous learning and improvement.

Figure 2 The process of education in associations with TQM



Source: Honapour A., Jusoh A., Nor K., “Knowledge management, TQM and Innovation: A New Look, <http://www.cielo.cl/pdf/jotmi/v7n3/art03.pdf> (16.04.2013)

The first and most important step in the implementation of the training is the identification and analysis of the training needs by:

- strategic point of view coupled with the knowledge, skills and experiences;

- functional aspect, identification of functional problems in the association;
- individual aspect, monitoring the role of the members (Figure 3).

No matter how well-identified training needs, mediation training will be effective only if selected and set appropriate conditions and training methods. Then, training is carried out and it's necessary that the members know and understand that every new or changed responsibilities are part of a continuous process, important not only during training. They also need a regular evaluation (assessment of the total value of the training program and in social and financial terms). Link the needs for training with their goals, in order to create an objective that is based on the outcome.

Training can only be effective with the support and consent of the association as a team and teamwork by practicing and supporting new skills and knowledge. Active participation is an essential part of the process and the only way we can provide improvement, successful training and placement practice to use and re-evaluate.

Figure 3 Cycle of training according to TQM in the associations of producers of organic products



Adjusted to Hafeez K., "TQM, Innovation, Organizational learning and Knowledge economy: Is there a connection?", <http://qc.hbmeu.ae/QC4Proceedings/PDF/TQMOrganisationalLearning.pdf>, (01.10.2012)

The application of this methodology may run into difficulties because of the mentality of the producers who usually oppose external (foreign) models of learning and changes caused by fear of losing traditional values and their own identity and others who gladly accept developments and changes without detailed analysis and application and instant dissociation of the tradition. The application of the successful model of education should also be a blend of traditional and trendy civilization values that govern the world.

Conclusion

Quality in agribusiness is an important tool that enables successful placement of agricultural product because it expresses the extent of its durability, reliability, accuracy and visibility by the consumer. Besides producing quality food, agribusiness constantly have to follow consumer demands who needs constant increase in terms of quality. These requirements restructure agribusiness, so it's more focused on continuous improvement of quality in the production process. It entails greater cooperation of members and creating teamwork, and thus member satisfaction. This shows that the TQM as a way of organization and operation should be present in agribusiness because it leads to greater knowledge of the requirements of customers/consumers; improves the quality of work and as a result - product quality; highlights the ideas and suggestions of members and creates leadership thinking, employee satisfaction and teamwork.

The first step in the implementation of TQM is education, therefore the purpose of training under the principles of TQM should build knowledge and awareness among members to better and efficiently accomplish the tasks of quality, i.e. the activity of the company.

The educational process should take place in the form of cycle whose end result is to improve the knowledge and opportunity to promote

all functions in the operation of the association. This cycle represents the initial stage in the creation of associations as “learning organization.” It need not to occur only when necessary or in case of a problem, but as a habit and a routine. Consequently, existing knowledge is constantly utilized in the strategic objectives of the association and it is easily prepared to face the changes ahead.

References

1. Badungodage V., Mendis M., Mudannayake M., & others, “TQM in HRM”, University of Kelaniya, 2007
2. Certo S.C., Certo S.T., “Moderni menadzment”, 10 izdanje, Mate, Zagreb, 2008
3. Dahlgaard J.J., Kristensen K., Kanji G.K., Fundamentals of Total Quality Management, Taylor & Francis, London and New York, 2002
4. Hadzi Naumova-Mihajlovska K., ““Opportunities and prospects for application of TQM into association’s producers of organic products in the Republic of Macedonia” (2014) Doctoral dissertation, Institute of economics – Skopje
5. Hafeez K., “TQM, Innovation, Organizational learning and Knowledge economy: Is there a connection?”, <http://qc.hbmeu.ae/QC4Proceedings/PDF/TQMOrganisationalLearning.pdf>, (01.10.2012)
6. Honapour A., Jusoh A., Nor K., “Knowledge management, TQM and Innovation: A New Look, <http://www.cielo.cl/pdf/jotmi/v7n3/art03.pdf> (16.04.2013)
7. Heleta M., “Menadžment kvaliteta”, Univerzitet Singudum, Beograd, 2008
8. Krieger S., Schiefer G., “Quality Management Schiemes in Europe and Beyond”, AFITA/WCCA JOINTCONGRESS ON IT IN AGRICULTURE, 2004, <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.200.1930&rep=rep1&type=pdf>, 2.10.2013
9. Mitreva E., Chepjunoska V., Prodanovska V., “TQM strategy in the design of an quality system in the agribusiness”, Научно-практическа конференция с международно участие, Свищов, 2009
10. <http://www.fpopm.com> 2.02.2013

MARKO ANDONOV*
ZORAN JANEVSKI**
ELENA DAVITKOVSKA***
IRINA MAJOVSKI****

**CURRENT LEGAL SETTING AND FUTURE MARKET
REGULATORY CHALLENGES OF SECURITIES MARKET IN
THE REPUBLIC OF MACEDONIA**

Abstract

The legal setting of the Macedonian capital market primarily reflects the Law on Securities and all the relevant bylaws. The aforementioned law was enacted in November 2005 and amended on several occasions. It is largely harmonized with the relevant EU Directives, as well as the standards and principles of the International Commissions on Securities (IOSCO). One objective of the paper is to depict and analyze the current legal and institutional setting of the domestic capital market. In this regard, all the significant aspects of the relevant regulations will be highlighted. At the same time, we will review the latest regulatory challenges in this area resulting from the development of two newly drafted laws, which are expected to shed a new positive momentum on the Macedonian legislation in this field following their adoption and to contribute to the dynamic development of the domestic capital market. In this way, the paper will determine the degree of compliance of the said draft legis-

* PhD, Dean and Associate Professor, School of Law, University American College Skopje, e-mail: andonov@uacs.edu.mk

** PhD, Associate Professor, Institute of Economics - Skopje, Ss. Cyril and Methodius University in Skopje, e-mail: zoran.janevski@ek-inst.ukim.edu.mk

*** PhD, Assistant Professor, Institute of Economics - Skopje, Ss. Cyril and Methodius University in Skopje, e-mail: edavitkovska@yahoo.com

**** PhD, Assistant Professor, Institute of Economics - Skopje, Ss. Cyril and Methodius University in Skopje, irina@ek-inst.ukim.edu.mk

lation with the relevant EU directives and regulations. We will finally draw conclusions from the legal analysis displayed in the paper.

Keywords: capital market, securities, regulation

JEL classification: K22

Introduction

When it comes to the Macedonian market of securities, it seems that in the relatively short period of twenty years a significant progress was made in terms of creating a legal framework which allows businesses to reorganize, consolidate and increase their competitiveness in the domestic and foreign markets. Undoubtedly, the legal framework for securities (hereinafter S) to a high degree complies with the relevant regulations in the European Union, and it also includes the principles and standards accepted by the wider international community. Besides the Law on Securities (hereinafter LS), the legal framework in the field of securities in Macedonia consists of the Law on Takeovers, Law on Investment Funds and Company Law, Banking Law, the Foreign Exchange Law, the Law on prevention of money laundering and terrorist financing, the Regulation in the area of taxation of securities, and others.

The basic law regulating operations with securities in the Republic of Macedonia is the Law on Securities and the bylaws that arise from it. The Law on Securities dates from November 2005 and has been repeatedly amended. The law is harmonized with the relevant EU Directives, as well as the standards and principles of the International Organization of Securities Commissions (IOSCO), whose full member since 1994 is the Macedonian Commission for Securities. The Law on Securities regulates: the manner and requirements for the issuance and trading of securities; the manner and conditions for requirements for securities clearing and settlement of commercial transactions and non-trading security transfers, and restrictions on the rights of ownership of securities; and the manner and requirements for the functioning of the market of securities and its authorized participants.¹

¹ Law on Securities (unofficial consolidated text) (Official Gazette No.95 / 2005, 25/2007, 7/2008, 57/2010, 135/2011, 13/2013, 188/2013, 43/2014, 15/2015, 154/2015 and 192/2015)

The Law on Securities is based on the principles of legality, transparency, non-discrimination, competition, protection of owners of securities and investors, thus strengthening and increasing legal certainty and stability of securities market in general.

1. ISSUANCE, OFFER AND SALE OF SECURITIES

This section concerns the procedures and actions to be taken regarding the issuing, offering and sale of securities. It defines and regulates who can issue securities and in what form, the procedures for public offer (requesting approval to issue, the documentation to be submitted, the institution that reviews the application and the submitted documentation, time frame for deciding, procedure for registration and payment of securities as well as implementation and (un)successfulness of the public offer, private offer, purchasing own shares, as well as exemptions from giving approval to issue securities. Hence, it is important to know that in Macedonia, securities may be issued by: the Ministry of Finance on behalf of the Republic of Macedonia, the National Bank of Macedonia, the municipalities, the City of Skopje, joint stock and limited partnerships companies with shares and other domestic and foreign legal entities. The securities are issued and considered to be a dematerialized form. The shares have a nominal value, which can be expressed in MKD or in foreign currency. No matter how the nominal value is expressed, commercial transactions in the country are carried out in MKD.²

The issuance of securities in the primary market, including the sale of own shares, is made after a prior approval by the Commission, except in exceptional cases defined by law. The issuance of securities may be by public or private offering.

A) Public offer

The issue, offer and sale of securities through a public offer is made after prior authorization from the Commission at the request of the issuer. A Commission approval for the issue of securities is not required

² Manual for training and taking the exam for working with Securities, Commission for Securities, Skopje, 2015, p.27

for the issue of securities through a public or private offering whose total amount does not exceed 25, 000 EUR in MKD. The Commission, on the basis of the obligatory documentation, makes a decision on approving or refusing the application for issuance of securities through a public offer within 60 calendar days from the date of submission of the application to the Commission. The issuer is obliged to start the procedure of registration and payment of the offered securities within 30 calendar days from the receipt of the approval by the Commission. The deadline for the public offer cannot be longer than 12 months from the date of commencement of registration and payment of the securities³.

The public offer of securities shall be considered successfully completed if within the determined legal deadline at least 60% of the securities offered in the Prospectus are registered and paid, unless the issuer has not provided in the Prospectus a higher percentage of registration and payment of securities for the emission to be successful. Upon completion of the public offer, all securities that are not paid cannot be subject to sale. After successful completion of the public offer of securities, the issuer shall register the securities at an authorized depository.

B) Private offer

Private offer is an offer for registration and payment of securities which is addressed to no more than 20 people, individually referred to in the act of issuing securities, which are not shareholders in the corporation and are not related with the shareholders or the shareholders' company, unless stipulated otherwise by another law or the obligation of the shareholder to increase their participation in the share capital is requested by an authority or institution responsible for oversight or supervision of the operations of the companies based on LS or other law and:

- Which is addressed only to institutional investors,
- In the case of increase of the principal assets of the company,
- In the case of a conditional increase of the core capital, and
- In the case of a loan that was transformed into a deposit in the company in the process of increasing the company's equity when the loan is given by a single company shareholder.

³ Ibid, p.29

2. DEPOSITORY FOR SECURITIES, REGISTRATION OF SECURITIES, NON-TRADE TRANSFERS

For registration of securities, settlement of trade transactions and performing non-commercial transfers of securities, a depository for securities was founded. The Depository functions as a self-regulatory organization. The functions of the depository are:⁴

- a) Registering the issuance and transfer of securities in the Republic of Macedonia in electronic form (keeping a register of securities);
- b) The issuance of international identification number of securities (ISIN) for all issues of securities;
- c) Registration of owners of securities;
- d) Settlement of trade transactions under the principle delivery versus payment;
- e) Performance of non-trade transfers;
- f) Providing conditions for lending securities;
- e) Monitoring the financial health of its members in order to manage the risk associated with a possible settlement of trade transactions, and
- h) Performing additional services to issuers of securities.

The rights of ownership of the securities result from the registration of securities at the expense of the owner in the depository and are transferred by registering the securities on the account of the new owner in the depository. In this context it is important to note that the rights of the securities are acquired, restricted or transferred by a corresponding entry on the account of the new owner in the securities depository, unless the law stipulates otherwise.⁵

In depository all commercial and non-commercial transfers made with securities in the country are recorded. Permitted non-commercial transfers provided by the LS are:

⁴ Law on Securities (unofficial consolidated text) (Official Gazette No. 95/2005, 25/2007, 7/2008, 57/2010, 135/2011, 13/2013, 188/2013, 43/2014, 15/2015, 154/2015 and 192/2015)

⁵ Ibid

- 1) Contract as a gift;
- 2) Realization of a contract for loan of securities,
- 3) Inheritance, and
- 4) Court decision.

The settlement of all trading transactions with securities shall be made in the depository. Republic of Macedonia accepted the principle of settlement “Delivery versus payment”. Namely, it means that the obligations to transfer securities arising from the trade transactions are settled with simultaneous change of the entitlement of securities from the seller’s account to the buyer’s and payment of the amount of money for purchased securities. The settlement of trade transactions with securities can be performed immediately, but no later than three working days after the conclusion of the transaction. The Depository supervises the settlement of trade transactions of its members in order to detect any violation of the regulations of the depository or other offenses by members of the Depository.

3. TRADING SECURITIES - STOCK EXCHANGE

In Macedonia there is an obligation that all commercial transactions take place through an organized market for securities, i.e. the Stock Exchange, which was commissioned by the Commission for Securities (CS). Trade transactions that are not made by an authorized Stock Exchange are void. The fact that stock market as an institution of securities in the country has a long tradition reflects the appropriate legal treatment of its operations viewed from several aspects. The Law on Securities is in line with the strengthening of the institutional placement of stock market securities. In that sense, similar to the depository, the stock also explicitly acquires the status of a self-regulatory organization and adopts rules of conduct and discipline in order to enforce their own laws.⁶

The law defines and regulates the establishment (license to establish, because more Exchange markets can be set up), the functions of the stock market, who may be a shareholder in the stock market, the management bodies, internal regulations, operational rules, trading with securities,

⁶ Петковски, М. (2009) Финансиски пазари и институции –второ изменето и дополнето издание, Универзитет „Св. Кирил и Методиј“ – Економски факултет – Скопје, p.133

conditions and restrictions in relation to the listing of a stock exchange, supervision over the operations of the stock exchange, reports and work program to be submitted to the CS.⁷ It is important to note that the Stock Exchange of Securities has adopted rules for trading.

The Stock Exchange shall require the Commission to agree on: a) the Statute and any amendments; b) membership rules, rules for trading, listing rules, rules of arbitration, rules of conduct and discipline measures and any amendments thereto; c) tariff and all its amendments, and d) the various forms of connecting and merging with other stock exchanges.⁸

The Commission shall also approve the appointment of Director of the Stock Exchange at the request of the stock exchange. In terms of documentation relating to trading, we would like to emphasize that the original is kept at least five years and on an appropriate electronic media. The Commission supervises the overall operation of the Exchange and its members.

4. THE SECURITIES AND EXCHANGE COMMISSION

In most countries with developed market economy, the Securities and Exchange Commissions (SEC) are founded for regulation of the market of securities. Some are set up as independent legal entities. The main role of the Commission is maintaining the integrity of the capital market and increasing investor confidence, which is necessary for the accumulation and concentration of capital, providing standards of supervision of all other self-regulating market participants and imposing sanctions on those who do not respect the norms and rules set by regulators in order to protect the interests of investors.⁹

The SEC is the institution responsible for legal and efficient functioning of the capital market in the country, which cares for the protection of investors' rights in order to strengthen the public trust in the institutions

⁷ Беличанец, Т. (2010) Банки, инвестициски фондови, берзи, Универзитет „Св. Кирил и Методиј“ - Скопје, Правен факултет- Скопје, р. 87

⁸ Law on Securities (unofficial consolidated text) (Official Gazette No. 95/2005, 25/2007, 7/2008, 57/2010, 135/2011, 13/2013, 188/2013, 43/2014, 15/2015, 154/2015 and 192/2015)

⁹ Беличанец, Т. (2010) Банки, инвестициски фондови, берзи, Универзитет „Св. Кирил и Методиј“ - Скопје, Правен факултет- Скопје, р. 90

of the market of long-term securities in the country. Also there are provisions that the SEC is given powers to conduct investigations, control, take measures and impose sanctions against participants on the security market. In this section it is important to emphasize once again that the SEC is an autonomous and independent regulatory body with public authorizations within LS.¹⁰

In terms of LS, the Commission controls the operations of the authorized participants with securities due to the application of LS, regulations adopted on the basis of LS and rules of self-regulatory organizations.

5. FUTURE REGULATORY CHALLENGES ON THE MACEDONIAN MARKET OF SECURITIES

In the upcoming period, one of the main challenges of the Macedonian market for securities will be further harmonization of national legislation with the relevant EU directives and regulations. This is a process which is currently underway and which primarily means enacting two new laws for regulating the market of securities in the country.

As a result of reforms, investors and professionals in the capital markets will apply the same rules that apply in all EU Member States, and the same level of protection of their rights. The amendments are expected to strengthen and enhance the area of transparency of investment companies by obtaining more information on the transactions themselves, which will be of great importance for investors. Many more details will be developed regarding investment companies and their rights and obligations. Furthermore, the novelties will clarify the procedure for cooperation when an investment company from Macedonia wants to cooperate with such a company from the EU. Part of the planned innovations will enter into force on the date of entry to the EU. Also, one additional way to protect the rights of investors, both administrative and court proceedings. The proposed legislation does not reflect only the EU requirements in this area, but it takes into account the current level and the specifics of the domestic market, which is especially important.

The main legal acts of the EU, such as the Directive and Regulation on Markets in Financial Instruments II, the Regulation on Market Abuse

¹⁰ Manual for training and taking the exam for working with Securities, Commission for Securities, Skopje, 2008. p. 58

II, part of the Directive on Regulation of Capital Requirements IV, the Prospectus Directive, the Transparency Directive and the Directive on the admission of securities value of the official listing on a stock exchange, will soon become part of the Macedonian legislation.

The current Law on Securities, which was elaborated above, will be replaced by two new regulations: **Law on Financial Instruments and the Law on Prospectuses for Securities and obligations of issuers to transparency.**

6. BASIC CONCEPT OF THE DRAFT LAW ON FINANCIAL INSTRUMENTS

The Law on financial instruments will regulate the entire process of trading in financial instruments, including the infrastructure of the capital markets. The scope of the law includes investment companies, providers of trade data and market operators, places of trading, a central depository for securities and investment guarantee fund. Among other things, the law gives definitions of securities, financial services, market abuse, etc. Capital requirements for investment companies are also included in this law. In addition, part of this law is the insolvency regime for investment firms.¹¹

It could be pointed out that the general conditions laid down in the current legal regime for the Central Depository of Securities, the compensation scheme for investors and guarantee fund and the insolvency of investment companies remain unchanged. Also, it is important to mention that in the Draft Law there is a new comprehensive list of financial instruments, consisting of different types of transferable securities, instruments on the money market, shares in collective investment funds and other types of financial derivatives.

The novelty is that the law introduces an entirely new nomenclature for intermediaries in the market, which in the current law are referred to as brokerage houses. The draft law contains the term “investment company”. It is important to point out that in the draft law on financial instruments the internal organization for investment companies is also determined. In relation to the stock market, it should be kept in mind that

¹¹ “Introducing of the relevant EU Directives in the new regulatory framework of the Financial Market in the Republic of Macedonia” – manual, Alternative Consulting, PWC, Skopje, 2016, p.7

the term “market” is not used in the draft. Instead, in accordance with the provisions of MIFID II, three so called “Trading Places” are introduced. It is the concept of a regulated market, multilateral trading platform (MPT) and organized trading platform (OTP).

The initial capital (minimum licensing capital) of the investment companies is set at a level of MKD equivalent of EUR 730, 000. However, this amount is required for the award of so-called “full” or “large” license to companies that would like to offer the entire range of investment services, including operations for own account or registering transactions based on company commitments. Investment companies that have no intention of working for their own account or enroll cross sanctions based on company commitments, but want to keep money or security customers, should have a minimum initial capital of EUR 125, 000. Finally, those who do not intend to work for their own account or record transactions based on company commitments and who will never keep money and securities customers should have a minimum initial capital of EUR 50, 000¹².

The draft law on financial instruments has integrated the EU framework for market abuse, in particular the Regulation on market abuse, which comes into force in June 2016. Some of the proposed changes will take effect on the country’s accession to the EU. Generally, new conditions provide a wider scope to include all financial instruments traded on the regulated market or MTP/OTP in the country.

Regarding the position of the regulatory body - (SEC), it should be emphasized that the overall concept is not changed. The status, composition, operation and powers of the Commission for Securities is in accordance with international standards of those government officials and will not be changed. The draft Law merely makes clear distinction between the functions, tasks, powers of the SEC and supervisory measures and sanctions.

The draft law introduces the concept of prudential supervision and prudential requirements which features the international standard term for supervision of compliance with the conditions for financial well-being for investment firms and credit institutions. Prudential supervision of the stakeholders of the capital market will be divided as it is now divided between the CS and banks. Prudential supervision of investment companies will be implemented by the CS, while supervision of credit institutions (banks) will be implemented by the Central Bank.

¹² Ibid, p. 15

7. BASIC CONCEPT OF THE DRAFT LAW ON PROSPECTUSES FOR SECURITIES AND OBLIGATIONS OF ISSUERS TO TRANSPARENCY

The main purpose of the Law is to ensure investor confidence and market stability by creating the conditions necessary for investor protection and the development of transparent, fair and efficient capital market. The approach used in the preparation of the draft law is the implementation of the conditions stipulated in the relevant EU legislation, taking into account the specificities and the level of development of the domestic market.

Regarding the content of the Prospectus, it should contain information on the issuer and the securities which are offered as well as a summary. The information should be of such quality and quantity that will allow investors to make realistic estimates based on reliable information, assets and liabilities, financial position, profits and losses and prospectuses of the issuer and any guarantor, and the rights associated with such securities.

The Commission decides on public offer of securities in the territory of the country, and admission for trading on regulated markets. There are general requirements such as compliance of the issuer and the securities to domestic legislation, the securities must be freely transferable and other listed in the draft Law. The information on who might have control over the issuer is extremely important for investors because they can have a significant impact on the decision, storage, sale or purchase. For this reason, in the EU legislation there are clear rules for disclosure of such information. The directive on transparency lists detailed requirements for shareholders rights, as well as entitled neutral entities or financial instruments that affect the specific rights. The conditions are listed in the draft Law. The new regime, according to the draft law provides that, where the interest of a person for certain stocks, measured by the control of the right to vote (through acquisition or sale of shares listed on the regulated market and other financial instruments of the shares) exceeds or is less than the established thresholds, such person is obliged to inform the issuer of the changes. The threshold proposed in the Draft Law is 5%, and then at intervals of 5% to 75%.

Conclusion

Undoubtedly, it can be concluded that the current legal framework of the Macedonian capital market in an appropriate way reflects and meets

its needs. Firstly, here we imply the current level of development of the domestic market of securities. However, taking into account the integration processes of RM itself is a need for further harmonization of national legislation on the subject area with the relevant EU directives and regulations. Hence, it is safe to conclude that with the new legal framework, the Republic of Macedonia will be harmonized with EU legislation in the field of market securities and investment services. The basic idea is to establish a highly efficient system for the development of a strong, stable and transparent capital market with high standards of investor protection, which will mean a positive movement in the domestic market of securities, while improving the overall business environment in the country.

References:

1. Barbic, J., (2010) *Pravo drustava, knjiga druga, drustva kapitala, Organzaitor Zagreb.*
2. Mishkin, F. S. &Eakins, S.G. (2005) *Financijska tržišta i institucije, Mate, Zagreb.*
3. Недков, М., Беличанец, Т. и Градишки-Лазаревска, Е. (2009) *Право на друштвата, Правен факултет „Јустинијан Први“, Скопје.*
4. Беличанец, Т. (2010) *Банки, инвестициски фондови, берзи, Универзитет „Св. Кирил и Методиј“ - Скопје, Правен факултет-Скопје.*
5. Петковски, М. (2009) *Финансиски пазари и институции –второ изменето и дополнето издание, Универзитет „Св. Кирил и Методиј“ – Економски факултет – Скопје, Скопје.*
6. Ferran, E. (2008) *Principles of Corporate Finance Law (Феран, Е., Начела на корпоративно финансво право, Просветно дело АД, Скопје, превод на македонски 2009)*
7. *Прирачник за обука и полагање на стручен испит за работа со хартии од вредност, Комисија за хартии од вредност, Скопје, 2015 год*
8. *“Introducing of the relevant EU Directives in the new regulatory framework of the Financial Market in the Republic of Macedonia” – manual, Alternative Consulting, PWC, Skopje, 2016*

UDC 338.121:37(497.7)
338.121:001(497.7)
Original scientific paper

FATMIR BESIMI*
AZIS POLLOZHANI**

EDUCATION AND HUMAN CAPITAL: ECONOMIC GROWTH AND SOCIAL COHESION IN MACEDONIA

Abstract

Economic growth and social cohesion for the Republic of Macedonia as a small economy and young democracy with multiethnic society on its path towards European integration represent very important aspect of successful integration of Macedonia into the European Union. In this context, education plays an important role in society with regards to social cohesion and in terms of economic growth and prosperity. As it seems for the economic growth and the compliance with the criteria for joining the EU, Macedonia should increase the competitiveness of its economy, which primarily implies larger investments in education, research and science, which is expected to enhance innovations, technological development and increase the human capital as important factor of growth taking into account the challenges demographic trends both in terms of migration, and in terms of the age structure of the population.

Key words: education, social cohesion, human capital, innovations, economic growth.

JEL Classification: I2, J1, O1, O3, O4, F22

* PhD, Visiting Senior Fellow, The London School of Economics and Political Science, London, United Kingdom Email: f.besimi@lse.ac.uk

** PhD, Rector, University Mother Teresa, Skopje, Republic of Macedonia Email: a.pollozhani@unt.edu.mk

Introduction

Education is the main pillar of society in profiling its citizens, nurturing their values and their well-being. The role of education in maintaining peace and in the improvement of general welfare is argued in several academic and policy discussion. Its transformational power is necessary, especially in transition societies, and is as such a key tool of all state policies for faster and more efficient transformation of societies towards new challenges.

The historical challenge to become a member of the European Union, places the education as one of its top priorities for the Republic of Macedonia, in order to adapt the society to European values and standards, as the key component in the context of social learning. This is also expected to have an impact on social cohesion which is becoming more relevant in multiethnic society as that in Macedonia.

Education, science and research are becoming more important determinants of economic growth in terms of increased competitiveness of the economy, especially important considering the commitment to the membership of the Republic of Macedonia into the European Union, a larger and more developed market with higher competition. In order to cope with competition within the EU market, the competitiveness of the domestic economy should increase through higher productivity, notably by increasing human capital and innovation through investments in education, science and research.

In the context of economic growth, when it comes to human capital, certainly in the analysis special attention should be given to demographic developments, such as migration, Diaspora and the age structure of the population.

1. DEMOGRAPHIC DEVELOPMENTS

1.1. Migration

The characteristics of demographic trends in the Republic of Macedonia were migration trends abroad and internal movements of population from rural to urban places. Migration abroad after World War II until the 1970s was mainly towards Turkey and to the developed coun-

tries, especially in Europe, USA and Australia. Internal migration from villages to cities started with the industrialization of the urban regions during the 1960s and 1970s. Then, the transition period after the 1990s reopen the migration process that has already taken larger dimensions in the context of internal rural-urban and migration abroad (European Commission, 2015).

The trend of the Balkan exodus, according to the Eurostat, reached about 70 thousand asylum applications in 2014, compared to 10 thousand in the period before the visa liberalization. The first in the list is Kosovo with 35 thousand asylum seekers, followed by Serbia, Albania, Bosnia and Herzegovina, Macedonia and Montenegro. Migration from the Balkans in the 1990s were because of the war in the territory of ex-Yugoslavia (especially in Bosnia and Herzegovina and Kosovo), while in the recent years, migration is mainly for social and economic reasons. Emigration of the population apparently remains a challenge in these decades, as well.

Faced with a large number of migrants, in May 2015, the European Union adopted the Agenda for Migration with urgent measures to overcome the current problems, as well as policies to improve the situation of migration (European Commission, 2015). Urgent measures were focused on saving the lives of migrants, fighting crime trading with people, resettlement and resettlement of migrants in various EU Member States based on the principle of solidarity and cooperation with non-EU countries to prevent migration. The long-term measures to improve the situation of migration include: reducing circumstances that stimulates illegal migration; protection of life and securing external borders; strengthening the common asylum policy; and develop a new policy on legal migration.

1.2.Diaspora

Diaspora as a byproduct of migration is an important economic potential that needs to be anchored to our economic ground. Diaspora from Macedonia in 2010, according to a report by the European Committee for Southeast Europe (European Commission, 2012), is estimated to be about 550 thousand immigrants, meaning about 26% of the country's population with permanent or temporary residence abroad. Another assessment of migration (Diaspora) can be done if we calculate the list of

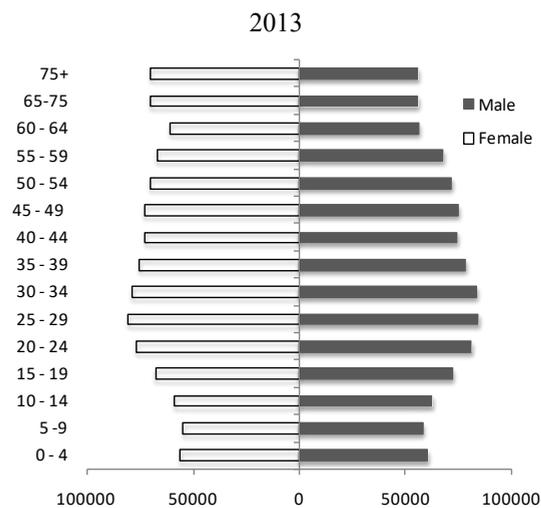
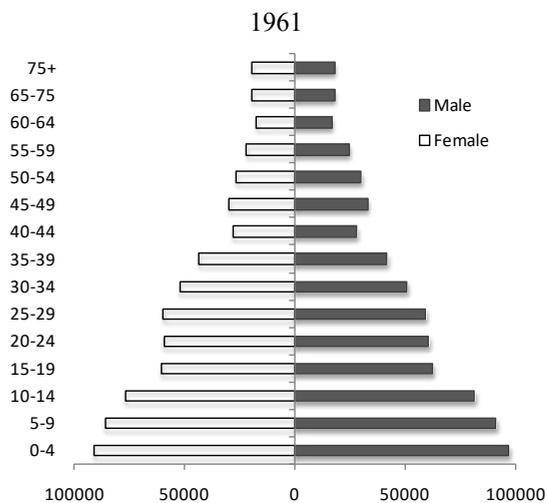
voters in Macedonia, which is 1.8 million people. This is calculated to 2 million inhabitants, where according to the age group over 18, with right to vote, is around 1.5 million, assuming that the lists are cleared, it seems that the difference of about 300 thousand voters is from the Diaspora. Approximately similar estimation for Diaspora can be reach when compared the data from the Health Insurance Fund, according to which 1.8 million people have health insurance, assuming that the rest of 200 thousand persons compared to the general population are in Diaspora. However, the annual statistical data cannot be seen high outflow, namely net emigration of citizens is about 700-1, 000 annually, while the balance turns positive given the immigration of foreign nationals.

It is a structural loss of labor. However, the Diaspora has played and continues to play an important role in our economy. Remittances proved to be a stable factor in the balance of payments over the period of economic transition in Macedonia. Private transfers, which include remittances from the last decade ranged around 13% to 21% of GDP with only remittances exceed a value of one billion euros of foreign exchange inflows in the economy, which are higher compared to foreign direct investment inflow (NBRM, 2015).

1.3. Age structure

People as a resource for development remains a particular challenge in this century of global aging population. Demographic pyramid according to the age-structure of the XXI century apparently flipped up-down - from stable pyramid with a solid foundation, it became a demographic vortex (Figure 1). In Europe in 2012 were about 18% of its population over age 65, while 2050 is expected to reach 28%. Considering the level of development, the population over age 65 in developed countries reaches 23% in developing countries is 9% and in countries with weaker growth is 5%. Macedonian population over 65 years of age in 2013 was 12%, which represents an increase compared with 2002 when it was 10.5% (United Nations, 2013). The same can be said and seen by the average age of the population in Macedonia, which currently is 35-37 years old thus being still younger compared to the EU (about 40-43 years of age).

Figure 1. Population structure by major age groups in Macedonia



Source: State Statistical Office, R. Macedonia

If we look at the age structure of population in Macedonia in 2012, it is as follows: 0-14 (17.1%), 15-64 years (71.0%) and 65+ (11.9%) and can be noticed an ageing trend compared to 2002 when the corresponding age structure was 21.1%, 68.3% and 10.6%. Important news from the economic aspect is the fact that it has increased the portion of the working population to 71% and it can affect economic growth if we can create more jobs, it will also generate more public revenue that could be used for investments in education and science, youth and adults, social security and pensions for the elderly.

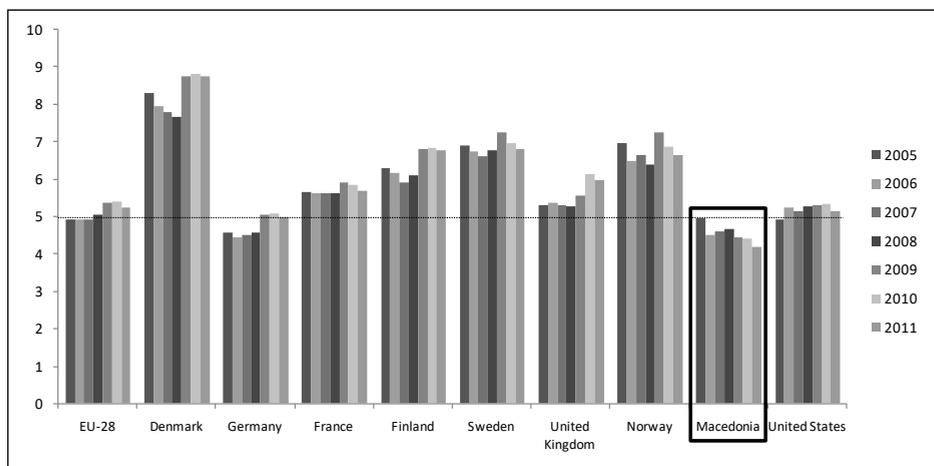
2. EDUCATION, HUMAN CAPITAL AND INNOVATIONS AS A FACTOR OF ECONOMIC GROWTH

2.1. Education

Following the experience of developed countries the response to demographic challenges seems to be investment in people and creation of human capital! The creation of human capital will boost the growth potential of the economy across the demographic challenges of migration flows and the ageing of population. Knowledge-based economy implies that investments in education and science, innovation and increased economic productivity! Following this, we will do a short comparative analysis of the statistical data for Macedonia and selected EU member states.

Investments in education in the EU-28 is at a level of 5% to 5.5% in the last five years and in Macedonia about 4% of GDP. By comparison, in the Scandinavian countries (Denmark, Sweden, Norway and Finland) invested over 7% of GDP (Figure 2). So, we have a relatively low investments in education compared to the EU, and that becomes more obvious when we consider that our GDP per capita is only 36% of the EU average. The situation is similar if we analyze investments according to the number of students in Macedonia, that on average invest about 1, 000 euros per pupil /student per year from the state budget, which is about 1/3 of it is invested in Europe (compared to GDP PPS - purchasing power standards).

Figure 2. Public expenditure on education (% of GDP)

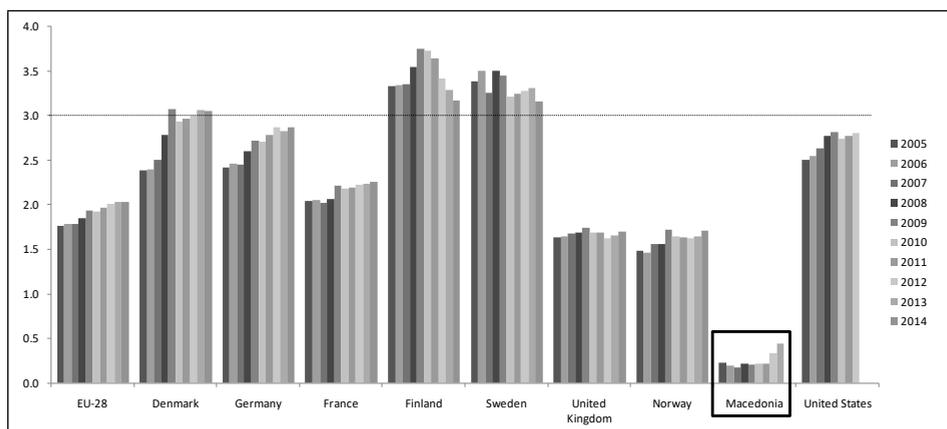


Source: Eurostat (Macedonia data are 2009-2015, State Statistical Office, RM)

2.2. Innovations, research and development

Taking into consideration the role of research and innovation for economic growth, we may draw the suggestion that investment in research and innovation should also be increased in order to increase the competitiveness in the domestic economy. This we can rely on the evidence from the EU-28 and selected EU member states (Figure 3). By comparison, in the EU-28 investments in research and development is about 2% of GDP and is expected to reach 3% by 2020, while in Macedonia currently have only 0.2% of GDP.

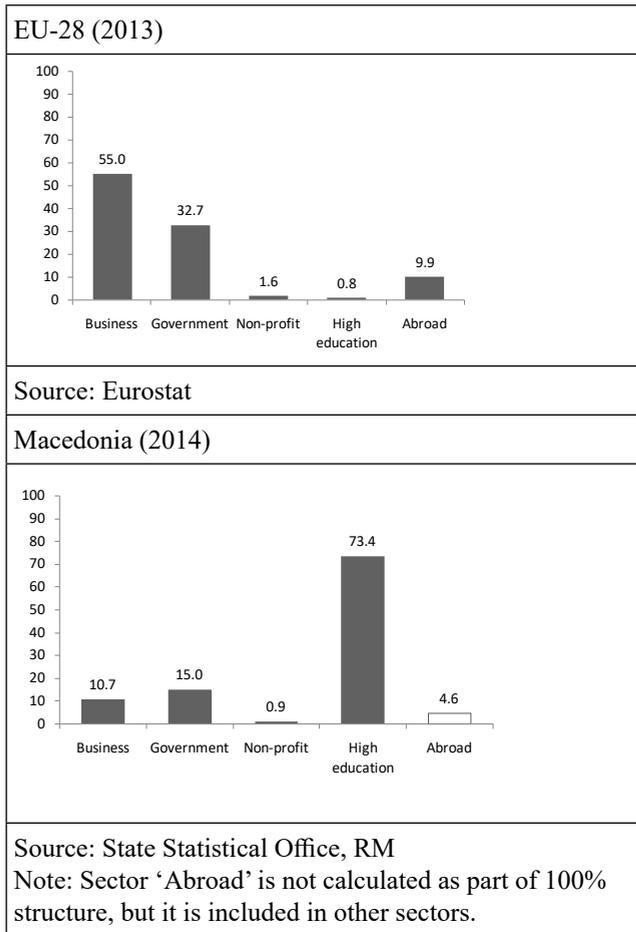
Figure 3. Investments in research and development (as % of GDP)



Source: Eurostat

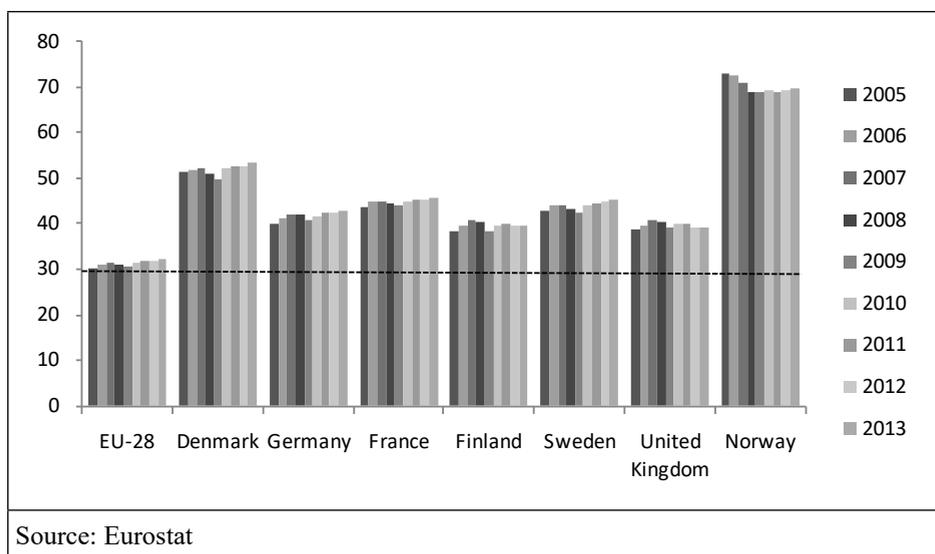
We need to highlight that most of this anyway small size of investments in research and innovation in Macedonia is provided from public sources (88.4%). The private sector, which is intended to be the largest investor in scientific research and innovation amounts to 10.7%. Of the total amount, 4.6% are financed from abroad. Compared to the EU, the private sector accounts for 55% and sources from abroad are about 9.9% (Figure 4).

Fig.4 Structure of expenditures in R&D by sectors



In order to be competitive in the European market, Macedonia needs to increase the productivity of labor, which according to current estimates is equal to 1/3 of the EU average, where productivity is valued over 32 euros/hour. Also worth to underline is that, the Scandinavia where investments in education and science are higher, performs higher productivity, valued at 50 to 70 euros per hour (Figure 5). According to the World Economic Forum in 2015, as regards human capital, Macedonia is ranked in 55 place out of 124 countries in the world (ranked in the region after Croatia and Serbia). According to the same report, globally, the Nordic countries are ranked in the top 10 countries (Finland in the first place).

Fig.5 Labour productivity (Euro per hour worked; index 2005=100)



If we compare the data from the end of 2014 of the labour market in Macedonia, we will see that from 1, 676, 198 capable of working over 15 years, according the law 1, 463, 524 may be permanently employed (15-64 years old), while the labor force is 961, 416 people actively seeking work. Of these employed are 696, 046 (41.6%) and unemployed 265, 370 (27.6%), of which 45, 240 were aged 15-24 years (where unemployment reaches 50.4%). Retirees are around 292, 500 (of which 76, 350 are family pensions). So, seven employees hold three pensioners and every second young person is unemployed in an economy with labor productivity below the European average. This is another potential pressure for

emigration adding here and political context and the challenges in the Euro-Atlantic perspective of our country. Therefore an increase of labour productivity, investment in science and research is a precondition for creating human capital and increasing the competitiveness of domestic economy which is also important in the context of higher economic growth and integration into the European economy.

3. EDUCATION, SOCIAL COHESION AND EUROPEANIZATION

3.1. Critical learning and social cohesion

Critical learning has proven to be the most appropriate methodology that provides the most suitable space for accommodating various innovative open concepts and ideas in children. As such, it is not easy to practice and represents an even greater obstacle for teachers who are not ready for this pedagogical approach.

This approach becomes even more important in mixed societies, where modalities and values should be encouraged and cultivated with the purpose of strengthening social cohesion. In Macedonia, in spite of the “significant development of the education system in the past decade, in regards to education in the mother tongue, events are developing in a direction that should be given attention to and corrected, in order to avoid a greater ethnic distancing”, as is stated in the Strategy for Integrated Education (2008). In these conditions, it is no coincidence that there are shortcomings in the promotion of tolerance, mutual understanding, dialogue, etc. In the Republic of Macedonia this is shown through inappropriate curricula, inadequate schoolbooks, especially on subjects important for social cohesion, low level of knowledge about each other, high level of prejudice and stereotypes that result in the creation of parallel worlds and a fragmented society.

In Macedonia there is good basis for an integrated approach to education. The Ohrid Framework Agreement established a series of legal instruments that enables the strengthening of internal cohesion. However, there still exists an evident need to find new mechanisms that will enable the implementation of policies in the direction of increased interethnic integration in education. Supporting critical thinking and values that facilitate social cohesion is the first step in this direction. Qualitative reforms, which are needed for the improvement of social cohesion, are important from the wider aspect and Europeanization of the society (EIP, 2015).

Although there are different instruments in the European Union for the Europeanization of the education system in Macedonia, such as TEMPUS, Erasmus programs, BASILEUS, Comenius program for primary education, Leonardo da Vinci vocational education program, we must think of more profound and structured reforms specific for the context of Macedonia.

3.2. Challenges in education towards its Europeanization

The potential of education as an important pillar in helping fragmented multiethnic societies, is documented and promoted as a conflict resolution tool by the OSCE in the documents known as the Hague recommendations, Ljubljana Guidelines, etc. One of the reasons why the Republic of Macedonia is lagging in overcoming this situation is the fact that the education system is constantly focused on ethnic political agendas, and it constantly ignores the importance of civic and critical education.

Civic education in the Macedonian context is not only learning the necessary knowledge and skills for autonomy of the individual, but should also be aimed at instilling habits and values in children that a citizen of a democratic society should possess (Brighouse 1998: 722), which is the claim of sociologist Gutmann (1999). This is important in the Macedonian context due to two reasons. Firstly, it will promote the equality of citizens, and in the frames of this model, by manners of study that promote critical thinking, all students will be encouraged to build their own personalities, and secondly, it will promote values necessary for democratic citizenship such as tolerance, understanding, dialogue and compromise, which are values that are closely related to what we frequently name as European values. However, these values become even more important if analyzed from the aspect of the need for social learning.

3.3. Education as the starting point of social learning

A European Union approach was initiated in Macedonia through conflict management. According to Tocci (2007) this framework is based on three pillars: conditionality, social learning and passive enforcement. In this paper, we will focus on social learning, where the potential of education is highest.

Social learning in the literature on Europeanization is mentioned and introduced in an institutional sense. In Tocci's social learning frame-

work, it represent what Checkel defines as “‘complex learning’ (1999: 90), which is a process when in the absence of clear motivating materials, actors get new values, norms and benefits as a result of the close (*ibid.*) institutional interaction with the EU (Katzenstein 2006: 21)” (Pollozhani, 2012: 12). This social learning is a collection of norms and values that can facilitate the EU integration of the country, even in the absence of material motivation, as a result of the contact between institutions and the transfer of values and interests. According to Tocci, in such circumstances actors can change their behavior and their norms and thus become more adaptable, that is more ready for “negotiations and compromise and towards international law instead of unilateralism” (Tocci, 2007: 15).

However, there are questions on “how to realize social learning” or “how, in conditions of lack of sufficient understanding of this context, can such learning occur, bearing in mind that it is developed through long term contacts with institutions” (Pollozhani, 2012: 12). This process is still not happening in Macedonia, at least not in the necessary and expected measure. Because social learning is a result of direct contact between institutions, education is not the main subject for research, but this brief study presents the argument that they are essentially interconnected. Civil oriented education can facilitate dialogue and compromise, which are necessary in the contact with EU institutions. Considering that the Macedonian education system is evaluated as rather rigid, the expected norms and beliefs that should facilitate social learning are not present. Consequently, it is almost impossible that social learning becomes a component and important part of the process of Macedonia’s EU integration. Additionally, the lack of a system that motivates social learning can be a problem in future. Taking into consideration that integration, in accordance with EU norms, is a lengthy process that continues even after accession, it is important to create the fundamentals for social learning to occur. Investing in civic education could serve this purpose, because through this education all future actors can be informed from the earliest age about the norms and values that can facilitate contact with EU institutions.

Each country has its own various particularities which derive from their historical, cultural, economic and geographic context. Adapting these differences to European norms and values is a difficult and painstaking process. In this context, this process is especially particular for countries characterized with by ethnic and cultural specifics, i.e. for multiethnic and multicultural societies. In such circumstances, integration, mutual under-

standing and compromise are both an internal need and a precondition for EU integration. Aware of the difficulties on this road, various recommendations and resolutions have been designed to facilitate this process. One of the most relevant is contained in the Ljubljana Guidelines: “In the context of integration of societies with differences, individuals and/or groups can reach acceptable solutions to all issues they face through negotiation and mutual accommodation. The outcomes of negotiation are likely to be more sustainable and thus better contribute to lasting stability when both majorities and minorities are willing to accommodate the claims of the other parties to the extent possible.” (Ljubljana Guidelines: 19).

3.4. Modalities of social learning in the education

Considering the context of social learning and the shortcomings identified in the analyses of the educational policies in RM, with the aim to build concrete support of the process of integration with necessary substantial elements, education policies (reforms) must be aimed not only at the quantitative, but also the qualitative elements. This means reforming the education system towards innovative methods that encourage critical and civic thinking. Foremost, reforms must take into account the interest of the child, and his or her future. Herein, critical thought is very important, because it enables children to think as autonomous individuals and citizens, and not as part of an ethnic or socioeconomic group. This would enable children to learn openly with one another and not to be limited only to the knowledge based on books, but to be encouraged to practice their knowledge. This environment would enable a system in which compromise; universal values and tolerance are an integral and inseparable part. This is the way to achieve socioeconomic and citizen equality in a multi-ethnic and multicultural environment.

Conclusion

Economic growth and social cohesion for the Republic of Macedonia as a small economy and young democracy with multiethnic society on its path towards European integration represent very important aspect of successful integration of Macedonia into the European Union.

In terms of economic growth, we may suggest that education, research and innovations play significant role as presented from the evi-

dence in EU-28 average, as well as the selected individual countries from the EU. In this context, education plays an important role in society with regards to social cohesion and in terms of economic growth and prosperity. As it seems for the economic growth and the compliance with the criteria for joining the EU, Macedonia should increase the competitiveness of its economy, which primarily implies larger investments in education and science, research and development, which is expected to enhance innovations and increase the human capital as important factor of growth taking into account the challenges demographic trends both in terms of migration, and in terms of the age structure of the population. In conclusion, we may say, investing in education and science, increases productivity, create high-quality personnel for a competitive economy and thus the creating new jobs opportunities for young people and opportunities for returning of Diaspora with capital investment - all this in a function of faster economic growth based on knowledge and competitiveness.

In terms of social cohesion and Europeanization, education represents the pillar of the integrated society. Macedonia, a country in which integration and social cohesion are still imperfect, and which is determined to be a part of the European Union, needs innovative reforms in order to achieve these two goals. Critical learning and civic education would enable Macedonian citizens to overcome ethnic and socioeconomic divisions and prepare them for their future role in society and in the institutions as responsible citizens. Competent and open citizens possessing knowledge and skills and convinced in the need for dialogue, compromise, and tolerance would help the country progress towards and into the European Union. Social learning, an important component for Europeanization of the country, can only function in an environment where institutions are open and used to compromise and debate. Without these preconditions, the more profound and important EU reforms, even if contained in the laws, will not be able to be implemented to the desired extent. Education is the key in having institutions and citizens capable of showing and implementing values and practices on the road to the EU. Further, in order to improve the quality of education, Macedonia will have to make steps towards innovative and qualitative reforms with the aim of supporting the development of equal and competent citizens.

References:

1. Brighouse, H., Civic Education and Liberal Legitimacy, *Ethics* 108(4), 1998, pp. 719-745.
2. Checkel, J.A., Social construction and integration, *Journal of European Public Policy*, 6(4), 1999, pp. 545-560.
3. European Commission, Social Impact of Emigration and Rural-Urban Migration in Central and Eastern Europe: Country Report Republic of Macedonia, EC DG Employment, Social Affairs and Inclusion, Authors: Bornarova S. & Janeska V., April 2012, Brussels
4. European Commission, A European Agenda on Migration, COM(2015) 240 final, 13.5.2015, Brussels
5. European Institute for Peace, Ohrid Framework Agreement Review on Social Cohesion, 2015, Available at: <http://eip.org/sites/default/files/OFA%20Review%20on%20Social%20Cohesion.pdf> [Accessed: 26 Apr. 2016].
6. Gutmann, A., *Democratic Education*, Princeton University Press, 1999, Princeton
7. Katzenstein, J., Multiple Modernities as limits to secular Europeanization? in Byrnes, T.A., Katzenstein, J. (eds) “Religion in an Expanding Europe”, Cambridge University Press, 2016, Cambridge, UK.
8. Ministry of Education and Science, Steps Towards Integrated Education in the Education System in the Republic of Macedonia, 2008, Skopje, RM.
9. National Bank of the Republic of Macedonia, Annual Reports, 2005-2015, Skopje, RM.
10. OSCE, The Hague Recommendations Regarding the Education Rights of National Minorities, 1996, Available at: <http://www.osce.org/hcnm/32180> [Accessed 26 Apr. 2016].
11. OSCE, The Ljubljana Guidelines on Integration of Diverse Societies, 2012, Available at: <http://www.osce.org/hcnm/96883> [Accessed 26 Apr. 2016].
12. Pollozhani, L., Integrating Stability into EU Conflict Management: Insights from Macedonia, 2012, . Available online at: https://www.academia.edu/14490599/Integrating_Stability_Into_EU_Conflict_Management_Insights_from_Macedonia_2012_ [Accessed 26 Apr. 2016].

13. State Statistical Office, Skopje, RM, Available at: <http://www.stat.gov.mk/Default.aspx> [Accessed 26 Apr. 2016].
14. Timssandpirls.bc.edu., Available at: <http://timssandpirls.bc.edu/isc/publications.html> [Accessed 26 Apr. 2016].
15. Tocci, N., *The EU and Conflict Resolution: Promoting peace in the backyard*, Routledge, 2007, London and New York.
16. United Nations, *World Population Ageing 2013*, Department of Economic and Social Affairs, Population Division, 2013, New York.
17. Wiborg, S., Political and Cultural Nationalism in Education. The Ideas of Rousseau and Herder Concerning National Education, *Comparative Education*, 36 (2), Special Number (22): Nigel Grant Festschrift, 2000, pp. 235-243.
18. World Bank, *South East Europe Regular Economic Report No.6*, Report No. 87962-ECA, May 2014, Washington DC.
19. World Economic Forum, *The Human Capital Report*, 2013, Geneva, Switzerland.

UDC 005.742:005.72]:334.72:657.6-051(497.7)
Original scientific paper

JANKA DIMITROVA*
OLIVERA GORGIEVA - TRAJKOVSKA **
BLAGICA KOLEVA***
ALEKSANDRA NACHKOVA****
EFTIMIJA DIMITROVA*****

**CORPORATE GOVERNANCE AND FINANCIAL REPORTING
IN MACEDONIA THROUGH THE PRISM OF INDEPENDENT
AUDITORS REPORTS**

If management means running the business,
governance means proper running of the business.

Every company needs
both governance and management “

Prof. Bob Trikeri

Abstract

In companies with good corporate governance decisions are made not only for achieving economic objectives, in the strict meaning of this concept, but also because of protecting the interests of the stakeholders. One of the most important characteristics of companies with good corporate management is their commitment to maintain a high degree of transparency, demonstrated by consistently reporting of their situation. In the

* Assoc. Prof., PhD., Goce Delcev University Stip, Faculty of economics, E-mail: janka.dimitrova@ugd.edu.mk

** Assoc. Prof., PhD., Goce Delcev University Stip, Faculty of economics, E-mail: olivera.trajkovska@ugd.edu.mk

*** Assist. Prof., PhD., Goce Delcev University Stip, Faculty of economics, E-mail: blagica.jovanova@ugd.edu.mk

**** Postgraduate student, Goce Delcev University Stip, Faculty of economics, E-mail: nachkova_91@live.com

***** Student in high school Yahya Kemal Strumica, E-mail: eftimijadimitrova@yahoo.com

terminology of corporate governance, one of the most important form of transparency is *disclosure* of data and information for companies.

Through transparent disclosure of financial statements, the companies inform stakeholders about the financial position and performance, changes in equity and cash flows, as well as the accounting policies used in disclosures of operating activities in the reporting period. Through the opinion of the independent external auditor, stakeholders are informed whether the financial statements are prepared in accordance with generally accepted financial reporting framework and applicable legislation.

Companies clinging to quality corporate governance are introducing control and informative systems, to maintain the high level of quality of its products and services, as well as quality prepared financial statements, for which the external auditors provide a positive opinion. From this reason the paper presents research on the quality of corporate governance in Republic of Macedonia, through the prism of the reports of the independent auditors, by analyzing the audit reports of 100 companies listed on the Macedonian Stock Exchange.

Keywords: corporate governance, reporting, transparency, decisions, smallest risk

JEL Classification: G30; M41; M42; M48

Introduction

The globalization, which involves free movement of capital, money, labor and technology between countries, exerts pressure on the application of generally accepted principles and behaviors in many areas, including the area of corporate behavior. In this sense, corporate governance based on global standards can be understand as the introduction of a pattern of behavior of companies, that would be understood by every participant in the global market, regardless of his origin.

The introduction of corporate governance means nothing else but standardization of processes, procedures and behavior in the companies, which is based on the principles of responsibility, transparency and control in decision making, daily operations and reporting the situations in the company. Like any other standardization, its aims to reduce uncertainty and

risk of entering into relations with the company, and in this case, goal of increasing confidence in the company is particularly important. Accepting the standardized approach to the management and running of the business it gives the companies a special kind of added value - a value derived from business in an ethical frames.

The companies with good corporate governance abide by special reporting rules. This has particular significance for companies working on the capital market. In order to decide whether to invest in a company, investors want to be sure where to invest with the purpose the investments not to bring harm or loss. Standardized systems of disclosure of data and information about the companies, with standardized practices for the operation of companies in general, provide certainty to investors that investment bears the lowest risk¹.

1. DEFINITION OF CORPORATE GOVERNANCE

The term corporate governance, in the broadest sense, refers to method of establishing balances of interests in certain company, which exists between different persons and entities. Despite the growing popularity of the term in recent decades, from the multitude of definitions can not be selected a comprehensive one, that in the same time precisely and briefly explains its essence. The main reason is the complexity of the concept of corporate governance, its fulfillment with different contents, each of them equally complex, and hard to define.

Some definitions focus on the financial aspects of corporate governance, some on his legal background, while however, a growing number of definitions are attempting to explain it in detail and more fully specify the structure of corporate governance. Here are several definitions of the term corporate governance:

- **James D. Wolfensohn**, the ninth president of the Group World Bank: “*Corporate governance means promoting fair relations, transparency and accountability*”².

¹ Guidelines for Corporate Governance in Macedonia, Second Edition, 2011, p.12

² James D. Wolfensohn to *Financial Times*, June 21, 1999

- Professors **Andrew Shlajfer** (Harvard) and **Robert W. cherries** (University of Chicago): “*Corporative management refers to the ways those corporation’s funders ensure that their investments will return*”³.
- Professor **Henrik Matjesen** of Center for Corporate management of the Copenhagen Business School: “*Corporate management is an area of economics that explores ways through which the application of incentive mechanisms, such as contracts, authorities design and regulation, are providing efficient management of corporations. It is often limited to the issue of improving financial performance, for example - how owners of corporations can motivate managers in the corporation to provide horse-competitive contribution*”⁴.
- Sir **Adrian Cadbury**, the promoter of the debate on corporate governance, a businessman and longtime director of central Bank of England: “*Corporative management aims to maintaining a balance between economic and social goals and between individual’s goals and goals of the community. The framework of corporate Management should encourage efficient use of resources while simultaneous insistence on the responsibility of those who manage resources. The goal is the interests of individuals, corporations and society to get more closer*”⁵.
- Professor of Corporate Governance at the University of Cambridge, **Simon Deakin**: “*The corporative governance denotes the way companies manage and control. Good Management is a necessary ingredient of corporate success and sustainable economic growth. Research in the field of management should be rely on interdisciplinary analysis, mainly on economics and law, good knowledge of contemporary business practices resulting from depth empirical studies in national terms*”⁶.
- **Margaret Blair**, economist, professor of managerial right of Vanderbilt University, USA: “*Corporative Governance introduces a host of legal, cultural and institutional activities that accurately determine*

³ Andrei Shleifer, Robert W. Vishny in *Survey of Corporate Governance*, The Journal of Finance, Juni 1997

⁴ Henrik Mathiesen, 2002

⁵ Sir Adrian Cudbary, “*Global Corporate Governance Forum*”, World Bank, 2000

⁶ <http://www.corpgov.net/library/definitions.htmlIFC-priracnik-1-11-final:new-moment-Anglisko7.qxd> 07.12.2011 14:47 Page 16-17

*what would work public corporations, who will control them, how will the control be performed, and how will the risks and benefits of the activities that corporations had undertaken be distributed*⁷.

Experts from the Organization for Economic Cooperation and Development (OECD): *“Corporate governance a system that manages and control business corporations. The structure corporate governance has specifies the distribution of rights and responsibilities among the various participants / members of a corporation such as those on board, managers, shareholders and concerned persons, and detail describes the rules and procedures for making corporate decisions. That way, it also provides the structure through which the company sets their objectives, the resources with which these goals are achieved and the manner of monitoring Performance”*⁸.

Maybe, the most appropriate definition of corporate management is: *“Corporate governance is system by which the business corporations are managed and controlled. The structure of corporate governance specifies the distribution of rights and responsibilities among different participants / members of the corporation, such as those on board, managers, shareholders and other concerned persons and describes in detail the rules and procedures for making corporate decisions. Thus, it provides the structure through which the company sets their objectives, the resources with which these goals are achieved and the manner of monitoring performance”*⁹.

2. ORGANIZATIONAL STRUCTURE OF CORPORATE GOVERNANCE

A good organizational structure of corporate governance is the one in which a successful system of setting goals is established, making decisions and proper monitoring of implementation of the decisions and meeting the goals of the company. By this way of built relationships and

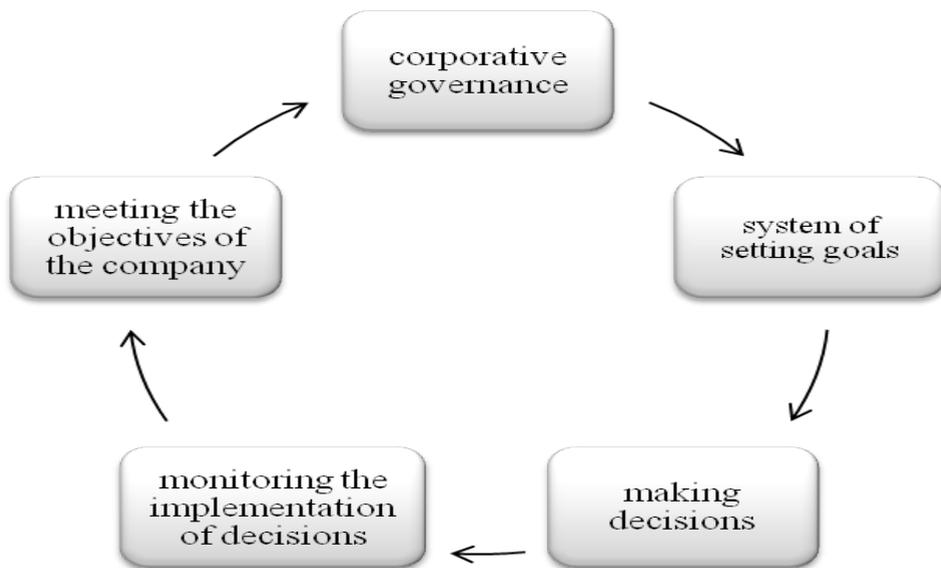
⁷ Margaret Blair, *"Ownership and Control: Rethinking Corporate Governance for the Twenty-First Century"*, Brookings, 1995

⁸ OECD, April 1999

⁹ Nikolce RUNCHEVA * Boris Krastev ** Mirjana Golomeova "K orporativno management vs. corporate management ", University Goce Delchev Stip, 201 0, p.4

processes structure, the company can successfully face the changes in the surrounding area and, thereby, to respond in a way that does not jeopardize the interests of any of the groups concerned.

Figure1. Structure of the corporate governance



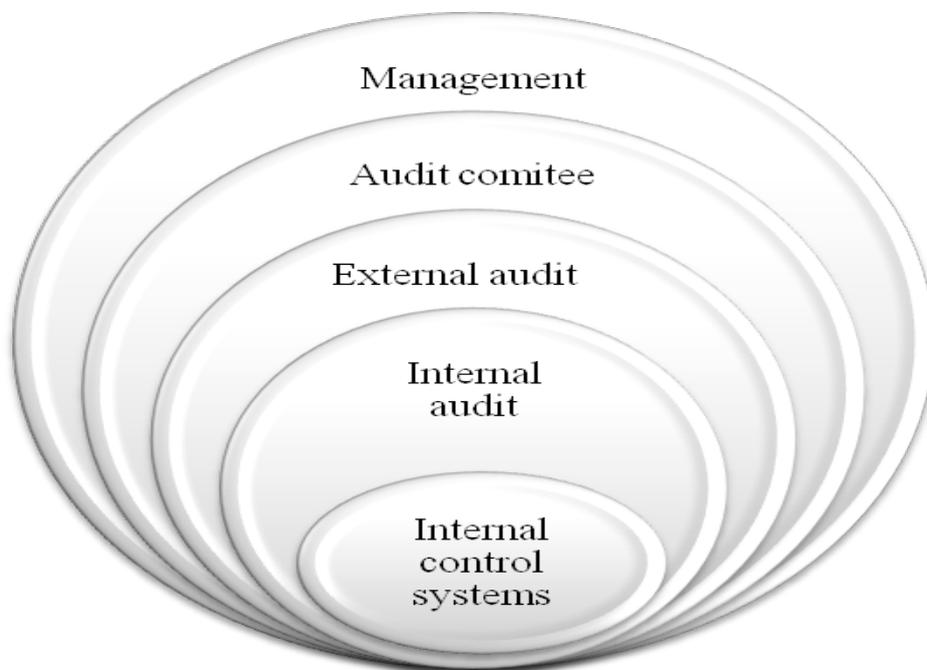
One of the key characteristics of companies with good corporate governance is their readiness for regular disclosure of data and information on the operation of the companies. With shareholders, potential investors and other stakeholders, the company should communicate in a way that will allow them to receive accurate, realistic, timely and relevant information on the situation in the company, its financial performance, its objectives and development. Voluntary disclosure of information and data for companies contributes to the improvement of corporate governance.

The internal and external control and audit are important tools both for management and for oversight of the companies. They provide information about how much the information for the management work, finance and other aspects of the operation of the company are realistic and integrated, and the extent to which the organization structures and systems in the company is the basis for respect policies, laws, regulations and procedures.

Quality preparation for the company's financial statements, free of material errors and mistakes, has responsibility by the management, but also

and the chartered accountants, administrative and managerial staff, the Audit Committee, the employees in the sector for internal audit give input¹⁰.

Figure2. Systems for quality corporate governance



Quality of corporate governance is visible from the efforts of management to establish **internal control systems** in all sectors of its organizational structure (production, marketing, sales, human resources, Finance, Accounting ...) in order to improve the quality of their products, the confidence in purchasers and finally to achieve maximum profit. The introduction and implementation of commonly accepted standards for quality products and services is also an indicator of the quality of the corporate governance.

¹⁰ Phd. Janka Dimitrova The contribution of the audit and audit reports to improve the quality of financial reporting and to increase the international flow of capital, "Managing the development of economic and regional systems: an Eurasian perspective", Organizers: "Higher Business School "OmSPU (Omsk, Russia)" Goce Delcev "University (Stip, Macedonia), 30-31.05. 2016, p. 3

The Internal audit is an activity organized by the management of the company or other business entities for assistance in assessing the working as a whole or of individual segments. It is part of the management supervising of business functions in order to perform them more effectively, and thus to ensure the functioning of the information subsystem that will provide information, as a base for taking appropriate business decisions of the management.

The scope of internal audit includes examination and assessment of applicability and clarity of the system of internal controls, and quality execution of undertaken responsibilities. **Therefore, the internal audit is management's service. The management organizes it as own "extended arm" in order to supervise the accounting system and the system of internal controls, giving contribution in meeting the planned objectives.**

As in many other areas related to the corporate management, the last decade brought vast number of changes in internal audits. Especially progressed the profession of internal auditors, particularly in terms of adaptation to the needs of the companies. The internal audit is growing more and more in consulting activity that helps the management with risk management. Exactly, the risk management is the new specific focus of the internal audit, in addition to the general role to be the last internal guarantee of a company that laws, regulation, internal rules, policies and procedures are respected¹¹.

The external auditors are independent, competent, educated, experienced and professional individuals, charged to investigate the presented financial statements of enterprise customers for the needs of the numerous external and internal users. Expressed opinion of the independent auditor's reality, objectivity, truthfulness and honesty of the presented information increases the credibility of the financial statements in the eyes of a wide range of customers of audit services. "An audit includes examination and evaluation of the working, organizational and business functions, the way of the adoption of business decisions, the functioning

¹¹ Interview with the President of the Institute of Internal Auditors, the most important worldwide organization of professional internal auditors, Mr. Richard Chambers, the magazine of the parent magazine of the Institute - *Boarding Auditor* from April 2010.

of the information system of the audited entity, as well as other issues relevant to their work”¹².

With the help of auditing the quality of financial reporting is improved, which reduces financial misunderstandings by customers, thereby increasing the possibilities for external financing, investments and investment efficiency¹³. The audit confirms the accuracy of the assertions in the financial statements for: comprehensiveness, accuracy, existence, occurrence, valuation, measurement, rights and obligations and presentation and disclosure. The purpose of the audit is to provide the stakeholders evidence regarding the reliability of certain information obtained from those entrusted to manage the company’s property.

On the base on the performed audit of the financial statements, the auditor gives opinion that may be:

- Unqualified opinion -unconditional opinion;
- Unconditional opinion with an emphasis on a particular issue;
- Qualified opinion;
- Disclaimer of opinion and
- Negative opinion.

In the audit process the auditor and his audit report represents the link between the users of the financial statements and the management team of the company, whose financial statements are audited.

Companies with good corporate governance form a separate body - **An audit committee**, whose scope of work are the three main areas: financial reporting, risk management and internal and external audit. The Board of Audit is a management body of a legal entity of public interest. The Audit Committee shall perform the following:

¹² Nikolovski Dr. Pece, Organization of audit of financial statements, Faculty of Economics, Prilep 2004, p. 44

¹³ Nemit Shroff, Real Effects of Financial Reporting Quality and Credibility: Evidence from the PCAOB Regulatory Regime, Massachusetts Institute of Technology, 2015, p. 14

- Monitor the statutory audit of financial statements,
- Monitor the compliance of the legal entity of public interest regulations relating to accounting standards and financial reporting,
- Monitor the review process of the legal entity of public interest and assess the work the audit firm or certified auditor - sole proprietor,
- Proposes the audit company
- Monitor the operations and assess the effectiveness of internal audit and systems risk management.

The audit company, informs the board review of the key issues arising from the statutory audit, with special emphasis on issues related to the material weakness in internal control of legal entity of public interest, in terms of financial reporting.

The objective of the formation of this body is to assist the Supervisory Board in providing a complete insight into the quality and integrity of accounting, internal control systems and financial practice of the subject.

3. BENEFITS OF GOOD CORPORATE GOVERNANCE

Corporate governance refers to the structures and processes for the direction and control of companies through strategic approach to relations between managers, directors, owners / shareholders and other stakeholders. Although some of the pillars that underpin corporate governance consist of laws and regulations, corporate governance is much more than compliance with general standards. Corporate governance brings substantial benefits for companies and financial institutions, and outlines a framework for defining and achieving corporate goals. Good corporate governance practices are integrated into business objectives, allowing companies and financial institutions to thrive and achieve their goals.

Figure 3. Corporate Governance Framework



Briefly, good corporate governance practices help companies in:

- Improving results, operation, competitiveness, profitability and creating long-term value
- Establishing clear roles, responsibilities and accountability
- Improving the decision-making process and the quality of decisions
- Definition and implementation of corporate strategy and direction
- Growth in a sustainable way
- Identifying and managing risks
- Increasing the internal control structures

- Creating appropriate incentives for employees in accordance with the business strategy
- Attracting capital, investments and business partners
- Building reputation by strengthening relationships with stakeholders
- Preparing the future generations

Corporate governance helps companies and financial institutions to meet the challenges of today's business environment, and create a structure through which the best possible decisions will be made, where it will be taken into account the diverse perspectives.

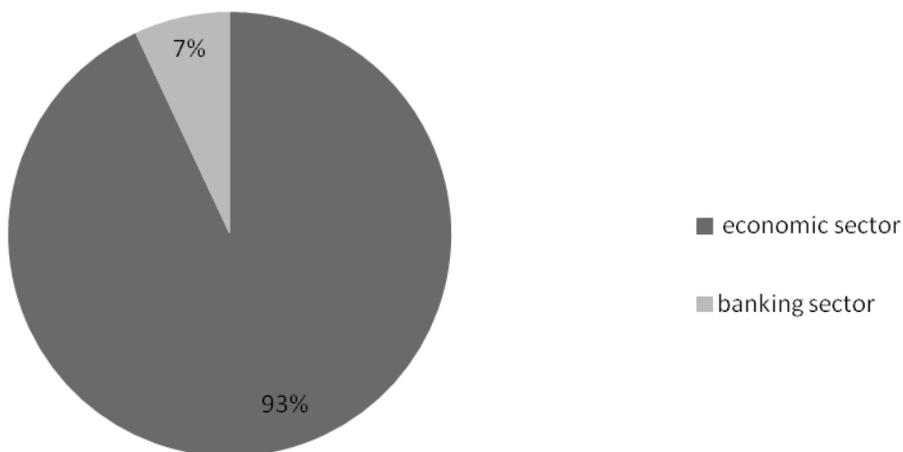
4. CORPORATE GOVERNANCE AND FINANCIAL REPORTING IN MACEDONIA THROUGH THE PRISM OF REPORTS OF INDEPENDENT AUDITORS

The main objective of this research is to analyze the quality of corporate governance and financial reporting in Republic of Macedonia, through the prism of the reports of the independent auditors for the years 2013 and 2014. For this purpose, audit reports of 100 Macedonian companies whose shares are traded on the Macedonian Stock Exchange, have been analyzed. The structure of the analyzed companies is the following: 93 companies are from the industry sector and 7 from the banking sector.

Table1. Analyzed companies by sector

By Sectors	2013	2014
Economic sector	93	93
banking sector	7	7
Total	100	100

Chart 1. Analyzed companies by sector



Source: Authors' research

The following types of an audit opinions have been identified in the analyzed 100 companies, for the business years 2013 and 2014:

- Positive opinion (unqualified opinion)
- Positive opinion by emphasizing the issue
- Qualified opinion
- A negative opinion
- Disclaimer of opinion
- Audit had not been done

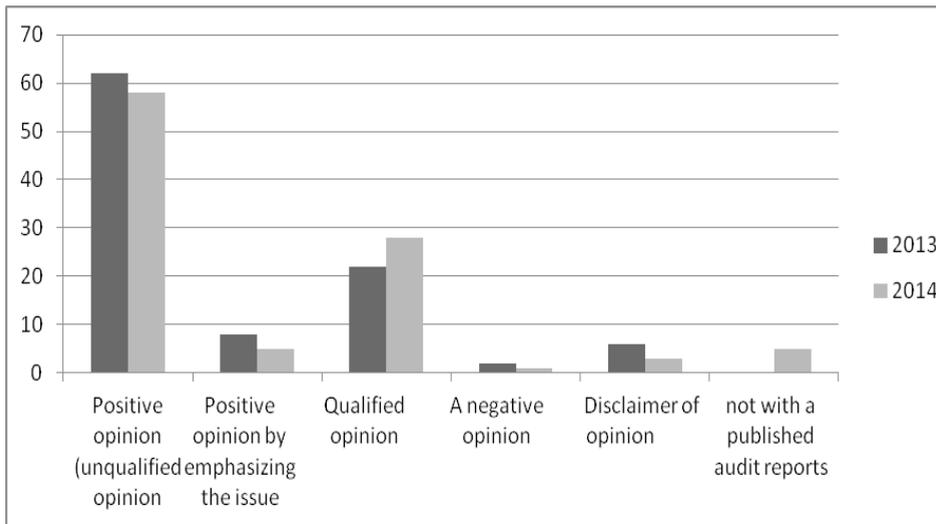
The above expressed opinions are analyzed by sector and by foundations to express a qualified opinion.

Table 2. Types of opinions:

Type of opinion	2013	2014	% change 2014/2013
positive opinion (opinion)	62	58	93.55
positive opinion by emphasizing the issue	8	5	62.50
qualified opinion	22	28	127.27

negative opinion	2	1	50.00
disclaimer of opinion	6	3	50.00
audit reports have not been published	0	5	0.00
Total	100	100	

Chart 2. Types of opinions



Source: Authors' research

From a total of 100 analyzed companies, opinions on the financial statements are as follows:

- Positive opinions in 62 companies in 2013 and 58 companies in 2014, showing noticeable decline of 6.45%
- Positive opinion with emphasizing the issue in 8 companies in 2013 and 5 companies in 2014, with a notable decline of 37, 5%.

- Qualified opinion in 22 companies in 2013 and 28 companies in 2014, with a noticeable increase of 27, 27%
- 2 negative opinions for the analyzed companies in 2013 and for 1 company in 2014, with a notable decline of 50%
- Disclaimer of opinion in 6 companies in 2013 and 3 companies in 2014, with a notable decline of 50%
- Audit have not been performed for 5 companies in 2014,

The analysis of the opinions expressed and their reasons follows :

Positive opinion (unqualified opinion) - is expressed when the auditor concludes that the financial statements give a true and fair view (or are presented fairly, in all significant aspects) in accordance with established financial reporting framework. Unqualified opinion, implicitly suggests that any changes in accounting principles' or methods of their application and their effects are properly determined and disclosed in the financial statements¹⁴.

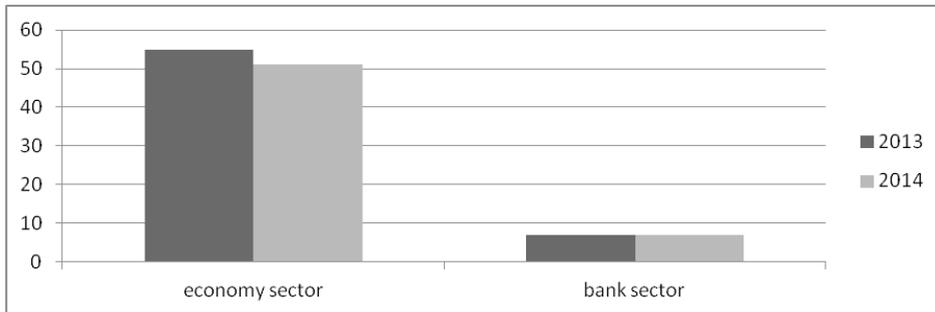
The structure of the positive opinion, as an indicator that the financial statements contain no material omission and errors, by sectors, is presented in Tables 3 and 4 .

Table 3. Positive opinions by sectors

Positive opinion	2013	structure	2014	structure	% change 2014/2013
economy sector	55	88.71	51	88	92.73
banking sector	7	11.29	7	12	100.00
Total	62	100%	58	100%	93.55

¹⁴ Professor. Dr. Janka Dimitrova Audit (theoretical and practical aspects) University Goce Delchev Stip 2013, p. 122

Chart3. Positive opinions by sectors



Source: Authors' research

From the table above it is evident that the banking sector's positive opinion is expressed in all analyzed 7 banks in the years 2013 and 2014, while in the economic sector the decrease of 7.27% in 2014 is recorded.

Table 4. Positive opinion sectors in terms of total

positive opinion by sector from the total	Total	2013	2014	2013 / total	2014 / total
economic sector	93	55	51	59.14	55
banking sector	7	7	7	100	100
Total	100	62	58	62	58

In the economic sector positive opinion presents 59.14% in 2013 and 55% in 2014, while in banking sector positive opinion is expressed in all analyzed 7 banks in 2013 and 2014.

It is characteristic to emphasize that from a total of 62 positive audit opinions in 2013, within 55 companies were positive in 2014 too, while 7 companies in 2014 expressed qualified opinion.

Positive opinion by emphasizing the issue - the audit report may be modified by providing passages that highlight issues affecting the financial statements included in the notes to the financial statements in which these issues are widely explained. The addition of such a passage highlighting an issue does not affect the opinion of the auditor.

From a total of 8 opinions by emphasizing the issue, given in 2013, in 2014 in 3 companies the opinion is positive, in 2 companies the opinion remained unchanged and in 3 companies the opinion transformed into qualified opinion.

Qualified opinion - is expressed when the auditor concludes that he cannot express an opinion without reservation, but when the effect of any disagreement with management or limitation on scope is not material or distributed to impose adverse opinion or disclaimer of opinion.

From a total of 22 qualified opinions in 2013, within 20 companies the opinion remained the same in 2014, with all flaws and errors listed.

Negative opinion - is expressed when the effect of the disagreement is so material and widespread in the financial statements, that the auditor concludes that the reserve report does not correspond to disclose the fact that the financial statements suggest incorrect conclusions or incomplete.

In 2013, 2 negative opinions were expressed from which 1 with the same reasons repeated in 2014.

Disclaimer of opinion - is expressed when the possible effect of limiting the scope is so significant and widespread that the auditor was unable to obtain available appropriate audit evidence, and therefore was unable to express an opinion on the financial statements.

There is disclaimer of opinion in 2013 in 6 companies and in 2014 in 3 companies.

Not published audit reports - in 2014, in 5 companies audit reports have not been published. It is characteristic that some of these companies went into bankruptcy and others are working with huge losses and risk of impaired business continuity.

The main reasons for modification of the audit opinion are:

- An assessment of the fair (market) value of property, plant and equipment in accordance with IAS 36 - Impairment of Assets, has not been made
- Inoperative assessment of the net realizable value of old stock
- Registered land for which there is no title deed
- Trade receivables and liabilities to suppliers are not confirmed

- Litigation - impairment loss on advances for capital expenditures
- Overvalued assets and financial position
- Overstated operating income
- Shown net investments on the sidelines instead of retained earnings
- Correction is not made on the value of claims and liabilities towards suppliers
- Overstated inventory
- Underestimated costs and liabilities Interest
- Obsolete receivables and trade payables towards suppliers
- Uncertainty about the reality of accrued interest
- Inoperative assessment of the fair value of investments available for sale
- Incompatibility of the equity of the Company to that in central register RM
- The absence of physical inventory report
- Overstated costs, other operating expenses and retained earnings from previous years, etc.

Conclusion

The state of corporate governance in the country is improved in the past few years, but there is considerable scope for further action. The state of corporate governance in general is a moving target and it should be run continuously, because the areas of corporate governance, such as planning for succession of senior positions, do not allow occasional or ad hoc action. In this context, the financial sector (banks) may be pointed, because there is a significant quality and presence of good practices in the field of corporate governance, which reflects their positive performance.

It is evident that in the economic sector in the country, there is still the need for improving the organizational structure of companies and the introduction of quality control systems that will contribute to quality corporate governance and financial reporting. Considering the fact that in spite of the auditor's indications for correcting and detecting the mistakes, in the next years the same findings are repeated, the need for continuing educa-

tion and upgrading of accounting and finance workers in the field of international financial reporting standards and other legal financial reporting framework should be emphasized.

References

1. Alfateh Dr. A -Amin Al / Rahim El- Fakki, The Role of the Audit Committee in Improving the Audit Report impartiality Using Analysis of the statement of Cash Flow-Analysis Study, 2013
2. Andrei Shleifer, Robert W. Vishny in *Survey of Corporate Governance*, The Journal of Finance, Juni 1997
3. Henrik Mathiesen, 2002
4. James D. Wolfensohn to *Financial Times*, June 21, 1999
5. Janka Dimitrova, The contribution of the audit and audit reports to improve the quality of financial reporting and to increase the international flow of capital, "Managing the development of economic and regional systems: an Eurasian perspective", Organizers: "Higher Business School" OmSPU (Omsk, Russia) "Goce Delcev" University (Stip, Macedonia), 30-31.05. 2016
6. Janka Dimitrova Audit (theoretical and practical aspects) University Goce Delchev Stip 2013
7. Blair Margaret, "*Ownership and Control: Rethinking Corporate Governance for the Twenty-First Century*", Brookings, 1995
8. Shroff Nemit, Real Effects of Financial Reporting Quality and Credibility: Evidence from the PCAOB Regulatory Regime, Massachusetts Institute of Technology, 2015
9. Nikolce Runchev, Boris Krastev, Mirjana Golomeova, Corporate governance vs. corporate management", University Goce Delchev Stip 2010
10. Guidelines for Corporate Governance in Macedonia, Second Edition, 2011
11. Adrian Cudbary Sir, "*Global Corporate Governance Forum*", World Bank, 2000
12. <http://www.corpgov.net/library/definitions.html> IFC-priracnik-1-11-final: new-moment-Anglisko7.qxd 07.12.2011

DEJAN KRSTEVSKI*
GJORGJI MANCHESKI**

TELECOM COST OPTIMIZATION: HOW TO SUBSIDIZE HANDSET SUBSIDIE

Abstract

The increasingly contentious issue of smartphone subsidies is rapidly ascending to the top of CFO agendas, not only because they present a means of tapping much-anticipated yet unrealized data revenues, but more worryingly because widespread use of such incentives is exerting pressure on the bottom lines of telecoms. For telecom operators chasing growth in mature markets, equipment installment plans, SIM-only offer, sharing subsidy cost with third parties is a way to reduce subsidy budgets, expand the customer base, reduce churn, increase sales and, importantly, increase earnings. While there's a lot of good in this for carriers and customers, there's also a significant amount of risk which, if not mitigated, can have a devastating impact on company bottom line. Hence, in a broader sense, the objective of this article is to suggest some steps towards reducing handset subsidies and measures to mitigate the possible risk.

Key words: Handset Subsidy, Equipment Installment Plans (EIPs), Sim-Only, Handset Financing

JEL classification: M2, G34

Introduction

The telecom industry was founded on significantly subsidized handsets. One definition of the practice, using the term subsidy is the follow-

* Ph.D., Ass. Prof. Faculty of Economics – Prilep, University “St. Kliment Ohridski” - Bitola, Macedonia, e-mail: dejan.krstevski@eccfp.edu.mk

** Ph.D., Prof. Faculty of Economics – Prilep, University “St. Kliment Ohridski” - Bitola, Macedonia, e-mail: gmanceski@t-home.mk

ing: “a handset subsidy is the monetary value, i.e. the difference between the purchase price and the sale price of the handset, given to a customer during the subscription process”.¹ As noted, under some models, operators offer a lower initial price for a handset in exchange for a binding contract period during which they aim to recover the difference, with the sale price, via monthly fees. Essentially, subsidies are one of the pillars on which the ecosystem was built. They have served the industry well as it developed, helping operators to offer attractive handsets to consumers at affordable prices and gain critical market share. However, as device innovation has accelerated, the same subsidy model has begun to work against operators in terms of their bottom lines. Mainly, financial analysts look to see if operators are disciplining or reducing their use of handset subsidies and associate this with higher margins.² As the wireless industry moves toward a different economic model of no-contract plans, companies are exploring the use of financial partners to offload the risk of handset costs. Many customers didn’t really understand the true cost of the device as a result, and the model also meant customers who held onto a device beyond the standard upgrade cycle were paying the carrier far more than the cost of the device. As such, the switch to installment plans is a good thing for consumers, because it introduces transparency over the relative costs of service and hardware. It’s also good for the carriers, because they can slowly reduce the costs of subsidizing handsets while being more competitive on service pricing.

Another way to reduce handset subsidy is the introduction of SIM-only offer. The SIM-only concept was pioneered by discount MVNOs in northern Europe and is now being embraced enthusiastically by mobile operators. It holds two key attractions for operators, according to the latest research. First, it enables them to accelerate the migration from prepaid to postpaid price plans. And second, it significantly reduces subscriber-acquisition and -retention costs. SIM-only customers keep their existing phones, so operators do not need to resort to costly device subsidies. With the impending credit crunch in many developed markets, SIM-only services are extremely attractive to users who are prepared to

¹ Kim, H., Byun, S., & Park, M., 2004. “Mobile Handset Subsidy Policy in Korea: Historical Analysis And Evaluation”, *Telecommunications Policy*, 28, pp. 23–42.

² Battersby, L., 2012. “Mobile phone costs rise as price war ends” by Lucy Battersby, *The Sydney Morning Herald*, 2012, Accessed December 29, 2015. <http://m.smh.com.au/business/mobile-phone-costs-rise-as-price-war-ends/20120730-238rp.html>

keep their old phone in return for lower subscription and usage fees. Some operators have started handing out “free” SIM cards as part of a special promotion. Even though the vast majority of these cards remain unused, it is a relatively low-cost and effective way for an operator to market its service and can generate a good return on investment with even an extremely modest take-up.

What are the other possibilities to decrease handset subsidy: Simply, share it! Operators might share subsidy costs by establishing new alliances and creating new business models together with third parties. Alternatively, operators can also opt to reduce their SAC by increasing the knowledge of customer / handset base. Mainly, understand the evolution and its consumption dynamics, measure the CLV per handset / customer, support the decision making-prices for sales, procurement and marketing purposes will answer the questions how to maximize customer and handset analytical information to support business decisions, which are the important business metrics to consider and how to use these metrics to effectively anticipate and change handset subsidy.

Hence, in a broader sense, the objective of this article is to suggest some steps towards reducing handset subsidies and measures to mitigate the possible risk. The plan for the article is as follows. In section 1 we first present a conceptual framework of equipment installment plans (EIPs). Afterwards, we discuss the need to reinforce the 3G/4G SIM-only model to cut down the costs that carriers pay to subsidize the handset devices for customers. In section 3 we discuss how to reduce handset subsidy by sharing cost with third parties and other alternative approaches. Finally, we conclude and debate contributions of our study.

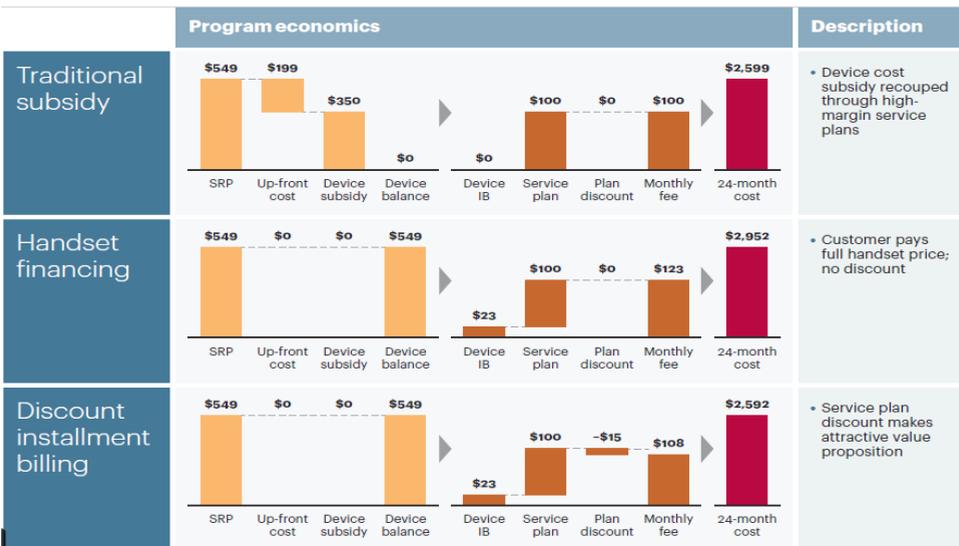
1. EQUIPMENT INSTALLMENT PLANTS – HANDSET FINANCING AND DISCOUNT INSTALLMENT

Some national wireless carriers are turning to a new business model to attract customers. This same model will also cut down the costs carriers pay to subsidize the handset devices for customers. The model, known as equipment installment plans (EIPs), is gaining ground as sales of smartphones continue to grow. Under EIPs, consumers would pay an upfront fee

or in many cases without paying anything at the time of purchase for the phone, and then steadily pay off the phone's cost over the next few months. These new, more affordable installment plans offer customers an easier way to pay, compared to traditional lump-sum payments. Because of this, customers are more likely to sign up for the latest mobile devices. The plans also help carriers remain competitive with other carriers' offerings, which is crucial in an increasingly commoditized industry. This is contrary to the more traditional model of getting a subsidized device in exchange for a two-year service contract. EIPs separate the cost of the phone from that of the service, allowing customers to upgrade their devices without having to wait for their two-year service contract to expire. At the same time, many of these EIPs provide customers with reduced service pricing per month, accounting for the portion of the service contract that would have gone to subsidizing the device. If customers choose to pay off their devices in full, they get the permanent benefit of reduced service pricing without the monthly installment charges on their phones. By financing the cost of expensive smartphone devices over time, however, carriers are deploying significant amounts of working capital to cover the upfront costs of the device sold through the EIPs. And with smartphone sales continuing to grow carriers are employing billions of euros to finance these EIPs. To offset the cash flow impact from EIPs, some carriers have turned to accounts receivables factoring and may consider handset installment sales receivables securitizations in order to provide an alternative form of corporate financing and liquidity. Accounts receivables factoring and handset installment sales receivables securitizations have been used by players in the telecommunications industry; however, they are a new concept for some carriers. One step ahead in equipment installment plans could be a discount installment billing. In short, discount installment billing is the way to make handset financing an attractive customer value proposition. For equivalent or lower cost, the customer gains transparency and simplicity. There are no hidden fees and no device-specific plans. Customers understand, and pay for, true cost of the device. And, as explained below, they can gain better access to new technology through early upgrade programs. Meanwhile, for the operator, discount installment billing lowers subsidy budgets, in earnings improvements, while maintaining or improving the customer value proposition. The disadvantage, however, is that it reduces the monthly service revenues per consumer as it shows exhibit 1. That discount on the monthly service plan will lower ARPU. It may

increase overall absolute revenues, if enough new customers are attracted to switch, but that increase depends on successful execution of the strategy.³ For example, T-Mobile USA has shrewdly used an EIP strategy to help them achieve the fastest subscriber growth rate of late, among the big four carriers. That’s one reason why their competitors have introduced similar plans. There are also some financial benefits for using EIPs.

Exhibit 1. Discount installment billing eliminates traditional subsidies while reducing the monthly service fee (illustrative for \$549 device)



Notes: SRP is suggested retail price; device IB is device with installment billing

Source: Chaudhury, R., and Rooke, J., 2014. Wrestling the Subsidy Challenge in Telecom. A.T. Kearney Paper, pp. 3.

Why equipment installment plans? First, with the new plan configurations they no longer have to subsidize the phone and regain their costs through their higher price plans improving their bottom line. Second, they can change up the verbiage of their marketing to induce more interest because there is now a plan which now looks cheaper, along with low upfront costs to the customer. They get to put the new cost of the “Equipment Charge/Fee” in the fine print that no one looks at as well as move the

³ Chaudhury, R., and Rooke, J., 2014. Wrestling the Subsidy Challenge in Telecom. A.T. Kearney Paper, pp. 3-4.

discount up and down to receive higher margins. Third, companies now get to push their insurance plans harder because in order for customers to “upgrade early” the device has to be in good condition. Fourth, and final point, companies are now more than likely going to get the device from the customer where they are going to be able to make money on the secondary market of refurbished devices.

What are the risks behind the equipment installment plans? Customers who are used to subsidized phones under contract may have a hard time sorting out which of the various plans is best for them. Many end up choosing leased or financed handsets because of the low monthly cost without truly understanding what they’ve committed to do. With the high price of handsets, many carriers now have more value tied up in assets associated with bad debt than in outstanding service fees. While this shift has made asset recovery more urgent than ever, bundling equipment and service collections is extremely challenging and costly for carriers and collections agencies. Fraud has always been a major concern for carriers, but with the rise in leased and financed handsets, it’s becoming easier than ever to commit. All it takes is placing an initial payment for multiple devices on a credit card, cancelling the card and selling the phones online for people to use with a different carrier’s service. When customers don’t return leased handsets or financed handsets that weren’t paid for in full, not only do you lose out on the ability to resell the devices, you also lose out on hard cash.⁴

Smartphone and feature phone equipment installment plans now account for well over half of postpaid device activations in the US, putting customers more in control of their service experience and allowing carriers to better match costs to value opportunities in the market. The latest report from Strategy Analytics’ Wireless Operator Strategies (WOS) service, recommends more operators adopt de-coupled business models as a means of better targeting preferences across diverse customer segments by increasing device choice and upgrade opportunities. EIPs and leases accounted for 54% of postpaid device activations in Q1 2015 in the US, with further momentum seen in Q2 results at AT&T, Verizon Wireless and T-Mobile US (Sprint will announce results August 4 and is expected to

⁴ Kosh K., 2015. Mobile Handset Financing and Leasing: Best Practices for Mitigating Carrier Risk. On Process Technology, White Paper: Finance Handset. Accessed December 29, 2015. <http://www.onprocess.com/whitepapers/white-paper-mobile-handset-financing-and-leasing>

continue its growth trend in leasing uptake). With the majority of operators booking the full value of EIP payments when the device is sold, to coincide with the cost of goods sold, there are EBITDA gains over the subsidy business model. For example, Sunrise Switzerland recorded 13% growth in its postpaid EBITDA contribution between Q1 2014 and Q1 2015 after its switch to EIPs. While offering greater flexibility to postpaid device purchasing, EIPs can be extended into prepaid and SIM-only channels, where operator device sales options have either been limited or non-existent. France and Brazil have enjoyed success with this approach.⁵

2. REINFORCE THE 3G/4G SIM-ONLY MODEL

Despite the fact that most technology seems to go down in price, smartphones are an area where customers have steadily been paying more and more, both on the devices and on the contracts that go with them. It doesn't help that there's often a confusing range of contracts and buying options out there, making the decision on what's best for customers even harder. In fact, there are two main methods of buying a smartphone. First, customers can buy one on contract, where they're locked in for a set amount of time and are paying off their handset at the same time as paying for the service they use. Secondly, they can buy a phone outright and then choose to go with a SIM-only contract. The SIM-only model represents "no obligation" phone deal that comes with an agreed monthly fee, but does not include a subsidized handset. Within a SIM-only model the mobile carrier supplies their customers with just one piece of hardware, a SIM card, which includes an agreed amount network usage in exchange of set monthly payment to be made by the customer. Network usage within a SIM-only model can be measured in minutes, text, data or any combination of these. The duration of a SIM-only contract can vary depending on the deal selected by the customer. SIM only contracts differ from mobile phone contracts in that they do not include any hardware other than a SIM card. In terms of network usage SIM only is typically more cost effective than other mobile device contracts because unlike these other contracts a SIM only deal does not offset the cost of a mobile device over the contract period. Short contract length is one of the key features of SIM only which are made

⁵ Kendall P., 2015. Global Momentum for Equipment Instalment Plans as Verizon/AT&T See Further Growth Strategy Analytics' Wireless Operator Strategies (WOS) service report, pp. 8–10.

possible due to the absence of a mobile device. In this program, customers bring their existing phones and receive a discount on their subscription fee. This SIM only plan is a great choice if customers want to keep their phones but get a 4G data SIM. By getting a 4G data SIM customer will benefit from faster internet speeds - perfect for streaming music, watching videos, playing games and uploading photos to Facebook and Twitter. In our opinion, this method helps a lot to lower SAC. Wireless operators can embrace this model in the future when the limit of using smart devices reaches the expected levels.

Why SIM-only plans? Decisions for SIM-only are driven by price. Mainly, customers are focusing on lower prices (monthly access fee) and higher data inclusions (data allocation). Moreover SIM-only customers love their current handset and are looking to save. Current trends indicate that students love SIM-only plans with 1 in 3 students signing up to one or similar. The total market customer's demands show that more than 50% of consumers on postpaid today are considering SIM-only in the future, suggesting a likely shift in the market structure. Globally there is a shifting trend towards SIM-only removing subsidies to make handset cost more transparent. Also, 50% of iPhone customers will hand down their phone to family or friends. Furthermore, globally there were over 50% solely handsets sold – same SIM-only opportunities.

What are the risks behind the SIM-only offer? The decision to reduce handset subsidies should be advanced with carefulness by operators, as there is a trade-off between the clear benefit of reduced subsidies and the associated risk of losing control over how customers purchase handsets and use data services. Also, operators should consider carefully the extent to which they want to push towards a model characterized by the lack of handset subsidies to avoid becoming disintermediated from the mobile content and advertising value chains, potentially losing profitable new revenue streams. Furthermore, the key advantage for operators that have control over handsets is the ability to offer a differentiated end-to-end customer experience and to secure their position within the non-voice value chains. The risk associated with SIM-only tariffs is that operators are reduced to big pipes that add no value. However, the move towards a reduction in handset subsidization comes at a cost: an increased risk of higher churn due to the shorter lock-in period and lack of control of the devices connected can potentially lead to revenue loss, as customers equipped with old handsets may not be able to make the most of new

digital services. Lastly, the loss of control over handset distribution causes operators to lose the opportunity to determine the customer experience.

The present Western Europe SIM-only market circumstances show that SIM-only mobile plans are being paid cheaper, according to the newest edition of Telecom paper's EU Mobile Benchmark report on mobile prices. The comparison of the total cost of SIM-only plans per month, including connection fees and promotions, on offer in 16 countries in the third quarter of 2015 shows a general downward trend in prices in the past six months. Looking at one of the more common plans on offer, for over 1,000 minutes and more than 2 GB data per month, the median price fell in eight of the 16 countries surveyed, with especially strong drops in Italy and Germany. Compared to Q3 2014, prices for the same plan were also down in nine of the 16 countries. According to Telecompaper, competition on the Sim-only market is intensifying, as more operators move away from handset subsidies and customers turn to other channels to buy their smartphones. The migration to (near) unlimited plans is also driving the commodification of mobile services and putting pressure on prices. The research shows the volume of communication included in mobile bundles is still increasing. In Q3 2015, 41 percent of all SIM-only plans included more than 1,000 minutes, up from 37 percent in Q1 2015, while the share of plans with more than 2GB increased over the same period from 37 percent to 42 percent. That growth was strongest in Italy, where only 22 percent of SIM-only plans included more than 2GB in Q1 2015 but six months later that had grown to 83 percent. In the Scandinavian countries most plans included more than 2GB in Q3 2015, while Greece, Portugal and the Netherlands had the smallest shares of plans with over 2GB per month. Of the 16 countries surveyed, Denmark, Norway and Sweden showed the cheapest SIM-only prices, both in terms of median TCO and lowest TCO, while France, Italy and Spain were also relatively cheap. Greece and Switzerland were the most expensive countries, followed by Portugal.⁶

3. REDUCE HANDSET SUBSIDY BY SHARING COST WITH THIRD PARTIES AND OTHER ALTERNATIVES

Telecoms could leverage their subsidy costs by establishing new alliances and creating new innovative business models together with third

⁶ Telecompaper, 2015, EU Mobile Benchmark 2015 Q3, Accessed December 29, 2015 <http://www.telecompaper.com/research/publications>

parties. Facebook, Twitter, E-bay, Amazon, Aliexpress, newspapers and game producers might be willing to establish that kind of partnerships. This way, they are not just going to advertise a product, but they will reach number of several consumers and have chance to attract different type of customers' attention linked to their know-how area. Game producers might be a good choice for them while the game company advertise of their best-selling game ready to be played, they can work for operators at the same time by giving a place for the carriers' devices/products or doing initial advertising for the company and its products. Twitter and Facebook shortcuts pre-installed on feature phones by vendors or operators are an evident example. OTT providers such as WhatsApp and WeChat share in the revenue boom when smartphone penetration increases. Henceforth, operators can explore the option of sharing the cost of handset subsidies with these application providers. Alternatively, operators can also opt to reduce their SAC by requesting the customers to trade-in their old handsets to qualify for a new subsidized smartphone. In this way, operators can recover a portion of their handset costs by refurbishing and selling devices to the secondary market (such as developing markets) or by selling them for spare parts. For example, some operators offer its customers cash discount on the new handset when they recycle in their old ones during subscription renewal or new purchase. The amount of cash discount given depends on the value of the trade-in device.⁷

Alternatively, operators can also opt to reduce their SAC by increasing the knowledge of customer / handset base. Mainly, understand the evolution and its consumption dynamics, measure the CLV per handset / customer, support the decision making-prices for sales, procurement and marketing purposes will answer the questions how to maximize customer and handset analytical information to support business decisions, which are the important business metrics to consider and how to use these metrics to effectively anticipate and change handset subsidy.

Telco's could proactively offer discounts on subscription fees for each additional month if customer is willing to wait for renewal. Several operators offer competitively priced refurbishing services that allow customers to extend the lifetime of their mobile phones, even smartphones. In Western countries, most of the handset subsidies are incurred during

⁷ BMI Research, 2014, Operators Need To Take A Closer Look At Handset Subsidies, Accessed December 29, 2015 <http://www.bmiresearch.com/news-and-views/operators-need-to-take-a-closer-look-at-handset-subsidies>

renewals or upgrades rather than new customer acquisition. Consequently, increasing the length of time customers hold on to existing plans can increase the lifetime value of handset subsidies investment.⁸ In many countries, the minimum contract period is between one or two years on average, which tends to give telecoms enough time to recover the cost of handset subsidies. The problem comes when customers cut short their contract in favor of a new contract or terminate it. This kind of a risk is possible to be managed via reverse subsidies. Reverse subsidies is a concept whereby an initial subsidy is not given selling price of the handset, but rather, discounted from the monthly data plans of the consumers. This does not reduce default risk but increases stickiness through the monthly discount it generates. Reverse subsidies are now being offered by a growing number of operators. Furthermore, incentives need to be provided to customers to delay device upgrading, which doubled its smartphone upgrade fee for those moving up to the new model before the end of their contracts.

Conclusion

Telco companies are more and more feeling the burden of device subsidies on their bottom lines and are consequently looking for workable solutions that alleviate the pressure without negatively impacting their competitiveness. Despite the fact that subsidy costs are still under control in some telco markets due to a still limited share of postpaid subscribers, this is a call to action for operators to re-examine and rethink subsidy strategies as a matter of priority; to start educating the market before they find themselves sacrificing EBITDA. We expect that in the next two years, the majority of postpaid subscribers in mature markets worldwide will move to different equipment installment plans. Early adopters will therefore benefit from subscriber churn away from their slower moving competitors. Because of this market evolution, an equipment installment plan is going to be an essential strategy for any operator. In recent years there has been a surge in sales of SIM-only propositions. Well-designed SIM-only propositions can help operators achieve cost reductions as a result of lower handset subsidies and lower sales commissions. However, lack of contract commitment means the customer can leave at relatively short notice, with

⁸ Arlorio A., 2013. Smartphone subsidies and telco profitability. Delta Partners, Business Paper, Accessed August 29, 2016. <https://www.digitalnewsasia.com/mobility/smartphone-subsidies-and-telco-profitability>

higher churn a consequence. The key to success, then, is not the existence of the strategy but how well it is designed and executed. The winners will be those companies that offer customers a genuinely improved value proposition while mitigating the revenue risks.

References

1. Arlorio A., 2013. Smartphone subsidies and telco profitability. Delta Partners, Business Paper, Accessed August 29, 2016. <https://www.digitalnewsasia.com/mobility/smartphone-subsidies-and-telco-profitability>
2. Battersby, L., 2012. "Mobile phone costs rise as price war ends" by Lucy Battersby. The Sydney Morning Herald, 2012, Accessed December 29, 2015. <http://m.smh.com.au/business/mobile-phone-costs-rise-as-price-war-ends-20120730-238rp.html>
3. BMI Research, 2014, Operators Need To Take A Closer Look At Handset Subsidies, Accessed December 29, 2015. <http://www.bmiresearch.com/news-and-views/operators-need-to-take-a-closer-look-at-handset-subsidies>.
4. Chaudhury, R., and Rooke, J., 2014. Wrestling the Subsidy Challenge in Telecom. A.T. Kearney Paper, pp. 3-4.
5. Kendall P., 2015. Global Momentum for Equipment Instalment Plans as Verizon/AT&T See Further Growth. Strategy Analytics' Wireless Operator Strategies (WOS) service report, pp. 8–10.
6. Kim, H., Byun, S., & Park, M., 2004. "Mobile Handset Subsidy Policy in Korea: Historical Analysis And Evaluation", Telecommunications Policy, 28, pp. 23–42.
7. Kosh K., 2015. Mobile Handset Financing and Leasing: Best Practices for Mitigating Carrier Risk. On Process Technology, White Paper: Finance Handset. Accessed December 29, 2015. <http://www.onprocess.com/whitepapers/white-paper-mobile-handset-financing-and-leasing>
8. Telecompaper, 2015, EU Mobile Benchmark 2015 Q3, Accessed December 29, 2015.
9. <http://www.telecompaper.com/research/publications>

SERGEJ NAUMOVSKI*
MARJAN BOJADJIEV**
ANA TOMOVSKA-MISOSKA***
MIODRAGA STEFANOVSKA-PETKOVSKA****

**ORGANIZATIONAL ALIGNMENT IN THE FOOD INDUSTRY:
CASE STUDY OF A COMPANY IN THE REPUBLIC OF
MACEDONIA**

Abstract

The role of organizational alignment and culture in achieving the strategic objectives cannot be ignored. It guides all the modern business trends in the markets including new mergers and acquisitions whose cultures must be properly aligned to achieve success. Having low level organizational alignment eventually translates to organizational failures and hinders progress. Proper alignment of organizational structures and processes required strong leadership in order to achieve success, thus the difference between successful organizational and those that have failed lies in the integration of organizational culture and alignment. Therefore this paper analyses the organizational alignment and culture of a company belonging to the food industry sector in Republic of Macedonia. Furthermore it analyses the critical aspects of the organizational functioning in the company. The content of this paper includes literature review, research methodology and explanation of the general findings. The paper gives a critical examination of the literature in terms of different approaches in defining and measuring

* School of Business Economics and Management, University American College Skopje 1000, Skopje, Republic of Macedonia E-mail: sergej.naumovski@takt.consulting.mk

** School of Business Economics and Management, University American College Skopje 1000, Skopje, Republic of Macedonia E-mail: provost@uacs.edu.mk

*** School of Business Economics and Management, University American College Skopje 1000, Skopje, Republic of Macedonia E-mail: tomovska@uacs.edu.mk

**** School of Business Economics and Management, University American College Skopje 1000, Skopje, Republic of Macedonia E-mail: stefanovska@uacs.edu.mk

organizational alignment and culture. The study uses qualitative methods based on a questionnaire. Those methods used to analyze the organizational alignment are based on the “Vox Organizationis model” for measuring organizational culture and alignment. The general findings show satisfactory level of organizational alignment in the company, as well as a mutual understanding between the management and the employees.

Key Words: Organizational Alignment; Organizational culture; Leader, Employees, Values

JEL classification: M54

Introduction

In recent years, what organizations do is considered to be less important than the methods, tactics and approaches they use to do it. This implies that for organizations to sustain their levels of success and achievement, then the mode of product and service delivery is of critical importance.¹ Organizational strategists have documented examples of companies that have in the past plunged from a high level of success and prosperity to cases of failed organization due to issues of organizational culture and alignment. The most common reason among those that have failed sometimes is the case of poor cultural management and realignment of organizational operations that is eventually reflected in the service provision, including staff management and product delivery².

Most companies fail to emphasize the importance of human assets. Modern businesses have to be careful on their alignment and cultural strategies³. Research has established that organizations, which are properly aligned to core values, culture and goals, prompt their operations to

¹ Luham, J., Cunliffe, A. (2012) 'Key Concepts in Organization Theory'http://www.sagepub.com/upm-data/37949_Chapter2.pdf (Accessed: 28/10/2013)

² Chon, N. (1991) "Alignment" Theory: Creating Strategic Fit , The' Management Decision. 29 (1). <http://centstrat.com/wp-content/uploads/2008/06/strategic-alignment.pdf>

³ Hofstede, G., Neuijen, B., Ohayv, D., and Sanders, G. (1990) 'Measuring Organizational Cultures; A Qualitative and Quantitative Study across Twenty Cases' Administrative Science Quarterly.

take place at faster rates compared to others, and without much effort. This is because in such working environments, people, in this case the employees, often know what is expected of them or what to do, and hence there is always a greater bias for their action. The resulting outcome is that such an organization is better placed to achieve increased levels of output and get to be in better positions to withstand the dynamic market pressures of increased levels of demand and supply volatility. This paper seeks to analyse in depth the concepts of organizational culture and organizational alignment, the various theories that control the operations for these concepts and a criticism of the theories.

The aim of this paper is to analyse the organizational alignment of a company in the food industry in the Republic of Macedonia and therefore it has several objectives: to analyse the literature on the issue of organizational alignment in the food Industry and in the companies in general; to assess the organizational alignment in a company in Republic of Macedonia; and to provide recommendations for improvement for the company.

1. METHODOLOGY

1.1 Sample and Data collection

In this research a convenience sampling was used for the selection of the respondents. In the convenience sampling method the sample is chosen from the company that is the most convenient for the researcher⁴. This method can provide very good qualitative information and may provide precise correlations. The main research instrument was the questionnaire as a research tool that is consisted of set of questions with a purpose of gathering information from individual respondents⁵. The research was conducted by using an existing instrument within the model of Vox Organizationis. developed by Tomovska-Misovska, Bojadziev, Stefanovska and Nikolovska. This model's dimensions are developed to reflect the broader cultural environment and the needs of the organizations in Macedonia and the broader region⁶. The data was collected in 2015 by face-to-face adminis-

⁴ Saunders M., Lewis P., Thornhill A.,(2003) 'Research Methods for Business Students'

⁵ Saunders M., Lewis P., Thornhill A.,(2003) 'Research Methods for Business Students'

⁶ Tomovska- Misoska A., Bojadziev M., Stefanovska M., Nikolovska Z.,(2011) 'Vox Organizationis – theoretical basis and methodological considerations in the development of an instrument for organizational culture'

tration of the questionnaire to every employee in the company. In line with the proposed methodology a special questionnaire was given to the leader⁷. The questionnaire was given in hard copy to all 50 employees including the leader. The recipients were requested to complete the questionnaire and return it back as soon as possible. After one week 36 complete questionnaires were collected with an expected response rate of 72%.

1.2 Instrument

This instrument from the Vox Organizatins model consists of 35 questions intended to measure four dimensions of organizational culture:

1. Decision making and behavior (DMB) - intends to understand the level of bureaucracy in the studied Macedonian enterprises;
2. People versus task orientation (P-T) - is related to the social care or the human relations within the company;
3. Innovativeness and risk taking and (IRT); - is supposed to measure the tendency towards risk organizational actions
4. Open versus closed system (O-C) - will evaluate if the respondents consider their companies belonging to organizational models that do or do not depend on exterior surrounding in seeking for solutions of managerial concerns.

The four dimensions of the instrument were used to assess the practices of the organization as reflection of the organizational culture of Macedonian companies from the relevant sector. Each of the dimensions is bipolar and consists of set of questions measured by The answers were scored on a four point Likert type scale: 1 = "I strongly disagree", 2 = "I disagree", 3 = "I agree" and 4 = "I strongly agree".

The instrument consists of two questionnaires, one for the leader and one for the employees.

⁷ Tomovska- Misoska A., Bojadziev M., Stefanovska M., Nikolovska Z.,(2011) 'Vox Organizationis – theoretical basis and methodological considerations in the development of an instrument for organizational culture'

2. GENERAL FINDINGS

2.1 Decision-making and behaviour dimension

This dimension covers the decision-making and behaviour policies of the company. It has bureaucracy with strictly governed behavior by policies and procedure at the one end and democracy with decision making and behavior governed by shared understanding and culture and involvement of employees in decision making at the other end. The dimension is covered by 1-9 questions from the questionnaire.

Table 1: Decision-making and behavior dimension table

Dimension	Leader	Employees
		Average score
Decision making and behavior	3,00	2,71

Table 1 shows the score of the leader and the employees on the decision-making and behavior. On a Likert scale from 1 to 4 both the leader and the employees have high score, which means that they both agree that the company has democratic values and that the decision-making and behavior is governed by shared understanding and culture and involvement of employees.

2.2 People versus task dimension

As mentioned before in the methodology chapter this dimension emphasizes the care for completing the task at one side and the care for the wellbeing of the employees on the other side. This dimension is covered by 10-17 questions from the questionnaire.

Table 2: People versus task dimension table

Dimension	Leader	Employees
		Average score
People versus task	3,13	2,57

The perception and the score of the leader and employees are shown in the table above. Both the leader and the employees have average positive scores on this dimension on the Likert scale. These positive scores mean that they both have the same perception and agree that the company takes care for the wellbeing of the employees over thinking for only completing the tasks.

2.3 Innovativeness and risk-taking dimension

The innovativeness and risk-taking dimension concerns the high levels of innovativeness and risk-taking at one end and the low levels of innovativeness risk taking of the company at the other end. This dimension is covered with 18-24 questions from the questionnaire.

Table 3: Innovativeness and risk-taking dimension table

	Leader	Employees
Dimensions		Average score
Innovativeness and risk taking	2,57	2,53

In the upper table we can see how the leader and the employees perceive the level of the innovativeness and risk taking. The average scores are 2,57 and 2,53, which are high scores. Both the leader and the employees have perception and agree that there is high level of innovativeness and risk taking in the company.

2.4 Open versus closed system dimension

The open versus closed system dimension researches the collaboration and cooperation level between the employees and the level of openness to the new employees and the environment of the company. Questions 25 to 35 reflect on this dimension.

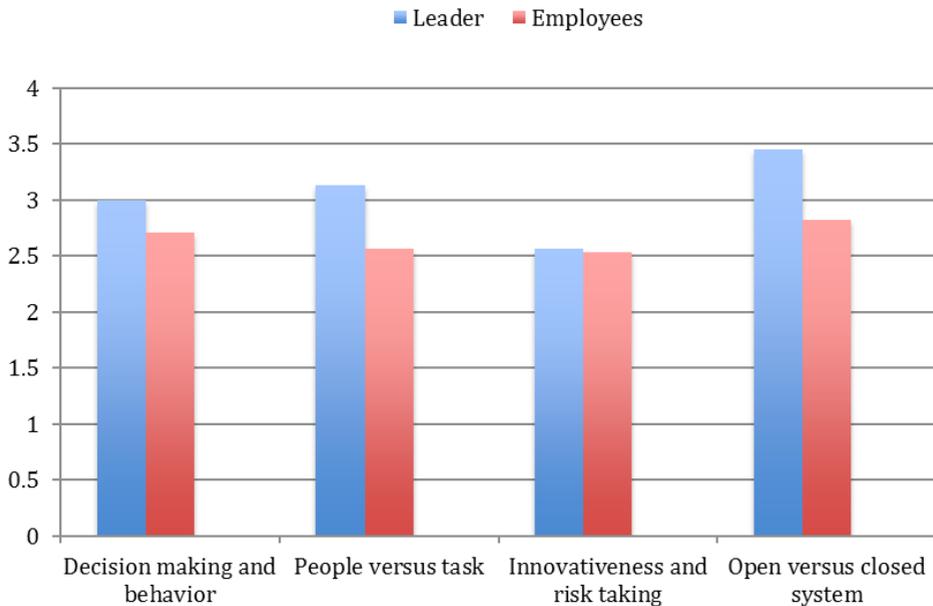
Table 4: Open versus closed system dimension table

	Leader	Employees
Dimension		Average score
Open versus closed system	3,45	2,82

The average scores of the open versus closed system dimension are shown in table 4. The leader has a score of 3,45, which means that he agrees with the perception that the company has open system in terms of cooperation level between the employees and the openness to new employees and environment. The employees have also the same perception as the leader with slightly lower score of 2,82 out of 4.

From all of the above stated we could see that the leader and the employees have generally aligned perception on the four dimensions on the company. Having satisfactory level organizational alignment eventually translates to good organizational functionality and progress for this particular company.

Chart 1: Leader versus employees dimensions scores chart



The chart above gives visual interpretation of the results on the four dimensions for measuring organizational alignment. The average scores on each dimension given by both the leader and the employees are very similar and we can conclude that there is no significant difference between their perceptions.

2.5 Formal aspects of the company

According to the answers of the leader the company functions in the following manner:

Decision-making and behaviour dimension

- The company have a formal strategic planning process
- The company have a strategic plan in a time frame of 2-5 years
- The company have action plans resulting from the strategic plan
- The action plans does not have clear goals for every employee, time frames and KPIs.
- The managers control their employees concerning the achievement of the action plan goals more than 4 times per year
- Only the management is involved in the process of drafting the strategic plan
- Only the management is involved in the process of drafting the action plans
- Only the management is involved in the process of drafting other bylaws and/ or procedures
- The company have a formal organizational structure
- The organization have clearly delegated duties/responsibilities for each employee
- There is a provision/bylaw, which clearly specifies the level of freedom of the employee in decision making for decisions related to his/her workplace
- The leader only consults some of his employees in the decision making process
- There is no written procedure according to which the employees can express their opinion to the management
- Not all decisions and procedures are distributed to all employees
- The leader makes the decision whether the decisions are going to be distributed or not, and the leader decides to which employees are they going to be distributed
- There isn't a bylaw according to which an employee may be penalized for not following the procedure, even though he/she managed to achieve the desirable result (KPI)

According to these aspects the company's functioning there is a clear view that the company functions with more bureaucratic than democratic principles on this dimension.

People versus task dimension

- The strategic plan or any other formal document addresses the working conditions of the employees (physical conditions, workplace protection, etc.)
- The strategic plan or any other formal document does not address the work-life balance (flexible working hours, absences/leaves for personal reasons...)
- The strategic plan or any other formal document does not address the social relationships in the company and organizational climate (employees' relations, management, mobbing etc.)
- The leader does not feel that the current strategic plan reflects "the best ideas" of the employees
- The leader believes that he has a clear vision for the future and means of achieving that vision which is shared by all employees
- The organization does not have bylaws/procedures, which include trainings, or professional development plans for the employees
- The company stimulates its employees to professionally develop and improve themselves through providing financial or other types of aid (financial aid, flexible working time, reduced working hours)
- The company does not have a formal process for performance management
- The employees are regularly informed about the results from the evaluation system

According to these principles in the people versus task dimension we can clearly see that the company is task oriented.

Innovativeness and risk taking dimension

- The company does not have a system for rewarding the innovativeness of its employees
- The company does not have a system/bylaw/procedure according to which the employees can present their ideas for introduction of new

products or services, improvement of the existing ones or improving the production process etc.

- The strategic plan includes some type of innovativeness (for example, market expansion, launching new products and/ or services, targeting new clients, etc.)

According to the way in which the company functions in terms of innovativeness and risk taking dimension, we can conclude that the company has medium level of innovativeness and risk taking.

Open versus closed system dimension

- The strategic plan or other documents does not include activities, which require inter-departmental cooperation or involvement of multiple departments
- The strategic plan or other documents foster/encourage teamwork
- The employees' reward system does not contain part for rewarding teamwork
- The strategic plan or other documents does not include parts on internal communication processes
- The strategic plan or other documents include parts which focus on satisfying customers'/clients' needs
- The strategic plan or other documents include parts on cooperation with other organizations/ companies (competition, suppliers, other related stakeholders etc.)
- The strategic plan or other documents does not include parts on collaboration with the local community (both governmental and non-governmental institutions etc.)The company is a member of organization (chamber, international organization and thus like)
- The strategic plan or other documents does not include part on improving the employees' loyalty (for example, reducing employee turnover)
- The company does not have a formal system for orientation and induction of new employees

According to the way the company functions in the open versus closed system dimension, this is a company more of a closed system.

3. LIMITATIONS TO THE RESEARCH

In this research there are several limitations. Firstly the sample used is not a representative sample. Having surveyed only one company in Republic of Macedonia, it cannot give a whole picture about the organizational alignment of the companies neither in Republic of Macedonia nor in the food industry in the country. Another limitation to the research is the limitation in terms of socio-ethnicity. This research was done in a company where the ethnic majority is Macedonian; therefore it does not represent the ethnic structure of the country

Conclusion and recommendations

The aim of this paper was to analyse the organizational alignment of a company in the food industry in republic of Macedonia. Furthermore this paper had several objectives. Its objectives were to analyse the literature on the issue of organizational culture and alignment in the food industry; to assess the organizational alignment in a company in Republic of Macedonia; and to provide recommendations for improvement. For this needs of the paper and for meeting the research objectives a combination of desk and field research was used. In this respect a significant amount of information and data from published articles, journals and researches has been used for the comparison of the results obtained in this research. In addition to this a field research consisted of data gathering questionnaire has been used. This type of research is a pioneer research in Macedonia and the broader region. The results of this research were presented and analysed in Chapter 4 of this paper. In accordance to the proposed methodology, the research results non-formal part were presented in accordance to the four dimensions developed by the researchers: decision making and behaviour, people versus task, innovativeness and risk taking, open versus closed system; and there will be explanation of the results for each dimension⁸. The formal part of the leader's questionnaire was presented in the second section.

Generally in the non-formal part the leader and the employees have aligned perceptions on the four dimensions on the company. Therefore the

⁸ Tomovska- Misoska A., Bojadziev M., Stefanovska M., Nikolovska Z.,(2011) 'Vox Organizationis theoretical basis and methodological considerations in the development of an instrument for organizational culture'

conclusion is that this company has satisfactory level of organizational alignment, which translates into good organizational functionality and progress. In the formal aspects of the company there is a clear view that the company functions with more bureaucratic than democratic principles on the decision-making and behaviour dimension. Furthermore in the people versus task dimension we can clearly see that the company is task oriented. In terms of innovativeness and risk taking dimension, we can conclude that the company has medium level of innovativeness and risk taking. According to the way the company functions in the open versus closed system dimension, this is a company more of a closed system. There is an obvious difference between the non-formal functioning of the company and the formal aspects of the same company. In the non-formal part of the research the employees and the leader have aligned perception that the company has democratic principles, people oriented, innovative and has open system. Unlike in the non-formal aspects, the formal functioning of the company shows that it has bureaucratic principles, task oriented, medium level of innovativeness and risk taking, and has closed system. Considering this results obtained from the research in this paper I can propose some recommendation for improvement for the company. As mentioned before the non-formal part the leader and the employees have aligned perceptions on the four dimensions on the company, but the formal principles of the company are not properly aligned with the non-formal functioning. This may translates into inefficient functioning of the company.

Considering the general findings and the limitations of this paper, there are some suggestions for further research as well. Firstly getting a representative sample for this research was an obstacle; therefore we can suggest further research with larger number of respondents. Secondly, we suggest the research to be done in more than one company in the industry. In this research only one company in Republic of Macedonia was surveyed, and it cannot give a whole picture about the organizational alignment of the companies neither in Republic of Macedonia nor in the food industry in the country. Thirdly, another obstacle in this research was the limitation in terms of socio-ethnicity. Therefore we suggest a further research to be done not only in companies where the ethnic majority is Macedonian but also in companies with different ethnic majority. With this improvement the research can represent the organizational alignment and culture in terms of socio-ethnicity in the country.

References:

1. Bakke, W.E. (1959) Concept of social organization. pp. 16-75, in: Haire, M. (ed), *Modern Organization Theory*, New York, NY: John Wiley.
2. Chon, N. (1991) "Alignment" Theory: Creating Strategic Fit , The' Management Decision. 29 (1): pp. 40-41. <http://centstrat.com/wp-content/uploads/2008/06/strategic-alignment.pdf>
3. Denison, D., Mishra, A. (1995)'Organizational Culture and Effectiveness:A theory and some preliminary empirical evidence, Academy of Management Best Paper Proceedings, pp. 168-172.
4. Henderson, J. and Venkatraman, N. (1990) 'Strategic Alignment' <http://dspace.mit.edu/bitstream/handle/1721.1/49184/strategic-alignme90hend.pdf> (Accessed: 26/10/2013).
5. Hofstede (1998) Attitudes, values and organizational culture: Disentangling the concepts, *Organization Studies*, 19 (3), pp. 477-492.
6. Hofstede, G., Neuijen, B., Ohayv, D., and Sanders, G. (1990) 'Measuring Organizational Cultures; A Qualitative and Quantitative Study across Twenty Cases' *Administrative Science Quarterly*, 35 pp. 235-316.
7. Habil, W. (2011). Rationality and irrationality of Max Weber's bureaucracies. *International Journal of Management & Business studies*, 1(4), <http://www.ijmbs.com/14/wasim.pdf> (Accessed: 29/10/2013).
8. Labovitz, G. (2004) How the Right Tools Enhance Organizational Focus. *Business Performance Management*.
9. Lois, J. and Fischler, L. (2008) 'Time to Check Your Alignment?' *Issues and Observations*. 28 (2):
10. McKinsey , 2011 7S Model: A strategic assessment and alignment model
11. O'Reilly, C.A., Chatman, J. and Caldwell, D.F. (1991) People and organizational culture: A profile comparison approach to assessing person-organization fit, *Academy of Management Journal*, 34 (3), pp. 487-516.
12. Powell, T. (1992) 'Organizational Alignment as Competitive Advantage' *Strategic Management Journal*. 13 (2): pp. 119-134. http://www.thomaspowell.co.uk/article_pdfs/Org_alignment_as_CA.pdf(Accessed: 29/10/2013).

13. Luham, J., Cunliffe, A. (2012) 'Key Concepts in Organization Theory'
14. http://www.sagepub.com/upm-data/37949_Chapter2.pdf (Accessed: 28/10/2013).
15. Saunders M., Lewis P., Thornhill A.,(2003) 'Research Methods for Business Students'
16. Schein, E.H. (2004) *Organizational culture and leadership*. San Francisco: Jossey Bass.
17. Swedberg, R., (1999) 'Max Weber as an Economist and as a Sociologist: Towards a Fuller Understanding of Weber's View of Economics' *American Journal of Economics & Sociology*. Oct99, Vol. 58 Issue 4, p561-582. 22p.
18. Semler, S. (1997) 'Systematic Agreement: A Theory of Organizational Alignment' *Human Resource Development Quarterly*. 8 (1):pp. 23-40.
19. Treven, S., Mule, j M.,Lynn, M.(2006)'The impact of culture on organizational behavior'
20. Tosti, D. (2007) 'Aligning the Culture and Strategy for Success', *Performance Improvement*. 46 (1):
21. Taylor, F.W. (1947)'Principles of Scientific Management'. New York, NY: Harper,pp.161-282.
22. Tomovska- Misoška A., Bojadziev M., Stefanovska M., Nikolovska Z.,(2011) 'Vox Organizationis – theoretical basis and methodological considerations in the development of an instrument for organizational culture'
23. Tsui, A.S. Wang, H and Xin, K.R. (2006) *Organizational culture in China: An analysis of culture dimensions and culture types*, *Management and Organization Review*, 2 (3), pp. 345-376.
24. Wren D., Bedelan A., Breeze J. (2002) ' The Foundations of Henry Fayol's Administrative Theory',pp. 33-47.
25. Windsor, C. A. and Ashkanasy, N.M. (1996) *Auditor independence decision-making: The role of organizational culture perceptions*, *Behavioral Research in Accounting*, 8, pp. 80-97. Williams, S.L. (2002) *Strategic planning and organizational values: links to alignment*, *Human Resource Development International*, 5 (2), pp. 217-233.

UDC 339.564:339.727.22(497.7)
330.55:339.727.22(497.7)
Original scientific paper

TOME NENOVSKI*
NINKO KOSTOVSKI**
DOBRILA DEJANOSKA***

INFLUENCE OF FOREIGN DIRECT INVESTMENTS TO EXPORT AND GROSS DOMESTIC PRODUCT OF DEVELOPING COUNTRIES – SPECIFICS OF REPUBLIC OF MACEDONIA

Abstract

It is widely accepted that the foreign direct investments play important role in the economic growth of the developing countries. They provide capital and positively affect these countries by transferring new technologies, establishing quality human capital, promoting integration into the global markets and the international community. In these terms, it is to expect that the foreign direct investments would also largely contribute to the host countries gross domestic product and their exports. While our research of the Republic of Macedonia time series proves significant correlation between the foreign direct investments and the gross domestic product growth, the association between the foreign direct investments and the growth of the exports is weak. We indicate on several topics for further research that would help better understanding of these results and conclude that the country specifics require detailed research in a wider social context if we want to learn more about the role of the foreign direct investments and before suitable recommendations to the policy makers can be made.

Key words: Foreign Direct Investments, Exports, Gross Domestic Product, Economic Development, Developing Countries

JEL Classification: E22, E44, F21

* Prof., Ph.D, University American College Skopje, e-mail: nenovski@uacs.edu.mk

** Prof., Ph.D, University American College Skopje, e-mail: kostovski@uacs.edu.mk

*** MBA, Head of Finance and Accounting, Ciklama Engineering, Skopje E-mail: contact@ciklama.com.mk

Introduction

The international capital flows, in general, gained significant momentum with the globalization. The same is true for their major subset, that of the foreign direct investments, that include mergers and acquisitions, building new facilities, reinvested profits, intra company loans and more than 10 percent voting stock in an enterprise operating in economy other than that of the investor. Financially speaking, the foreign direct investment is the sum of all capital transactions in the balance of payment of a given country. In more confined definition, the stock of the foreign direct investments refers to the difference between the total inward and the total outward direct investments of a country at a given date, (end of the year), excluding the portfolio investments. Foreign direct investments are all net inflows made by non-resident investors in the reporting economy. In these terms, strictly speaking, even the investments done by economic emigrants in their home country meet the criteria, at least before they return at home, if ever (WB, 2016).

The achievements of some of the fast developing countries during 1990s in the successful utilization of the foreign direct investments for the economic growth, put them into the lime light of many economists and policy makers around the world. There was even substantial jockeying of the countries in inviting the multinationals. With the domestic investment limited by lack of local demand, technology requirements, limited access to capital, the external stimuli to the investment process provided by foreign investors are critical for capital formation in many developing economies, typically plagued with low productivity, wages and saving. The foreign direct investments break this vicious circle. Moreover, the foreign direct investments also facilitate the access to the new technologies, knowhow and managerial practices. This raises not only the industrial output, but the competitiveness of the host countries. Globalization of the markets promoted further the growth of the emerging international investment sector. The developing, emerging and transitional economies all liberalized their legislations and employed various economic measures to attract more foreign investors. However, there are still various theoretical approaches to the effects of the relationship between the foreign direct investments and the gross domestic product and the exports. This paper explores these relationships in more detail in case of the economy of the Republic of Macedonia.

1. ROLE OF FOREIGN DIRECT INVESTMENTS IN DEVELOPING COUNTRIES

Many developing countries invite the foreign or multinational companies and provide various concessions expecting that the foreign investments will serve as substitutes for the missing local capital, lack of business initiative and shortage of knowledge. During the 1990s, many economists and policy makers praised the foreign investments as panaceas for virtually all development problems. Moreover, the entire concept of economic globalization was often equalled with the foreign direct investments. However, there are many who disagree stressing that the foreign investments are much more snake oil since they work only in the countries with already large local markets. Moreover, even then, when they leave, in the country nobody is better off, but actually poorer than before (Haynes, 2003).

2. MOTIVES FOR FOREIGN DIRECT INVESTMENTS

The literature on the foreign direct investments indicates on three most frequent motives for a company to invest abroad and hence on three main types of foreign investments: resource seeking, market seeking and efficiency seeking. According to Kudina and Jakubiag (2008) the availability of natural resources, raw materials and crops, together with the abundance of cheap labor attract the resource-seeking investors. The only requirement is reliable business infrastructure. Market-seeking investors are attracted by the size of the host country market and its potential for growth. For these investors, the market of the host country, if big enough, provides them chances to expand their sales and profits. This will allow them to stay competitive and grow internationally and at their native countries. Expanding the total markets where they sale these companies achieve extra economies of scale of their operations with yet focused scope. The countries with large market size and fast economic growth are particularly interested for these companies. The efficiency seeking investors look for ways to improve their cost effectiveness and thus their competitiveness. The efficiency seeking multinational companies prefer low wages countries with sufficiently skilled local labor. These companies are ready to trade off the lower labor productivity with the lower wages, achieving targeted productivity-adjusted labor costs that will allow them to pursue international cost leading strategy. However, they require availability of significant local

business services and friendly trade policy reflecting high degree of openness, as well as favorable currency rates. These factors are among the key location criteria for this type of investors. The degree of the development of the host country is instrumental for the location decision since it indicates on existence of the entrepreneurship attitude, quality education and reliable infrastructure, conclude Kudina and Jakubiag (2008).

3. FOREIGN DIRECT INVESTMENTS AND THE EXPORT

There is a lack of consensus among the scholars about the influence of the foreign direct investments and the host country exports, or more generally, on the relationship between the international factor movements and the international trade in goods. Although some recent research show that the foreign direct investments can stimulate the export growth, some other point out that the foreign investments can actually inversely affect the export, or at least the trade balance. Authors, like Kutan and Vuksic (2007a), highlight the positive effect of the foreign direct investments for the host country exports. Other, like Radulescu and Serbanescu (2012) argue that the foreign direct investments do not contribute, or at least, not significantly contribute to the growth of the exports, with some cases, when these investments can even worsen the trade balance, boosting the import and the consumerism in the host country.

Nevertheless, the positive effect of the foreign direct investments in promotion of the exports of a given host country may be summarized as direct and indirect. The direct effects refer to the actual export made by these foreign investments from the host country to the international market. The indirect effect stems from the influence on the performance of the domestic companies. The local companies have to meet high quality standards if they want to be part of the supply chain. However, the positive impact on the host country exports might not be present in all cases. For example, in case of the foreign direct investments in the non-tradable sectors of the host economy. Moreover, in the sectors in which the domestic companies already are exporting this additional offering might even move the local companies out from the market. According to Kurtishi (2013) the impact of foreign direct investments on the host country trade with the world, differs depending on the prevailing motive of the foreign investors. She claims that the output from the efficiency-seeking foreign direct investments is typically intended for export. Therefore, the impact of these

investments is likely to increase the overall exports from the host country. If the local firms can provide significant input to these investments, the value added of such exports could be much greater. In the cases where the intermediate goods are imported, the efficiency seeking foreign direct investments will simultaneously increase the imports. Nevertheless, since a good portion of the value-adding business processes is located within the host country, the impact on the trade balance and country value creation is positive. Regarding the market seeking investors, Radulescu and Serbanescu, (2012) stress that they expand the imports, but have no effect of the exports from the host economy unless the informal or other alternative channels of indirect export are not present.

Kutan and Vuksic (2007) surveyed the impact of the inward foreign direct investments in 14 transitional economies of Central and Eastern Europe, between 1993 and 2001, and found that they all improved their export performance. Their results indicated that the foreign direct investments had unambiguously positive and significant impact on the exports of the countries of the sample, as well as in the case of the two subsamples: the more advanced transitional economies and the new EU member states, and (2) for the group of transitional countries, Russia and Ukraine. However, they also found that the positive impact on the exports was much stronger in the case of the first subsample, possibly reflecting the fact that these countries have managed to attract more export oriented foreign direct investments. Surveying the potential for improvement of the export performance of the Croatian manufacturing by attracting more foreign direct investments, Vuksic (2005) using panel data for 21 manufacturing sectors between 1996 and 2002, found that the foreign direct investments in Croatia positively affected exports, but the extent of that impact is relatively low.

Radulescu and Serbanescu (2012) surveyed the relation between the foreign direct investments and the exports from the Central and Eastern European countries between 1990 and 2010 using statistical data and literature review and underlined the factors that determined the increase of exports from these countries. According to them, the foreign direct investments can contribute to higher exports by increasing the supply capacity and/or through foreign direct investments specific effects as multinational enterprises may have better knowledge about foreign markets, superior technology, lower production costs, and better ties to the supply chain of the parent firm than do local firms. They found that, the inflows of for-

eign direct investments contributed to the higher supply capacity of those countries, leading to more exports. On the other hand, the evidence for the foreign direct investments specific effects is mixed. The results suggest that this effect has been present mainly in the case of the new EU member states, reflecting, among other things, the higher amount of foreign direct investments that this countries received relative to the other countries of the Southeast Europe, but also the higher productivity of the local companies acquired by multinational companies.

Analyzing the foreign direct investment and its impact on economic growth in the Central and Eastern European countries between 2000 and 2012 , Hlavacek and Bal-Domanska (2016) found statistically significant link between the foreign investment and the gross domestic product. They also found spatial disproportion with in the inflow of foreign investment and in economic growth. Estonia, Hungary, the Czech Republic and Slovakia report high influence of the foreign direct investments to the gross domestic product while Lithuania, Poland, Latvia, and Slovenia report lower influence. That the foreign big companies present can also harm the local partners was originally noticed by Hamlett at al. (2008). During the 1970s, in case of UK they practically eliminated from the market the vibrant sector of small businesses set by the layoff workers. Similar effect is noticed by the US and Canada, too. The foreign big company first approach the local manufacturers, farmers and providers of various business services driving them from their local business partners. Once when they with low prices eliminate the competition, start growing the prices and offering unfavorable deals to the local suppliers. The buyers are left without alternative, as well as the suppliers. Since their former customers are out of the business, the local suppliers have no other option but to accept these detrimental new terms of cooperation. The Canadian National Bureau of Competition issued a special guide for the local communities how to trace and prevent such damaging practices (Predatory Pricing Enforcement Guidelines, 2009). Similar happened in the case of two big foreign direct investment in Republic of Macedonia in 2015 and 2016, when two big market seeking investors, McDonald's and Carrefour forced their local subsidiaries into bankruptcy leaving many people jobless in a short notice and many suppliers not compensated. No matter this, Krstevska and Petrovska (2012) using panel regression to assess the foreign direct investments impact on the export, employment and GDP in the case of the Republic of Macedonia, found that the foreign direct

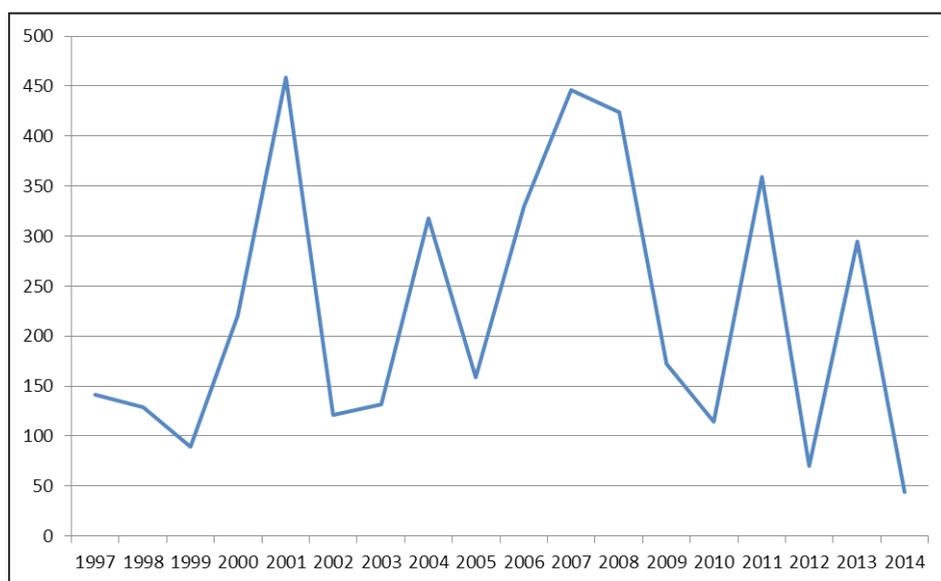
investments inflows, between 2002 and 2007, were important factors of the growth of the exports from the country.

4. FOREIGN DIRECT INVESTMENTS IN REPUBLIC OF MACEDONIA

Republic of Macedonia is a relatively new destination for foreign direct investments. In the past, numerous government strategies failed to bring tangible effects in terms of more foreign investments. The foreign investors were much more factor seeking and targeted the mining and steel, minerals, fresh fruits and vegetables or were market seeking and targeted the telecommunications, cable operations, utilities, financial services and health, the sectors with small but steady customer base. Only the radical and for some analysts and practitioners, controversial decision to set up a nationwide network of free industrial parks of high technologies, started to attract more significant numbers of efficiency driven investors. The country output and the GDP started to grow, the export also, even during the years plagued with recession or post- recession recovery in rest of the Europe. Currently, the foreign direct investments contribute to the increase of the country export and to the change of its structure towards more value added goods. Being a small transitional economy and lacking domestic capital, Republic of Macedonia had very high unemployment rate and low international competitiveness. The decisive commitment towards improvement of the business ambient, investments in the infrastructure and in education, only recently created the fundamental basis for moving forward from the previous vicious circle of low GDP, low employment, low saving and thus insufficient investments. In other words, the country promotes the foreign direct investments a main factor of its growth. Thus, one of the basic aims of the macroeconomic policy of the Republic of Macedonia today is to create environment in which the major investors will be the companies from abroad. Consequently, the authorities now are concentrated on maintaining a stable macroeconomic environment conducive for their business. This was significant change in the strategy and policies regarding the foreign direct investments. The country finally moved from the previous passive approach towards an aggressive quest for investors, radically removing any unnecessary administrative obstacles, introducing a flat corporate tax and fading the import duties. All of that was accompanied with large promotional campaign of these measures in some leading newspapers, magazines

and TV channels worldwide, stressing the suitable location close to the EU, reliable infrastructure and good educated workforce. Moreover, the free trade agreements that the country has with Turkey, Ukraine, CEFTA, EFTA and EU are additional incentives for location decisions of the efficiency driven investors. For the opponents of these policies, the results are maybe there but the actual figures are lukewarm. The Chart 1 shows the inflows of the foreign direct investments in the country. The peaks are results of the large major privatizations in the telecom, utility sector and banks; they claim (Kurtishi-Kastrati at al., 2016).

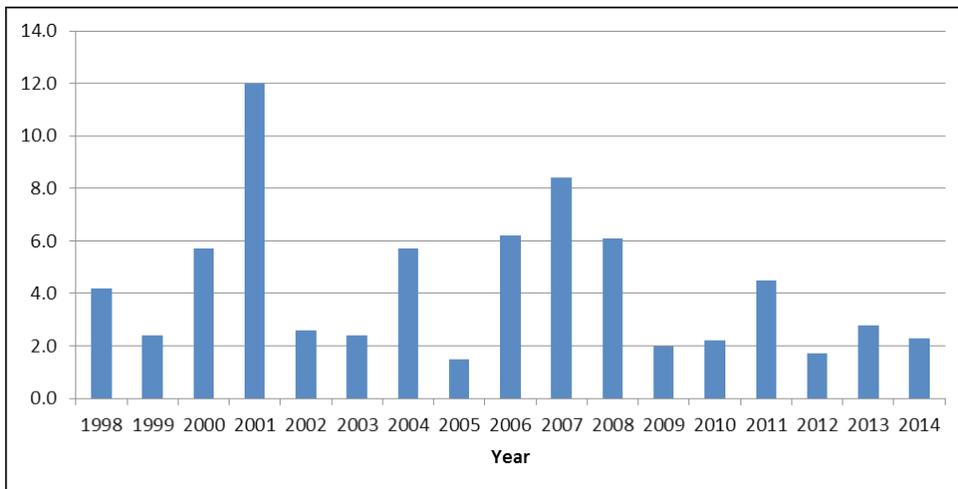
Chart 1 - Foreign Direct Investments in Republic of Macedonia, 1997 and 2014 (mil EUR)



Source data: National Bank of Republic of Macedonia

Between 2001 and 2014, the average annual growth rate of the foreign direct investments was 11.1%. The average annual foreign direct investments net inflows relative to the GDP, between 1998 and 2014 is app. 4%, much less than in the case of the other economies in the region (Bulgaria, Serbia, Montenegro, Albania), not to mention countries like Hungary, Slovakia, or the Baltic states.

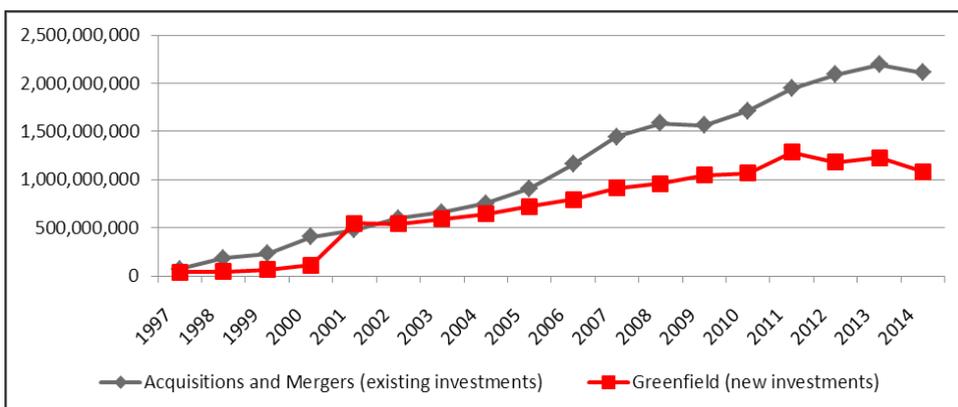
Chart 2 - Foreign Direct Investments in Republic of Macedonia as percentage of GDP



Source data: National Bank of Republic of Macedonia

Chart 3 depicts the overall structure of the foreign direct investments in terms of their two main forms, the acquisitions and the green-field investments, cumulative, from 1997 to 2014.

Chart 3 - Foreign Direct investments in Republic of Macedonia by type of the venture

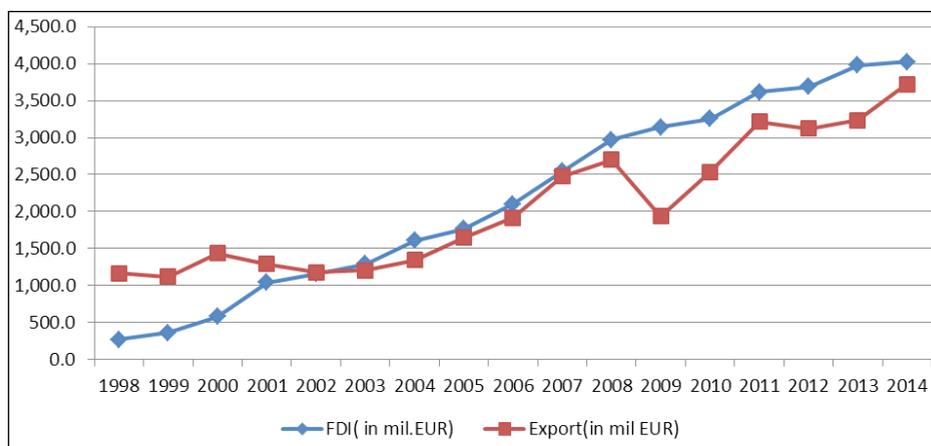


Source data: National Bank of Republic of Macedonia

Regarding the sector dispersion of the foreign direct investments, the services account for app. 51% of the total foreign direct investments stock, during the entire surveyed period. Regarding the countries of the origin, the majority of the foreign direct investments in the Republic of Macedonia currently are from Netherlands (22%), Austria (13%), Greece (11%), Slovenia (10%), Cyprus (9%) and Hungary (6%).

Since the local market is small, it is easy to predict that the growth of the foreign direct investments in case of the Republic of Macedonia will lead in a similar growth of the country exports. The foreign direct investments generate 60% of the country export (UNCTAD, 2012).

Chart 4 - Foreign Direct Investments and Export in Republic of Macedonia from 1998 to 2014



Source data: National Bank of Republic of Macedonia

As it can be seen from the Chart 4, the growth rate of the total stock of the foreign direct investments almost entirely matches that of the export from the country. Moreover, while the detrimental impact of the global economic crisis 2008 - 2009 and the aftershock in 2012 - 2013 is well depicted in the case of the exports, the foreign direct investments were practically not affected and kept almost straight-line trend. Table 1 shows the total stock of foreign direct investment, annual export and GDP from 2002 to 2012, and their increments. Chart 5 presents the increments of these three variables.

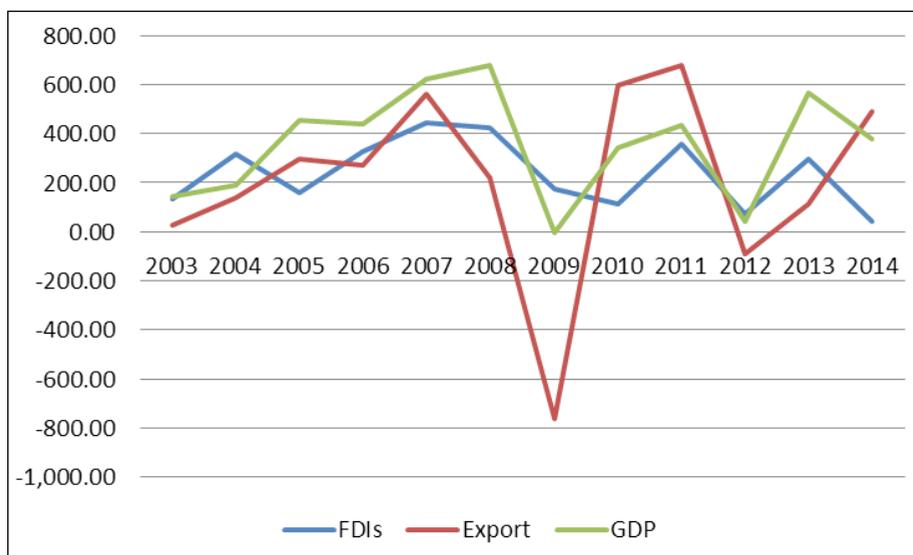
Table 1 Foreign Direct Investment, Export, GDP, and their increments

Year	FDIs	Export	GDP	Change in FDI	Change in Export	Change in GDP
2002	1,160.70	1,178.30	4,240.53			
2003	1,292.13	1,207.10	4,385.85	131.43	28.80	145.32
2004	1,610.22	1,345.90	4,577.71	318.09	138.80	191.86
2005	1,768.97	1,644.40	5,031.87	158.75	298.50	454.16
2006	2,098.57	1,917.50	5,472.27	329.60	273.10	440.40
2007	2,545.16	2,477.10	6,094.57	446.59	559.60	622.30
2008	2,968.75	2,697.60	6,772.02	423.59	220.50	677.45
2009	3,141.37	1,937.00	6,766.81	172.62	-760.60	-5.21
2010	3,255.97	2,534.90	7,108.76	114.60	597.90	341.95
2011	3,615.08	3,214.90	7,544.20	359.11	680.00	435.44
2012	3,685.54	3,124.00	7,584.92	70.46	-90.90	40.72
2013	3,979.96	3,235.20	8,150.00	294.42	111.20	565.08
2014	4,023.63	3,723.00	8,530.00	43.67	487.80	380.00

Source data: National Bank of Republic of Macedonia

The average foreign direct investment increment in this period is 238 million Euro with standard deviation of 133.41. The average export growth is 212 with standard deviation of 372 and the average growth of GDP is 357 with standard deviation of 213 million Euro. In other words, the figures are quite volatile and difficult to predict. This can be seen also from the Chart 5 that depicts the increments of these three variables in case of the Republic of Macedonia, between 2003 and 2014.

Chart 5 Table 1 Increments in Foreign Direct Investment, Export and GDP



Source data: National Bank of Republic of Macedonia

Due to this high volatility, the attempt to prove the presumed high correlation between the foreign direct investments and the exports, at least in the case of the Republic of Macedonia, turns correlation ratio of 0.25 and thus fails, since it is very weak to be statistically significant. The correlation between the foreign direct investments and the GDP is stronger, 0.64, and more than moderately significant. Only if three years moving averages are used, the correlation between the foreign direct investments and the exports, between 2004 and 2013, grows to 0.35, but being still below the presumed. The correlation between the foreign direct investments and the GDP in that case reaches 0.72.

Conclusions and Recommendations

High correlation does not imply actual cause-effect between two variables. Inversely, a failure of statistical attempts to show such association does not imply that relationship does not exist. Serious economists

would never argue the influence of the foreign investments on the growth in case of developing countries. However, researchers eager to deep probe the issue argue that the growth of the exports based on factor driven foreign investments is not necessarily prudent for the host economy and could lead to depletion of natural resources and over-exploration of local labor. In case of market driven investments, the conclusion that they not contribute to the export, while significantly drive up the import, might not hold always. Buyers in the big shopping malls in Skopje or Thessalonica are often from Macedonia and Kosovo, respectively. Politicians welcome the efficiency driven investments since they boost the industrial output, value added and GDP. However, these investors transfer their profits and leave only the payroll checks in the host country. On the other hand, when the expatriates invest in their homeland, their ventures are accounted as domestic.

No matter that data we collected failed to reveal stronger links between the foreign direct investments and the export in case of the Republic of Macedonia, this does not imply that the policy makers should stop considering the foreign investment important contributor for the export. This particularly having in mind that the recent foreign direct investments, at least in the case of the Republic of Macedonia, significantly changed the structure of the exports, introducing more value added products such as automotive parts, processed food, special steel, quality textiles and high valued business services and software.

References:

1. Canadian National Bureau of Competition (2009) "Predatory Pricing Enforcement Guidelines" available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/02713.html> viewed 28.03.2016
2. Hamlett, J., Alexander, A., Bailey, A, and Shaw, G. (2008). "Regulating UK supermarkets: An Oral-history Perspective". Available at <http://www.historyandpolicy.org/policy-papers/papers/regulating-uk-supermarkets-an-oral-history-perspective> viewed 20.03.2016
3. Haynes, J. (2003). 'Tracing connections between comparative politics and globalization'. *Third World Quarterly*. 24 (6). pp. 1029-1047.

4. Hlavacek, P, & Bal-Domanska, B 2016, 'Impact of Foreign Direct Investment on Economic Growth in Central and Eastern European Countries', *Engineering Economics*, 27, 3, pp. 294-303
5. Krstevska, A. and Petrovska, M. (2012) The economic impacts of foreign direct investments: panel estimation by sectors on the case of Macedonian economy, *Journal of Central Banking Theory and Practice*, 1(2), pp. 55-73.
6. Kudina, A. and Jakubiak, M. (2008) The Motives And Impediments To foreign direct investments In The CIS, OECD Global Forum on International Investment.
7. Kurtishi, S. (2013) The Effects of Foreign Direct Investments for Host Country's Economy, *European Journal of Interdisciplinary Studies*, 5(1), p.26-38.
8. Kurtishi-Kastrati, S., Ramadani, V., Léo-Paul, D., Ratten,V (2016) "Do foreign direct investments accelerate economic growth? The case of the Republic of Macedonia", *International Journal of Competitiveness*
9. Kutan, Ali M. and Vukšić, G. (2007) Foreign Direct Investment and Export Performance: Empirical Evidence," *Comparative Economic Studies*, 49(3), p.430-445.
10. Radulescu, M. and Serbanescu, L. (2012) The Impact of Foreign direct investments on Exports, and Export Competitiveness in Central and Eastern European Countries, *Journal of Knowledge Management, Economics and Information Technology*, 1(8), p.1-37.
11. Vukšić, G. (2005) Impact of Foreign Direct Investment on Croatian Manufacturing Exports, *Financial theory and practice*, 29, p. 131-158.
12. Vukšić, G. (2007) *Foreign Direct Investment and Export Performance of the Transition Countries in Central and Eastern Europe*. Available at www.ijf.hr/eng/employees/vuksic.pdf, [Accessed Date 01/07/2015]
13. World Bank (2016) "What is the difference between Foreign Direct Investment (FDI) net inflows and net outflows?", available at <https://datahelpdesk.worldbank.org/knowledgebase/articles/114954-what-is-the-difference-between-foreign-direct-inve>, accessed may 30, 2016

KATERINA FOTOVA ČIKOVIĆ*

EFFECTS OF THE ENTRANCE OF FOREIGN CAPITAL IN THE MACEDONIAN BANKING SECTOR

Abstract

Internationalization of the banking sector has had a tremendous impact on financial integration and economical development. It offers banks the possibility to determine and establish their optimum size, to provide economies of scale and range, to diversify their activities and to increase their revenue and profitability.

The purpose of this paper is to determine the effects of the entry of foreign capital in the banking sector in the Republic of Macedonia.

The results of the research show that despite of the large number of conflicting opinions in relation to the benefits from FDI in banking, in the case of the Republic of Macedonia, it can be concluded that in general, the effects were relatively positive and they appeared in the form of increased loans, modernization of the equipment and technology used by the banks, as well as greater availability of services to banks, due to the investments in the opening of new branches and offices in the country. The entrance of foreign banks and groupations in the Macedonian banking sector resulted in higher competition, decreased prices of banking products and services and lower number of banks on the market. The consolidation of the banking industry stimulated strong competition, where competitors are more capable, offer better quality of the bank services and products, as well as new products and services.

Keywords: FDI, foreign capital, commercial banks, Republic of Macedonia, banking

* M.Sc., MBA, PhD Student and researcher, Skopje, R. Macedonia e-mail: katerina.fotova@gmail.com

JEL Classification: G21, G34, F21

Introduction

In the past three decades, as a result of the globalization, liberalization and deregulation, the world (and especially the former socialist countries) has faced an increased entry of foreign capital in their financial sectors, especially in the banking sectors as the most profitable and most dominant sectors in the economies of these countries.

The theory suggests that there is a relation between the FDI and the economic growth of the host country. FDI in the banking sector are even more interesting for research, considering the fact that the banking sector is a key part of the financial system and has a tremendous influence on the financial stability of the country.

Crossborder (international) banking not only brings benefits to the host economy, but it actually gives banks opportunity to determine their optimum size, to achieve economies of scale and scope, to diversify their activities and to increase their income. With bank internalization, these benefits are expected to expand in the whole banking sector, leading to better and more efficient banking practices, better integration, greater depth, width and liquidity of markets. When foreign banks invest in transition countries, they bring their expertise and best risk management practices in order to reduce the risk of the acquired banks. They have more experience and more sophisticated financial systems, and thereby, they have much bigger chance and probability to increase the pressure on the local authorities to reform the financial system and make it more efficient.

In the extensive literature regarding this subject, there are many studies analyzing the effects of M&As with foreign banks and the banks' performance and efficiency after the acquisition (Figuera and Nellis 2009). According to Fraser and Zhong, (2009), in the short term, the acquisitions of banks by foreign banks have positive effects on the performances and the profitability of the bank, due to the expected long term positive effects of the transaction and the reaction of the market. Foreign banks that penetrate the transition markets improve the stability and the performance of the acquired banks and thereby strengthen the local financial stability. (Crystal, Dages and Goldberg, 2001). Proponents of FDI in the banking sector claim that the foreign banks can achieve better economies of scale

and higher diversification of risk in comparison with the domestic banks, by introducing new technologies (especially in risk management), better supervision and regulation and higher competition. (Detragiache, Gupta and Tressel, 2006).

This paper analyses the benefits and the negative aspects Macedonian banks have experienced ever since their internalization. It will also give an historical overview of the entrance of foreign capital in the country's banking sector. There are many studies which have examined the effects of the entrance of foreign capital in the banking industry; however, these studies have concentrated on developed markets and transition markets, but there are very few findings regarding the Macedonian banking sector. Our study contributes to the literature by researching how the FDI have influenced the banking sector in the country.

1. HISTORICAL OVERVIEW OF THE ENTRANCE OF FDI IN THE MACEDONIAN BANKING SECTOR

At the time of the monetary independence, there were only 5 banks operating in the Republic of Macedonia. However, as a result of the more liberal regulation to opening banks, in just one year, in 1993, this number climbed to 20 banks. In those first transition years, Macedonia (as well as the other neighboring countries) has introduced a liberal approach to establishing new banks. (Trpeski, 2003) This approach has required a small amount of capital and a quite simple procedure for issuing license. This has resulted in entrance of speculative capital in the banking sector, which easily enters the country but also easily exits it. (Pozzolo, 2009)

At the end of 1998, there were 22 commercial banks, 2 branches of foreign banks and 18 saving houses in the banking sector. What is interesting is the fact that until 31.12.1998, the participation of the foreign capital in the total capital in the Macedonian banks has been 15.5%.

In year 2000, strategic foreign investors entered the banking sector. This is the year with most FDI in the banking sector ever since the independence. Furthermore, 2000 is the year when NLB Group from Slovenia bought the majority shares in Tutunska banka and the NBG from Greece acquired Stopanska banka AD Skopje. Thereby, the participation of the foreign capital in the total capital in the banking sector has risen from 19.3% in 1999 to 40.8%. (NBRM, 2001)

The process of consolidation of the banking sector has been initiated by these acquisitions, and it has continued in the later years, followed by higher and fiercer competition, lower number of banking institutions but growth of the banking system, as well as reforms in the payment system.

In 2007, “Ohridska banka” AD Ohrid has been acquired by “Societè Generale” s.a. Pariz, “Komercijalno investiciona banka” AD Kumanovo by “Milestone” ehf Rejkjavik and “Internacionalna privatna banka” AD Skopje has been acquired by “Alfa Finance Holding” Sofija, after which the bank has been renamed into “Kapital banka” AD Skopje.

In 2008, Invest banka AD Skopje has been acquired by the Austrian Steiermärkische Sparkasse, which led to the creation of Sparkasse Makedonija AD Skopje. Other than this acquisition, Bulgarian CKB AD Sofija has taken over Sileks banka AD Skopje, and renamed it into CKB AD Skopje.

The Global financial crisis that occurred 2008 has inevitably left its mark on the Macedonian economy, thus the banking sector. Even though the effects of the crisis have occurred with a time lag, and were probably not as severe as the economies with developed financial markets, still, it has showed its impact. Even though the Macedonian financial markets are not well-developed, the crisis has had deep impact on the economy and the bank’s performances. What were recognized were slower growth of the financial system of the country, slowing of the process of entry of new foreign capital in the financial institutions as well as slower growth of the assets of the banking sector.

The banking system in Macedonia has remained stable, liquid and well capitalized. While NPLs continued to increase somewhat, they remained more than fully covered by provisions. The Macedonian banks (including subsidiaries of parent banks from the euro zone) are mostly financed by domestic resident deposits, do not depend on external wholesale funding, and have very limited credit exposure to countries or clients from the euro zone.¹

In 2009, more negative effects of the global financial crisis occurred, in the form of aversion to savings (at the side of the deponents) and psychological pressures while making decisions regarding financing clients (at the side of the banks). This has led to smaller financing and

¹ **Hafizi D., Bushi I.**, „Global Crisis Impact in Banking System for Western Balkan Countries“, *Economic Questions, Issues and Problems*, 2014, pp.117

lowering the amounts of loans approved in the economy.

In 2010, the banking activities have improved and have risen, due to the revival of the domestic economy. In 2012, Ziraat banka was acquired by Halk bank AD Skopje, and later in 2014 Postenska banka has been acquired by Eurostandard banka AD Skopje. In May 2016, a Swiss investment fund has taken over the small group bank Alpha banka AD Skopje. The acquisition was 1.2 million euros and the bank has been renamed in Silk Road Bank AD Skopje soon afterwards.

Nowadays, more than two decades after the monetary and country independence, the financial system of the Republic of Macedonia is characterized with very simple market structure, no complex financial groupations or cross-ownership between different sectors. It can be concluded that banks are the only institutions who dictate 'the rules of the game' and actually have a say and influence on the economy. (Fotova, 2011)

In the case of Macedonia, the consolidation of the banking sector has contributed to higher competition between more capable opponents, better quality of the services, cheaper cost of capital, introduction of new products and services and expansion of the financing offer. At the time of the introduction of the Macedonian currency (which was the same period of the basis of the Macedonian banking sector), the banking sector in 1992 was relatively underdeveloped and there were only 5 banks operating in the market.

Table 1: The restructurings in the Macedonian banking sector in the period of 1998-2015

<i>Number of banks in the Republic of Macedonia</i>		
<i>Year</i>	<i>Banks</i>	<i>Additional remarks</i>
1998	22+2	The license of „Aka Banka,, AD Skopje has been withdrawn. Two new institutions appear in the banking markets: MBDP- Macedonian Bank for Development Promotion and an affiliation of "Ziraat Bankasi".
1999	22+1	22 banks + 1 affiliation of a foreign bank

2000	22	Issued license for the International Commercial Bank of the People's Republic of China-Taiwan. Tutunska banka AD Skopje has become a part of the Slovenian NLB Group. Greek NBG has acquired Stopanska banka AD Skopje, whereas Alpha bank AE Athens has acquired Alpha bank AD Skopje.
2001	21	In 2001, NBRM has issued license to Eurosviss banka AD Skopje. Furthermore, NBRM has issued 3 licenses for status changes: merging of Zemjodelska banka AD Skopje to Sileks banka AD Skopje, merging of Pelagoniska banka AD Prilep to Komercijalna banka a.d. Skopje, as well as merging of Teteks banka AD Skopje to Kreditna banka AD Bitola.
2002	21	No changes in the structure.
2003	21	No changes in the structure.
2004	21	No changes in the structure.
2005	20	The license of "Radobank" AD Skopje is withdrawn and the saving house „Maleshevka,, AD Berovo has been acquired by „Invest Banka,, AD Skopje.
2006	19	Merging of „Tetovska Banka,, AD Tetovo and „Teteks-Kreditna Banka,, AD Skopje, thus creating "TTK banka" AD Skopje. The saving house „Makedonska stedilnica,, AD Skopje has been acquired by "Invest Banka,, AD Skopje
2007	18	The license of „Makedonska Banka,, AD Skopje is withdrawn. This year, Ohridska banka AD Skopje has become a part of the Societe Generale Group. Bulgarian Alfa Finance Holding takes over Capital bank AD Skopje.
2008	18	09/2008- Steiermärkische Sparkasse takes over Sparkasse Bank Makedonija AD Skopje (previously Invest banka AD Skopje), and CKB AD Sofija takes over CKB Banka AD Skopje.
2009	18	No changes in the structure.

2010	18	No changes in the structure.
2011	17	In January 2011, "Stater Bank" AD Kumanovo has merged into "Centralna Kooperativna Banka" AD Skopje. Halk Bank AD Skopje has bought the control package in IK Banka AD Skopje.
2012	16	Merging of „Ziraat Banka" AD Skopje and „Halk Bank,, AD Skopje.
2013	16	No changes in the structure.
2014	15	Postenska Banka AD Skopje has merged with Euro-standard Banka AD Skopje at 01.07.2014.
2015	15	No changes in the structure.
2016	15	In May 2016, Alpha Bank AD Skopje (a part of the Alpha bank AE Athens, Greece) has been acquired by a Swiss investment fund for 1.2 million EUR and has been renamed as Silk Road Bank AD Skopje.

Source: Fotova Čiković K., Fotov R., “Consolidation of the banking sector in Macedonia: effects and benefits”, International Conference on Economic Recovery in the Post Crisis Period, May 29-30 2015, Skopje

With these restructures and takeovers in the sector, the number of banks in the group of banks has changed (see table 2).

Table 2: Participation of foreign capital in the total banking capital in Macedonia (in %) from 1998-2015

Participation of foreign capital in the total banking capital in Macedonia (in %)	
1998	15,5
1999	19,3
2000	40,8
2001	40,1
2002	44,4

2003	48,6
2004	47,5
2005	52,5
2006	56,1
2007	69,1
2008	74,3
2009	68,6
2010	72,9
2011	74,7
2012	75,2
2013	75,2
2014	76,2
2015	74,8

Source: NBRM, Annual reports, 1998-2015

The participation of the foreign capital in 1998 has been 15.5%, and in 2015 it has reached an impressive participation of 74.8%. The biggest influx has been noted in year 2000, when the capitalization of Tutunska banka AD Skopje (Nova Ljubljanska Banka Ljubljana and LHB Frankfurt), Kreditna banka AD Skopje (Alpha Credit bank, Greece) and Stopanska banka AD Skopje (National bank of Greece, EBRD, IFC) occurred.

2. BENEFITS OF THE FDI FOR THE MACEDONIAN BANKS

Even though there are many opposite opinions regarding the benefits and effects of the internalization of the banks, in the case of Macedonia the effects were relatively positive. The consolidation of the banking sector has brought many foreign players in the market- around 71.8% of the shareholders are from the EU. (NBRM, 2014)

Due to this fact, it was inevitable for banks to modernize their marketing approaches as well as the technology they use and diversify the banking products and services. (Fotova Čiković, Fotov, 2015)

Table 3: Technology offered by the Macedonian banks

List of Banks	Technologies offered
Komercijalna Banka A.D. Skopje	Internet Bank, SMS Banking (for individuals and legal entities), m-Banka mobile application
Stopanska Banka A.D. Skopje	i-Bank (for individuals) with digital certificate, m-banking mobile application, e-banking (for legal entities), Phone banking
NLB Tutunska Banka A.D. Skopje	NLB klik using token, NLB Mobipay, NLB SMS Notification, NLB Proklik using token, NLB mKlik-mobile application
Halk Bank A.D Skopje	PayPass contactless cards, SMS notification, mobile banking, E-Banking
Sparkasse Banka A.D. Skopje	IndividualNet, NividualNet Plus, IndividualNet Plus- sToken
TTK Banka a.d. Skopje	e Banking; Web, e-mail & SMS notification
Ohridska Banka A.D.	<u>OBSGN@t- E-Banking</u>
Uni Banka A.D. Skopje	E- UNIBank (virtual bank)
Eurostandard Banka A.D. Skopje	E- Banking
Centralna Kooperativna Banka A.D. Skopje	E-Banking by using digital certificate for electronic signature
Alpha Banka A.D. Skopje	Alpha Web Banking (Web banking after the acquisition in 2016)
Stopanska Banka A.D. Bitola	E-Banking
Capital Bank A.D. Skopje	Microsoft CAPICOM- E- Banking
ProCredit Banka A.D. Skopje¹	E-Banking, Phone Banking and SMS Notifications

Source: Fotova Čiković K., Fotov R., “Consolidation of the banking sector in Macedonia: effects and benefits”, International Conference on Economic Recovery in the Post Crisis Period, May 29-30 2015, Skopje

As shown in table 3, we have conducted a research on the technologies currently used in Macedonian commercial banks. What we found out is that there is a positive correlation between the advanced technologies used by the banks (i.e. the more options for clients, the more software options and channels used) and their affiliation in a foreign group of banks, who are interested in the market and therefore investing in it. This review would actually confirm the fact that the Macedonian banks have benefited the merging by implementing new and modern technologies. This table shows the channels and types of software/technologies used by the banks. For instance, it can be concluded that NLB Tutunska Banka AD Skopje, Stopanska banka AD Skopje, Sparkasse Banka AD Skopje, Komercijalna banka AD Skopje and Halk Bank AD Skopje have been investing heavily in new channels and adjusting their offers to the market's needs. This only led us to the ultimate conclusion: the banks belonging to the group of big and middle-sized banks in the Republic of Macedonia can afford to offer modern technologies, software and gadgets to their customers, following the trends in the industry and the region, but that is not the case with the banks belonging to the group of small banks. (Fotova Čiković, Fotov, 2015)

This way, the Macedonian banks have gained access to innovation in banking, new assortment of banking products and services, different distribution channels, therefore higher growth of profits and customer base, by being a part of a bigger group of banks and having access to bigger funds, know-how and already applied software solutions. The consolidation of the banking industry has also stimulated fierce competition with more capable opponents, better quality of the services, lower cost of capital, and expansion of the financing offer.

3. NEGATIVE ASPECTS OF THE INTERNATIONALIZATION OF MACEDONIAN BANKS

There are many studies that show the positive effects of FDI and claim that FDI are crucial for the economical development, such as Crystal, Dages and Goldberg, 2001; Detragiache, Gupta and Tressel, 2006; Moreno and Villar, 2006. Then again, there are more and more studies in the literature that relate the negative consequences in the economy with the FDI. For instance, Claessens, Demirgüç-Kunt and Huizinga claim that the higher the participation of foreign investors, the lower the profitability

and the margins for the domestic banks. Vogel and Winkler (2011) point out that the foreign banks could transfer the financial disaster from their own countries into the host country.

The potentially negative effects of the internationalization of the banking sector are the possible reputational risks that acquired banks face. That way, the banks could lose their market power and position as well as their clientele.

In Macedonia, the reputational risk has increased in the case of NLB Tutunska banka, Stopanska banka and Alpha banka AD Skopje, the three of them in foreign ownership of banks coming from Slovenia and Greece, at the time when Slovenian and Greek economies weren't at ease.

In the case of NLB Tutunska banka AD Skopje, the bank has experienced reputation and security issues on more occasions. The first impact was in September 2012, when the media had published that the NLB d.d. Ljubljana's management has been under investigation, and the fact that the mother company is facing major losses due to the NPLs. The second impact the bank experienced was a larger-scale impact which had made deponents insecure and questioning the bank's ability to operate.

In June 2011, due to the crisis in the Greek economy, the Governor of the National Bank of the Republic of Macedonia had felt it was necessary to reassure the deponents in Stopanska banka AD Skopje (member of the Greek NBG Group) and Alpha bank AD Skopje (member of the Greek Alpha bank AE, Athens) that despite the crisis in Greece, the liquidity and capital adequacy of the two banks are high and there is no need to worry.²

Even though these turbulences did not leave long-term implications on the stability of these banks, they were actually a threat to the stability and efficiency of the whole banking system.

In order to determine whether this reputational risk has had an impact on these banks, we have analyzed the ratios of ROA and ROE of these three analyzed banks. The results (see table 4) show that the reputational risk they faced had no impact on their profitability, at least in the case of the big banks.

Namely, in the case of NLB Tutunska banka and Stopanska banka AD Skopje, the ratios ROA and ROE are constantly growing, even after

² **Fotova Čiković K., Fotov R.**, "Consolidation of the banking sector in Macedonia: effects and benefits", International Conference on Economic Recovery in the Post Crisis Period, May 29-30 2015, Skopje

2011/2012, the period when their mother banks were facing crisis.

Unlike them, Alpha banka AD Skopje (which enters the small banks' group) has experienced dramatic decrease in ROA and ROE in 2012, as a result of the net loss registered in the same year. Analyzing deeper in the financial statements of Alpha banka, we have found that in 2012 the bank has experienced decrease in interest income of 15% compared to 2011, while the interest expense stayed relatively unchanged. However, this loss is a result of the loan impairment charges in 2012. Thereby, it can be concluded that the Macedonian banks owned by Slovenian and Greek banks did not experience a decline in their profitability as a result of the crisis their mother banks faced.

Table 4: ROA and ROE of analyzed Macedonian banks in the period of 2009-2014

		ROA					
		<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>
NLB Tutunska							
banka		0,82	1,1	1,06	0,85	1,06	1,23
Alpha banka		-5,09	-8,14	-1,53	-8,34	-1,45	0,28
Stopanska banka AD Skopje		1,2	1,2	0,94	1,1	1,3	2,1
		ROE					
		<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>
NLB Tutunska							
banka		11,12	11,3	15,5	10,1	11,2	12,04
Alpha banka		-43,09	-75,73	-13,31	-96,96	-18,14	3,71
Stopanska banka AD Skopje		9,8	10,2	7,5	8,6	9,8	14,8

Source: Financial statements of the banks, 2009-2014

The negative aspects and the issues banks are facing as a result of the reputation of the mother-bank should not be underestimated and it is useful to create teams within the banks to actively manage these risks at all times.

However, according to Moura and Forte (2010), the effects of FDI on the economic growth depend on the existing internal conditions in the host country (the economic, political, social, cultural etc.). Thereby, the authorities in the host country play a crucial role in the creation of the conditions which will enable maximization of the benefits and minimization of the negative effects and their consequences.

Conclusion

The subject of this paper is to determine some of effects of the entrance of foreign capital in the banking sector as well as to give another perspective of some of the aspects that the banking sector has faced through internalization.

The results from the research show that in spite of the many different opinions regarding the benefits of FDI in banking, they actually brought more obvious benefits, in the form of increased financing, higher financial intermediation in the banking sector, modernization of the equipment and the technology used, as well as greater availability of banks' products and services (due to the expansion of the branch network of the acquired Macedonian banks).

The internationalized banks got an access to innovation in banking technologies, new assortment of banking products and services, various sales channels and higher growth of profits and clientele. They could not have possibly achieved this without having access to greater funds, know-how and already proven software solutions and market products and services.

However, it is worthwhile mentioning that there were some negative effects that some banks had to face, like the reputational risks Slovenian and Greek-owned banks in Macedonia had to experience. That has only temporarily "shaded" the benefits Macedonian banks experienced by the FDI in banking.

No doubt, the foreign capital in the banking sector in Macedonia has helped restore the clients trust in the banking and financial system. They have also established modern techniques for risk management and improved corporate management, and thereby contribute to a more stable banking system. It should come as no surprise that all the acquired banks by foreign investors and groups have led to a changed and improved IT system shortly after the acquisitions.

References:

1. Alfaro L., Chanda A., Kalemli-Ozcan S., Sayek S., (2006), "How Does Foreign Direct Investment Promote Economic Growth? Exploring the Effects of Financial Markets on Linkages", *Journal of Development Economics* 91, 2 pp. 242-256
2. Babic-Hodovic V., Mehic E., (2007), "Effects of mergers and acquisitions on B&H banking sector development", *JGSM – Journal of Global Strategic Management*, No.1
3. Duke A., Cejnar L., (2013), "Competition and the banking sector: friend or foe?", *Law and Financial Markets Review*
4. Filipović D., (2012), "Izazovi integracijskih procesa: Rast poduzeća putem spajanja, preuzimanja i strateških saveza", Sinergija, Zagreb
5. Fotova Čiković K., Fotov R., (2015) "Consolidation of the banking sector in Macedonia: effects and benefits", *International Conference on Economic Recovery in the Post Crisis Period*, May 29-30, Skopje
6. Kraft E., Hofler R., Payne J., (2004), "Privatizacija, ulazak stranih banaka i efikasnost banaka u Hrvatskoj: analiza stohastičke granice fleksibilne Fourierove funkcije troška", *Istraživanje I-14*
7. Mašić S., (2010), "Merdžeri i akvizicije kao strategija prekograničnog rasta europskih banaka", *XII međunarodni simpozijum "SymOrg 2010"*, Zlatibor, Srbija, 2010
8. Moreno R., Villar A., (2005), "The increased role of foreign bank entry in emerging markets", *BIS Papers No 23*
9. Pozzolo A.F. (2009), "Bank cross-border mergers and acquisitions", No 9, *Mo.Fi.R. Working Papers from Money and Finance Research group (Mo.Fi.R.) - Univ. Politecnica Marche - Dept. Economic and Social Sciences*, pp. 26
10. Ristić Ž., (2006), "Privatizacioni procesi u bankarstvu - motivi i modeli", *Panoeconomicus* 2, str. 191-221
11. Vogel U., Winkler A., (2011), "Foreign Banks and Financial Stability in Emerging Markets: Evidence from the Global Financial Crisis", *The Seventeenth Dubrovnik Economic Conference*

EDVIN MUSHE*

CUSTOMER SATISFACTION IN THE MACEDONIAN OIL RETAIL SECTOR

Abstract

In today's rapidly changing business environment and increased competitiveness, the battle to acquire and retain customers has imposed as a difficult and challenging task, especially for oil companies. Modern companies no longer perceive profit as an ultimate result of their business activities, rather they place more emphasize on customer satisfaction. This trend initiated a certain transformation in the practical concept of customer satisfaction, by changing companies' strategic focus from internal to external.

The structure of this paper, both theoretical and empirical, elaborates on the relevance of customers for the Macedonian oil retail sector. This paper refers essentially on customer satisfaction associated with the products from two leading oil companies in Macedonia: Makpetrol AD and Lukoil Macedonia. The aim of this paper is to emphasize the level of customer satisfaction in the downstream oil segment in terms of long term loyalty and economic consistency. The analysis of the customer satisfaction will be researched with elaborating and comparing customer satisfaction from oil companies in Macedonia - Makpetrol AD and Lukoil Macedonia – which have equal price and quality. The research is concentrated on the key elements that determine customer satisfaction from Macedonian oil companies. The analysis results indicate that customer's can clearly demonstrate affection toward certain company and concludes the utmost importance of customers' satisfaction for achieving sustainable competitive advantage within the Macedonian oil retail market.

* PhD Student, Faculty of Economics Skopje, Macedonia email:edvin_mushe@yahoo.com

Key words: customer satisfaction, oil industry, oil retail industry

JEL Classification: M10, M30

Introduction

Customer satisfaction has remained as one of the most sensitive topics in scientific research. The increased rivalry on the market and easy access to goods and services has enabled customers to sharpen their preferences by carefully selecting their suppliers. Nowadays, given the wide variety of products and services, customers' options have expanded, automatically making them more prone to change.

The concept of customer satisfaction is designed on the basis of the generally accepted notion that in order for a company to be successful, first it should fully meet its customers' needs. Thus the perception of customers and users of goods and services is critical for the survival of a single market.

Many industries, however, are paying greater attention on customer satisfaction, for several reasons such as increased competition and deregulation. This aspect is particularly applicable when it comes to the oil retail industry. The global character of the oil retail sector is quite competitive due to the practical application of the liberalization and deregulation principles. Consequently, at the global level, the competition within the oil retail sector is extremely intensive. Therefore companies are becoming more customer-centric in order to maintain a large portion of satisfied clients mainly due to the differentiated product lines which largely differ in price and quality. Leading global oil companies such as Exxon Mobil and Royal Dutch Shell pay key attention to customer satisfaction. Their devotion toward customer satisfaction is practically demonstrated by specialized customer focused program tailored to primarily fit consumer preferences. On the Macedonian oil retail market there are companies who have started to grasp the essence of customer satisfaction. However, this process is quite slow mainly due to the fact that Macedonian oil retail companies still perceive its products from a mass marketing perspective – solely as a commodity – thus neglecting the indistinguishable nature of oil as a product and its unique and complex composition as a means to sustain long term customer satisfaction.

This paper initially identifies the factors that influence customer satisfaction, followed by an analysis of customer satisfaction of the two leading oil retail companies in Macedonia. In the end, from the aspect of increasing customer satisfaction, further directions are provided in order to intensify future discussion concerning improving customer satisfaction in the oil retail industry in Macedonia.

1. FACTORS INFLUENCING CUSTOMER SATISFCATION

In highly competitive economies, it is imperative for companies to be consumer – oriented. Companies are obliged to design quality products and services which in turn will generate satisfied and loyal customers. Decades ago, customer satisfaction was a primary goal of each company on the market generally due to the strong consistent effect of which customer satisfaction has on the retention of key customers and boosting market share¹. In essence, customer satisfaction is influenced on number of factors which may be categorized differently:²

- Employees – where employees satisfaction determines the quality of services and has a vital role in the delivery of value to customers;
- Product quality – which influence the way customers perceive product attributes;
- Corporate image – which indicates the quality of accumulated multiple experience of customers in the context of emotional and functional characteristics of the product;
- Service quality – which affects the satisfaction and loyalty of customers thus generating greater income for companies;
- Accessibility – which refers on the network of general facilities, geographical positioning of retail facilities, and basic accessibility of customers to retail facilities.

¹ Hansemark, O., Albinson, M.:”Customer satisfaction and retention: the experience of individual employees”, *Managing Service Quality: An International Journal*(2004), 14 (1), pp. 40-57.

² Mihelis, G., Grigoroudis, E., Siskos, Y., Politis, Y., Malandrakis, Y.:”Customer satisfaction measurement in the private bank sector”, *European Journal of Operational Research* (2001), 130 (2), p.6.

It is significant that these dimensions cannot be seen from an independent aspect. Customer satisfaction is an element which encompasses a large segment of each of the elemental factors which in fact drive the level of customer satisfaction. Customers are more aware of what they purchase and once they feel unsatisfied they will instantly switch to rival companies. The customer is the only one who can determine the value of the product which he forms under the influence of various internal and external factors. The current value of a product is not only an expression of the required quality but the overall experience that the customer has when consuming certain products and services.

Nowadays, companies are aware that satisfied customer worth fortune on a long term. Satisfied customers provide recommendation to other potential buyers, repeat purchase, and are willing to pay additional amount for cooperation with a company they believe in. Every company that wants to position its self adequately and be competitive has to create a unique marketing strategy that will provide customers with a highest form of satisfaction. So far, scientific research, especially longitudinal³, has indicated that satisfied customers tend to be more loyal to a certain brand, which in turn affects revenue growth, reduces costs and price sensitivity.

2. MEASURING CUSTOMER SATISFACTION

Modern marketing philosophy is determined by customer satisfaction as a fundamental and most measurable standard for quality performance of companies. In this context, studies which are related with the measurement of customer satisfaction are based on the same basic principle: to evaluate the products and services of the company in terms of how they are perceived by consumers⁴. Recent studies⁵ have shown that modern companies that practice consumer – oriented strategies to better

³ Cooil, B., Keiningham T., Aksoy, L., Hsu, M.: “A Longitudinal Analysis of Customer Satisfaction and share of Wallet: Investigating the Moderating Effect of Customer Characteristics” *Journal Of Marketing* (2007) 71 (1): 67-83.

⁴ Cengiz, E.: Measuring customer satisfaction: must or not? *Journal of Naval Science and Engineering*, (2010) 6 (2): 76-88.

⁵ Ishaq, M., Bhutta, M., Hamayun, A., Danish, R., Hussain, N.: “Role of Corporate Image Product Quality and Customer Value in Customer Loyalty: Intervening Effect of Customer Satisfaction”, *Journal of Basic and Applied Scientific Research*, (2014) 4 (4): 89-97.

meet customers' needs indirectly comprehend the need to develop an advanced system for measuring customer satisfaction.

In order to achieve long term success on the market, it is crucial for companies to continuously monitor the level of customer satisfaction in the context of their product line and services on the market. Hence, companies will generate better insight concerning current level of customer satisfaction and use those findings to improve future strategic plans. In measuring customer satisfaction, companies are initially obliged to define which segment will be specifically evaluated, whether customer satisfaction will be examined from the perspective of products and services and which methodological approach will be most compatible in order to respond appropriately on the research objective. However, before companies start with the implementation of any system for measuring customer satisfaction, they have to essentially identify the characteristics of its customers. Therefore, measuring customer satisfaction is considered as an inevitable element for increasing customer satisfaction and thus it should be a continuous process that is carried out regularly. Understanding customer preferences can help companies to improve its business decisions and ultimately build competitive advantage over other rivals on the market.

3. OIL RETAIL SECTOR IN THE REPUBLIC OF MACEDONIA

Unlike the complex structure of the global oil market and extremely strong competition, the retail oil sector in Republic of Macedonia, which was and still is a subject to continuous transformation, lies to incomparably more static platform in terms of participation and intensity of competition. In essence, the sector of oil derivatives in Macedonia includes the following activities⁶: import and export of crude oil and oil products, crude oil production, bio fuel production, and distribution and sales of oil products. Therefore, it is important to distinguish that by its structure, Macedonian oil companies are horizontally integrated and they only participate in one segment – refining and distribution of oil derivatives, where the volume of competitive activities is the largest. Key companies that emerge as leaders in terms of refining, distribution and sales of oil products in Republic of Macedonia are: refinery OKTA AD, Makpetrol AD and Lukoil Macedonia.

⁶ MANU: "Strategy for energy development in Republic of Macedonia for the period 2008-2020 with vision to 2030" Macedonian Academy of Sciences and Arts (2009), p.44

Refinery OKTA which is also the largest and only refinery in Macedonia, from 1999 is owned by a private strategic investor from Greece E.L.P.E.T. Balkanika. The product lines of Makpetrol and Lukoil are slightly different, especially in terms of benefits for customers.

Table 1: Type of fuels of Makpetrol AD and Lukoil Macedonia

Makpetrol AD	Type of fuel	Lukoil Macedonia	Type of fuel
<i>Ultra 95 + Economy (Euro Super 95)</i>	Gasoline	<i>EKTO Sport (Euro Super 98)</i>	Gasoline
<i>Ultra 100 Race Pro (Euro Super 100)</i>	Gasoline	<i>EKTO Plus (Euro Super 95)</i>	Gasoline
<i>Ultra Diesel Power Jet (Euro Diesel EC)</i>	Diesel	<i>EKTO Diesel (Euro Diesel BS)</i>	Diesel
<i>Ultra Diesel Bio Jet (Bio Diesel B6 EC)</i>	Diesel	<i>LPG</i>	Liquefied Petroleum Gas
<i>Ultra LPG</i>	Liquefied Petroleum Gas		

Source: Macedonian Academy of Sciences and Arts: “Strategy for Energy Development in Republic of Macedonia for the period 2008-2020 with vision to 2030” (2009), p.44.

Table 1 indicates the type of fuels offered by the two companies on the market. In its production program, Makpetrol offers high quality fuels produced by cutting edge technology and designed according to the highest European and world standards. The advantage of these fuels is reflected in the fact that they were designed with aim to produce more power and lower costs for customers and lower emission of gas. On this way, Makpetrol’s management created double value for customers – more economical fuels which are positioned in line with those of the competition

and environmental protection. Viewed from a marketing perspective, for the same price, customers receive high quality fuels which improve the relative performance of their vehicles. In a similar way as Makpetrol, the product line of Lukoil is primarily designed to provide customers with a product that not only meets the basic energy needs of customers but also it is conceptually and chemically structured based on the highest environmental standards. The supply of oil as a commodity product is no longer considered sufficient to satisfy customers' needs. Integration of quality is vital in order to enhance the supply of oil and to distinguish the fundamental advantages of the key rivals on the market.

4. RESEARCH

The main objective of the research is to analyze customers' satisfaction from the products and services of the two leading oil distributors in Macedonia. The descriptive method, along with all its modalities, will have a central role in the research which means the research will include analyzing, comparing, and generalization.

For the purpose of adequately responding to the research question, the research is conducted by using a structured questionnaire on the sample of oil consumers and its satisfaction from the oil companies. The main research problem is about how much Macedonian consumers are satisfied or dissatisfied with the products of Makpetrol AD and Lukoil Makedonija. The results from the research are obtained on a sample of 300 respondents and data is obtained by using the electronic tool for research and statistical processing of data Survey Monkey. Thus, this research incorporates the following phases: collecting data, grouping and displaying data, and analysis and conclusion. The questionnaire was distributed electronically in Skopje by using email and social media networks. The questionnaire included respondents from different age, sex, and education level. In the sample, 300 respondents from Skopje are included, from which 57% are man and 43% are woman. More than half of all respondents (68%) are with higher education whereas 28% are with high school education.

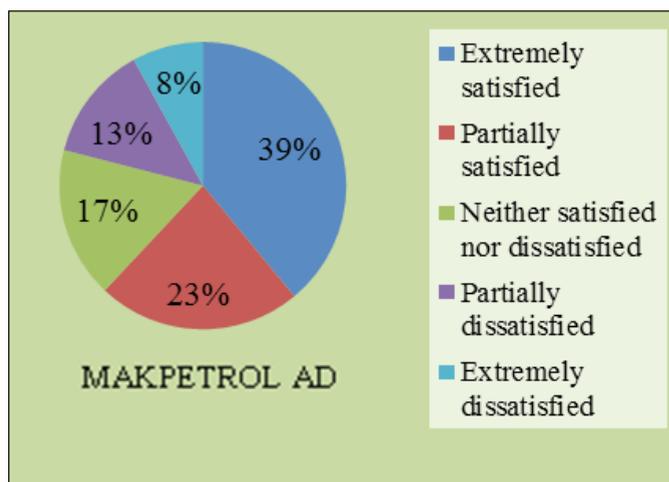
The questions within the questionnaire are defined to primarily generate information from the respondents about the quality of fuel and oil derivatives in general, and customers' preference toward certain product or company. The research was conducted in July 2015. The content of the

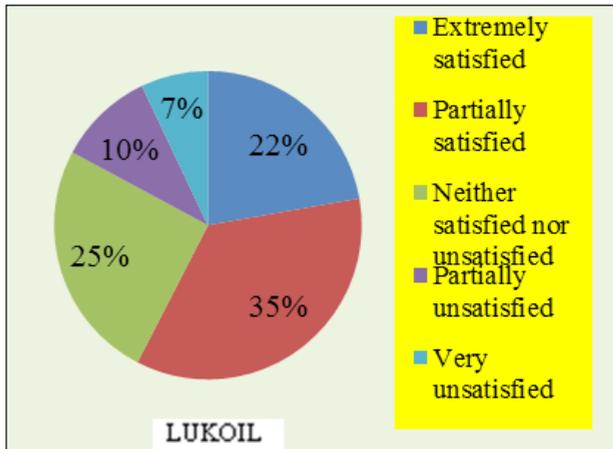
questionnaire consists of 10 questions divided in three main parts. First, all the questions are structured with a multiple choice answer whereas the initial part is designed to evaluate, from a general aspect, the satisfaction of customers from the products and services of Makpetrol and Lukoil Makedonija. Second, in the middle part of the questionnaire, the focus is put on the value that customers generate from the products and services of the two companies or the degree of preference which consumers demonstrate toward the two brands. The third part of the questionnaire is designed to determine how likely satisfied customers are willing to buy a product again from the two companies and how likely customer will recommend these two companies to their friends and family.

5. RESULTS ANALYSIS

Based on the research results, respondents were overall more satisfied from the products and services of the retail oil distributor Makpetrol AD. Hence, only those results from the questions considered significant for the research objective are presented. Both results from the questionnaire for Makpetrol AD and Lukoil are presented simultaneously. Concerning the question: *Overall, how satisfied/unsatisfied are you with our company?*, the following results were received:

Chart 1: Overall customer satisfaction of oil companies in Macedonia



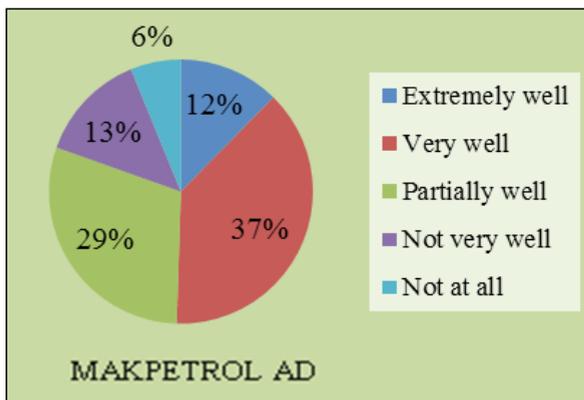


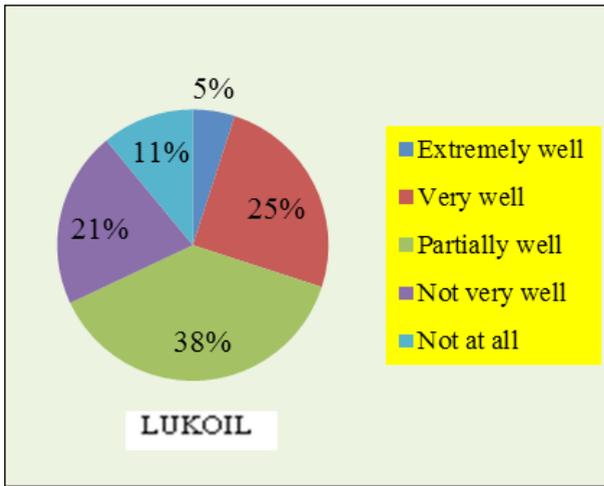
Source: Authors' research

As displayed on Chart 1, the answers indicate that 39% of the respondents are satisfied with the oil company Makpetrol AD and only 22% of the respondents were extremely satisfied with the oil company Lukoil Macedonia.

Regarding the question: *How well our products satisfied your needs?*, Chart 2 indicates that 12% of the respondents were extremely satisfied with Makpetrol products, and 5% percent of respondents were extremely satisfied with Lukoil products. These results indicated that consumers are more satisfied with the products of Makpetrol. Thus from the answers given we can conclude that consumers generally prefer to use the products of Makpetrol.

Chart 2: Customer satisfaction from oil products in Macedonia

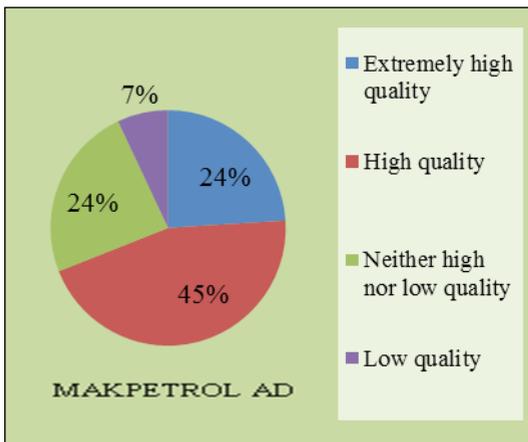


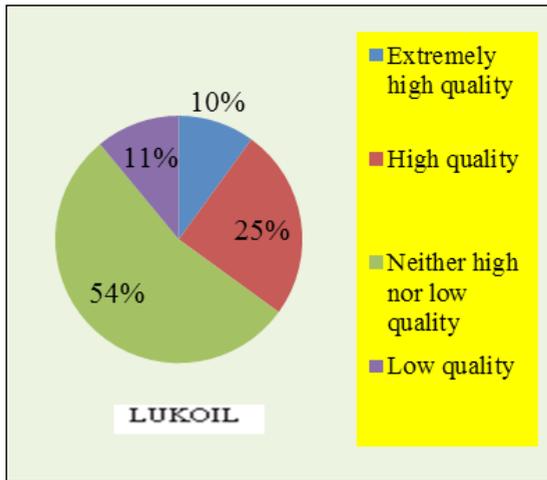


Source: Authors' research

Regarding the question: *How would you assess the quality of our products?*, Chart 3 indicates that 24% of the respondents consider Makpetrol products are with extremely high quality whereas 10% considered Lukoil products with high quality. From the given results presented in Chart 2, we can conclude that respondents consider that Makpetrol products are with better quality. Respondents' perceptions are primarily based on the longer experience that they had with this company, considering the fact that Makpetrol is one of the biggest and oldest oil distributors in Republic of Macedonia.

Chart 3: Quality of oil products in Republic of Macedonia

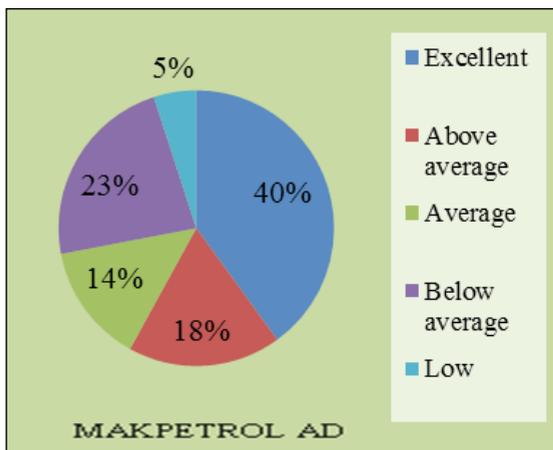


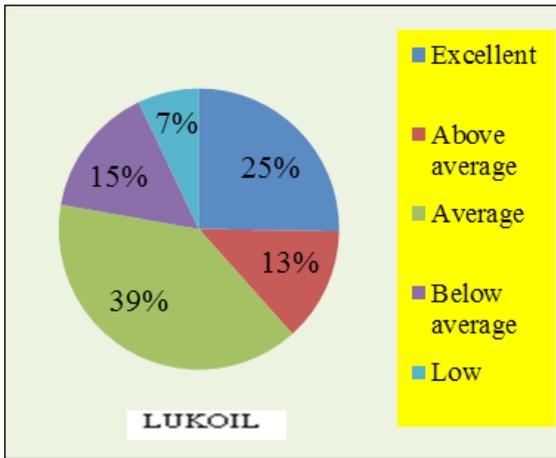


Source: Authors' research

Regarding the question: *How would you rate the 'value for money' of our products?*, Chart 4 indicates that the majority of the respondents or 40% rated Makpetrol's value for money as excellent and only 7% of the respondents considered Lukoil's value for money as excellent. This data indicates that customers, when making a purchase, generate more value for money – customers receive more efficiency and effectiveness of the purchase itself.

Chart 4: The value for money customers receive during purchase

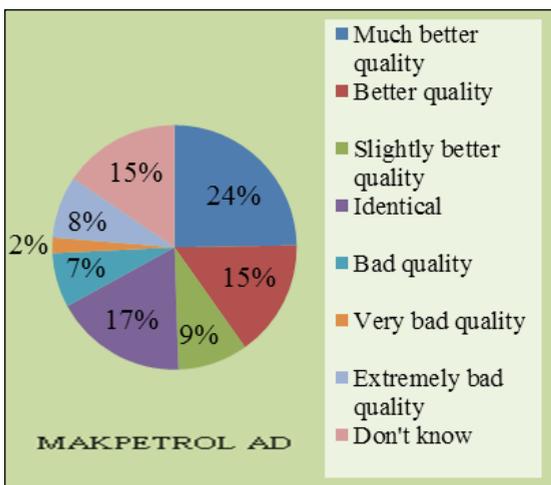


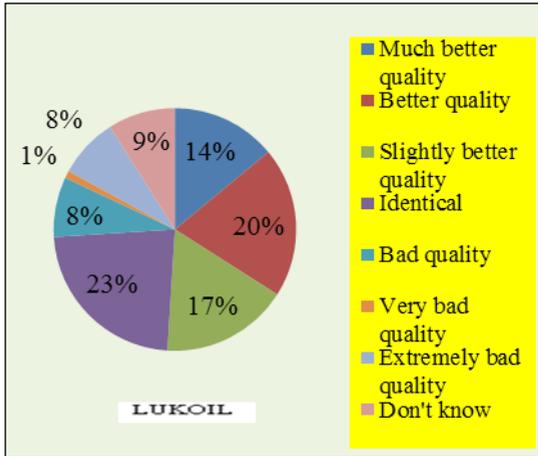


Source: Authors' research

Regarding the question: *Compared to our competitors, are our products with better quality, identical or worse?*, Chart 5 indicates that the majority of the respondents or 24% answered that Makpetrol products are with much better quality and 14% of the respondents considered Lukoil products with much better quality. This data indicated that customer have more faith in Makpetrol products mainly due to the advanced composition of its product line (advanced fuels with high octane composition).

Chart 5: Customers' perception about competitive products

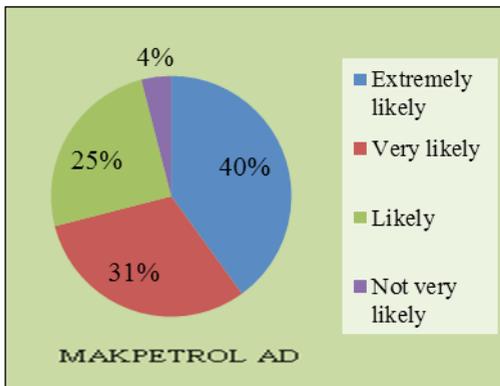


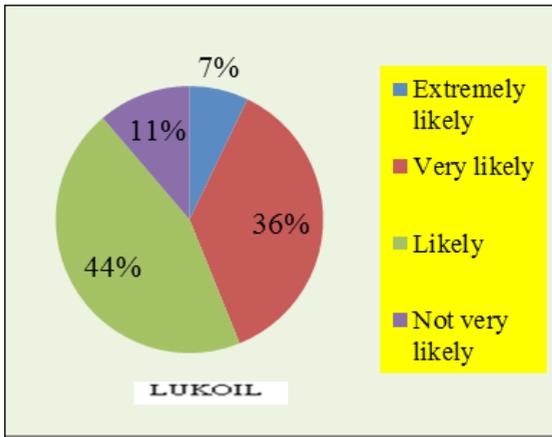


Source: Authors' research

Regarding the question: *How likely are you to purchase any of our products again?*, Chart 6 indicates that 14% of the respondents answered that they will extremely likely buy Makpetrol's products again and 7% of the respondents answered that they will extremely likely buy Lukoil products. The results indicate that customers tend to demonstrate repeated purchasing toward Makpetrol products as well as strong brand loyalty.

Chart 6: Customers recommendation

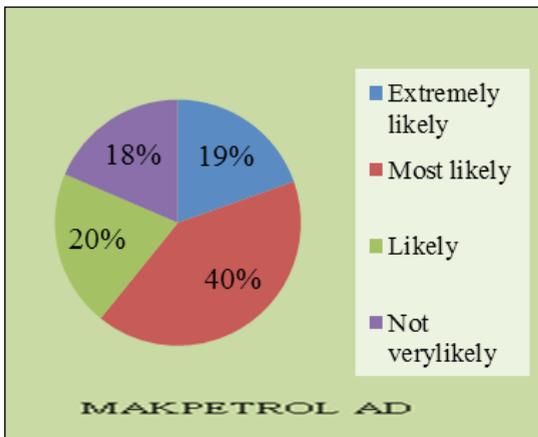


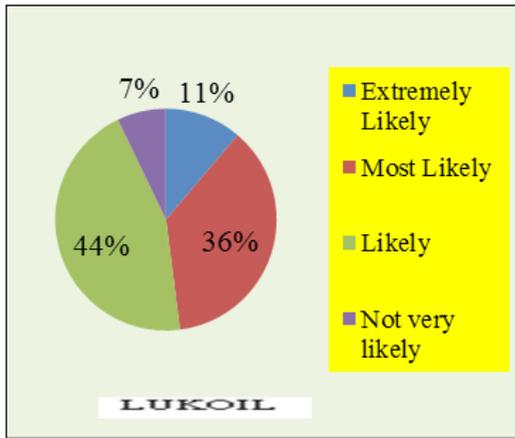


Source: Authors' research

Regarding the question: *How likely would you recommend our company to your friends and family?*, Chart 7 indicates that 40% of the respondents will extremely likely recommend Makpetrol to their friends and family and only 7% answered that they will extremely likely recommend Lukoil to their friends and family. The results clearly indicated that customers overall satisfaction is much higher with Makpetrol which in turn generates repeated buying and positive word of mouth.

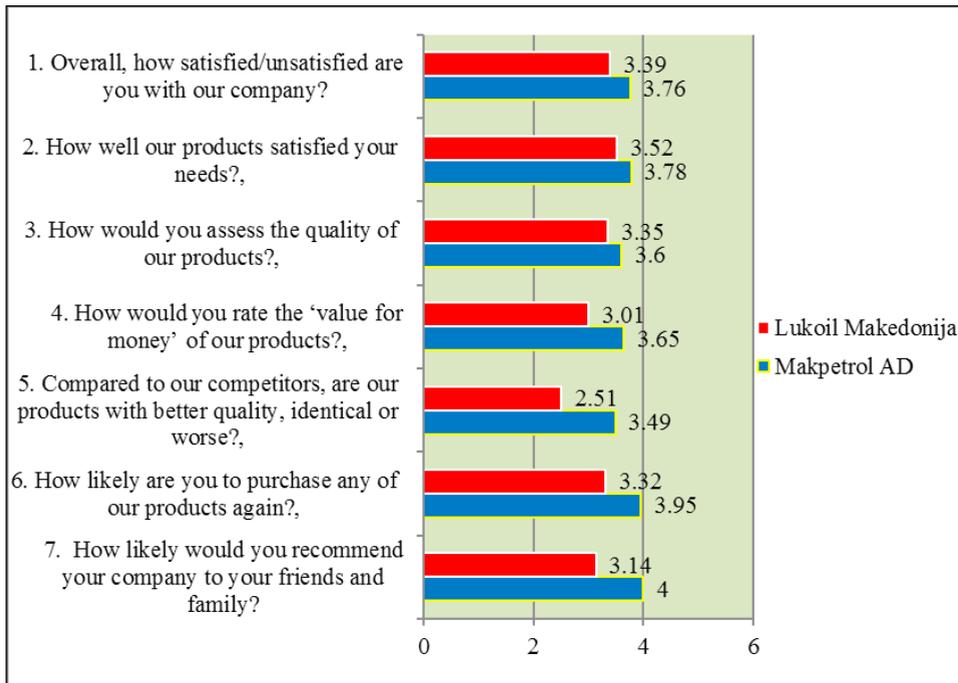
Chart 7: Customers degree of recommendation





Source: Authors' research

Chart 8: Comparing answers for Makpetrol and Lukoil based on the average value of each questions

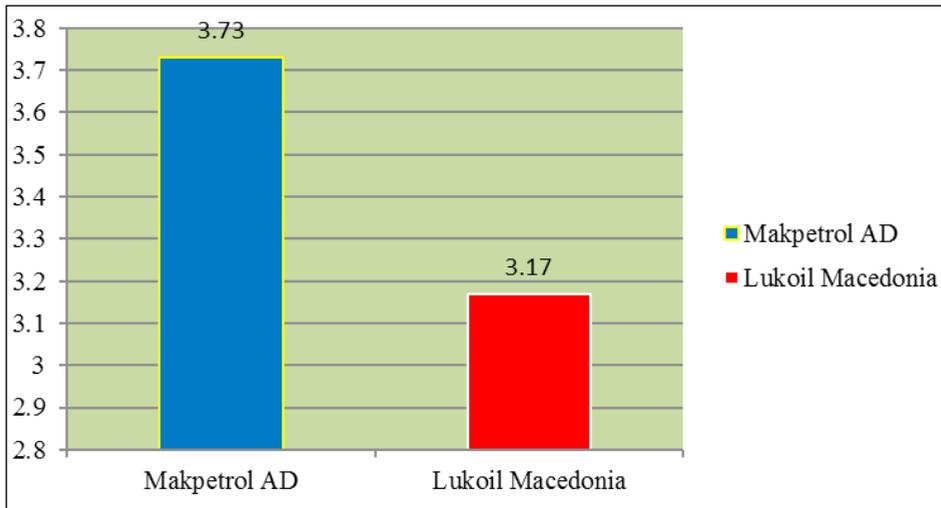


Source: Authors' research

Chart 8 indicates the average value of responses in terms of the total number of respondents. Responses are ranked on Likert scale from 1 (very dissatisfied) to 5 (very satisfied). When viewed from a comparative aspect, customer satisfaction from the two companies is relatively different. Regarding the first question - Overall, how satisfied/dissatisfied are you with our company? - Customers are overall more satisfied (3.76) with the company Makpetrol. On the other hand, customers are neutral (3.39) or neither satisfied nor unsatisfied from the company Lukoil. The second question - How well our products satisfied your needs?-revealed that Makpetrol products meet customers' needs very well (3.78) while the products of Lukoil partially satisfied (3.52) the needs of customers. The third question - How would you assess the quality of our products? – indicated that Makpetrol products are with high quality (3.6) while the products of Lukoil are neither with high nor with low quality (3.35). The fourth question - How would you rate the 'value for money' of our products? – revealed that Makpetrol value for money is above average (3.65). On the other hand, respondents rated Lukoil value for money as average (3.01). Regarding the fifth question - Compared to our competitors, are our products with better quality, identical or worse? – Respondents rated Makpetrol products with better quality (3.49) while the products of Lukoil were evaluated as identical (2.51). The sixth question - How likely are you to purchase any of our products again? – Majority of the respondents answered that they will very likely (3.95) re-buy products from Makpetrol while other respondents answered that they will not likely re-buy the products of Lukoil. Lastly, the seventh question - How likely would recommend our company to your friends and family? – indicated that the majority of the respondents will very likely (4) recommend Makpetrol to their friends and family and on the other hand, they will likely (3.14) recommend the company Lukoil to their friends and family.

The average value displayed on Chart 9 indicates the sum of all questions which reveals customers overall satisfaction from both companies.

Chart 9: Overall customer satisfaction from Makpetrol and Lukoil



Source: Authors' research

Conclusion

The research results have projected an evident difference of customer satisfaction among two biggest oil distributors in Republic of Macedonia, According to the research results, customers are generally more satisfied with the products of Makpetrol AD, due to its differentiated and quality products, higher value for money and positive rate of future recommendation. This confirms our previous theoretical discussion which proclaimed that the more customers are satisfied with a particular product the greater the chances to increase the number of repeated purchase or to transfer their positive experience to their friends. Also, the research results revealed that customers are more satisfied with the company Makpetrol AD, primarily due to the better adaptation of the company itself to its domestic consumers as well as multi practice in terms of the daily satisfaction of their needs and wants. On the other hand, lower customer satisfaction from Lukoil Macedonia is maybe a result from the emphasized global standardization of marketing activities and strategy in general, which in essence is risky and not always productive when entering new markets. If a company knowingly disregards these elements, it is more than likely that customers

will switch to competitive products which are willing to adapt its program and overall marketing efforts in order to adequately respond to the needs of local customers.

Customer satisfaction in the Macedonian retail oil sector is certainly an issue on which a significantly greater attention should be given in future. In commodity industries, customers are those which determine companies' profitability, hence understanding of customer preferences is essential for future growth oil companies in Republic of Macedonia.

References:

1. Cengiz, E.: Measuring customer satisfaction: must or not? *Journal of Naval Science and Engineering*, Vol.6, No.2, 2010, pp. 76-88.
2. Cooil, B., Keiningham T., Aksoy, L., Hsu, M.: "A Longitudinal Analysis of Customer Satisfaction and share of Wallet: Investigating the Moderating Effect of Customer Characteristics" *Journal Of Marketing* (2007) 71 (1): 67-83.
3. Hanselmark, O. and Albinson, M.: "Customer satisfaction and retention: the experience of individual employees", *Managing service quality: An international journal*, Vol. 14, No.1, 2004, pp. 40-57.
4. Ishaq, M., Bhutta, M., Hamayun, A., Danish, R., Hussain, N.: "Role of Corporate Image Product Quality and Customer Value in Customer Loyalty: Intervening Effect of Customer Satisfaction"
5. Mihelis, G. e.tc: "Customer satisfaction measurement in the private bank sector, *European Journal of Operational Research*, Vol.130, No.2, 2001, p.6.
6. MANU: "Strategy for energy development in Republic of Macedonia for the period 2008-2020 with vision to 2030" *Macedonian Academy of Sciences and Arts* (2009), p.44

UDC 336.714:336.763(100)
338.124.7:[336.714:336.763(100)
Professional paper

TOME NENOVSKI*
JADRANKA MRSIK**
SIMONA TRPOVSKA***

**A FRAUDULENT BEHAVIOR OF INVESTMENT BANKING
AS ONE OF THE REASONS FOR THE APPEARANCE OF 2008
WORLD ECONOMIC CRISES**

Abstract

This paper is focused on investment banking and analyzes specific cases from the past which had major impact on the crises with an aim to find possible solutions to eliminate the existing weaknesses in the finance and investments sectors.

Due to the lack of control and supervision, during the last two decades the investment banks exercised enormous freedom and were profit oriented taking highly risky trades and investments. These actions put them into a very difficult financial situation which did affect the whole world economy. The root of that is the amendment of the U.S. Glass - Steagall act (1999) which allowed intermingling of investment and commercial activities, the holes in the international standards and the introduction of two new products on the market: securitization and derivative trading. The trading with derivatives expanded the crises worldwide, turning the US collapse into international collapse. The crises took massive measures and drew the entire world economy into financial crises and the biggest recession in the history.

Key words: Investment banks, financial crisis, securitization, financial derivatives, financial regulation

* Prof., Ph.D, University American College Skopje, e-mail: nenovski@uacs.edu.mk

** Assoc.Prof., Ph.D, University American College Skopje, e-mail:jadranka.mrsik@uacs.edu.mk

*** MBA, e-mail: simona_369@hotmail.com

JEL classification: G01 Financial Crises; G24 Investment Banking

Introduction

The importance of investment banks in the world stage has significantly increased compared to their beginnings and expanded their activities.

All of investment bank's activities contain certain type of risk. Investment banks have to deal with business, investment, operational, market, legal and compliance risk. To be able to manage the risks and to prevent fraud, many regulatory bodies take different measures to ensure that work is done in accordance with specified rules and regulation. But, different regulations apply to different banking systems.

Special part of the paper is dedicated to the securitization and derivatives as the major causes of the crisis. This topic will be examined through the analysis of two case studies: Lehman Brothers and Golden Sachs. These are ones of the main major players in the US housing crisis and therefore, this research will assess their influence on the crises and based on that.

Subsequently, the main question that arises here is whether commercial and investment banks need to function separately and if yes, why!? Thus, in order for one to be able to understand the development of the 2008 crises, this study has to address this question.

1. THE ROLE OF INVESTMENT BANKS

Investment banks facilitate the flows of funds and the allocation of capital between those who are in need of capital and those who have money at their disposal to invest. Moreover, investment banks serve as intermediaries between the two parties, make the market and regulate the price during the transaction. Investment banks operate with high level of capital and large scale investments. Moreover, as Liaw (2012) and Morrison et al (2008) illustrate, they engage themselves in trading with shares warrants, bonds, capital notes and derivatives. They assist companies to go public and they participate in transactional banking internationally.

Investment banks provide various services: Public offering of debt and equity securities, private placement of debt and equity securi-

ties, Mergers and acquisitions, Financial advisory, Fairness options, Structured finance (securitization), Risk management, Merchant banking, Public trading of securities, Trading with derivatives, Wealth management, Other investments (private equity, real estates, international investment), Government financing, Underwriting debt and equity securities etc.

One can notice that each of investment banking activities encounters different level of risk and therefore, the profit for the investment bank for the allocation of capital and the settling of the price in these transactions varies.

2. SIGNS OF WEAKNESSES IN THE BANKING INDUSTRY AND FINANCIAL COLLAPSE

After the removal of the separation of Investment and Commercial banks in 1999, the control over the investment banks was much more difficult. Due the different nature of the two types of banking system, the regulatory bodies were not able to properly asses the working of the banks. Mayer (2009) point out that the level of risk toleration is totally different for the both banking systems. Subsequently, the functioning of the systems as well as the profile of the customers was totally different.

The big banks were the leading banks and therefore, their failure to comply with the rules and regulations imposed by the regulatory bodies created greater and greater tension in the society.

Given the fact that the investment banks tolerate higher level of risk, the commercial banks had very big liberalization in their way of working. Mayer (2009) points out that the big banks started giving easy housing loans to clients by using mortgage securities and collateralized debt obligations. In addition, private agencies started giving loans with mortgage securitization. As the prices of the houses begun to rise, more and more people demanded the housing mortgages in the USA. The banks and private loaners were giving credits without any control

The rising prices of the houses attracted investors to invest in the US housing business. The investors also acted through the big US banks as they were both, commercial and investment banks. Mayer (2009) points out that the rating agencies were pumping up the prices even more by giving very bias valuations and a housing bubble was created, that reached the peak in 2004. The asset prices began to fall rapidly. The investors started

losing huge amounts of money. Moreover, as the prices went down, the people were not liquid enough to repay their debts and the banking system started to become very fragile.

In 2007-2008 the credit markets collapsed turning into bankrupt hundreds of mortgage lenders. The investment banks and hedge funds were encountering losses, as well and trying to cover the losses they entered into borrowings which expanded the bubble.

3. SECURITIZATION, AN ACTION FOR FINANCIAL STRENGTH OR WEAKNESS?

Another reason for the outburst of the crises was the process of securitization. The aim of the system of the securitization was to protect the financial markets of potential crises. However, things went out of control and the system which was aimed to protect the US financial market took other direction. As the prices rose, there were more and more investors and more and more borrowers present on the market. However, what was failed to be taken in consideration, as the Federal Deposit Insurance Commission (2007) explains, is the fact that:

- the shadow market was also developing in parallel with the official financial market
- the credit ratings that the issuers performed were inaccurate
- the mixture of investment banking and commercial banking made it difficult for regulators to assess the lenders and the issuers which resulted with decreased regulation.
- the different kind of existing risks were not adequately calculated

Subsequently, when the bubble exploded, both the commercial and the investment banks were stacked in the middle. Mian and Sufi (2009) and the Federal Deposit Insurance Commission (2007) emphasize that the borrowers were not liquid to repay the debt and the investors were losing money. The securitization took the opposite direction and lead the financial market to a collapse because the two types of banking systems were involved in the same process, so there was no way to assist one another in a period of crises. Both, commercial and investment banks have different

activities and if they wouldn't work jointly in the securitization, one of them could have acted to help the other one and prevent financial disaster. However, as the prices started dropping the entire population was in panic and everyone was trying to save oneself, which at the end led to disaster.

4. DERIVATIVES, A NEW OPPORTUNITY, OR A TOOL FOR DISASTER?

During the housing bubble, the US banks favored trading with futures. Every market transaction has three components, trading, clearing and settlement. In a future transaction, as Mian and Sufi (2009) point out, the trading and clearing happens immediately, but the settlement will only occur at a specific future date. When the future matures, an exchange of the underlying asset should take place. However, the buyers of the future usually close the position before its maturity date and new future contract is concluded.

Mian and Sufi (2009) explain that the US banks used, the real estates as underlying asset of the futures, selling (short position) or buying (long position) them. Investors from all around the world started investing in futures expecting the prices of the real estate to rise. Closing the positions before their maturity and trading them further, they expanded the trading on global levels.

The prices of the real estate properties were constantly rising and the rating agencies were giving favorable valuations. Given the poor work of the rating agencies the prices of the real estates were artificially pumped up. Subsequently, when the bubble exploded, the prices of the real estates started dropping and panic among traders and investors arose. Every person that held a future wanted to sell it as soon as possible which pushed the prices of the real estates even more down.

Given the fact that the futures were transferred from one person to another on a global scale, the US crises expanded internationally and affected the world economy.

Consequently, the process of securitization, the trading of derivatives, the intermingling of the investment and commercial banking systems and the poor regulatory standards and the rating agencies played a major role in the US recession and economic crises and its expansion worldwide.

5. CASE OVERVIEW

In this paper we examine the two investment banks: Lehman Brothers and Golden Sachs in order to analyze the connection between investment banking and the economic crises of 2008. The main reason for selecting those two banks are:

- Lehman Brothers is was one of the biggest and strongest investment banks that failed during the housing bubble and as a multinational holding affected the entire world stage.
- Goldman Sachs is one of the rear cases that survive the housing bubble and the crises. Thus, it serves as a good comparison to Lehman Brothers.

How they acted and what preventive measures they have taken and how that influenced the world economy is of crucial importance to finding out the connection between investment banking and the recession of 2008.

5.1. Lehman Brothers

a) Fraudulent management behavior

As Augar and Harper (2008) illustrate the complex structure prevented the regulatory bodies to assess the firm's compliance with the banking rules and regulations and encouraged the management team to use unacceptable accounting practices in order to earn higher profits.

Far away from prudent corporate governance, as Lubben (2011) emphasizes Lehman modified its financial statements with an aim to demonstrate stability to the potential investors and gain their trust. Thus, the management team illustrated a strong financial stability of the company despite of the real situation. Moreover, they used bribery in order to cover its activities. Lubben (2011), Augar and Harper (2008) explain that the auditors doing company's financial statements, employees at Ernst & Young, participated in the fraudulent practices of the company. They violated the Sarbenes-Onexely Act and many other rules aimed at strengthening external auditing in order to disguise their finishing financial statements which later on created accounting scandals.

Another point that brought collapse to the company, as Augar and Harper (2008) portray, was the fact that the management board protected the individual interest over the interest of the company. They brought decision to increase the compensation bonuses of the senior management executives. Their bonuses increased to 480 million dollars which made Lehman's executives, the executives with the highest level of income.

Moreover, the company was crossing its own risk limitations and performing risky transactions just to gain profits. Lubben (2011) points out that the Security Exchange Commission was aware of these practices, however, due to bribery was ignoring the actions taken by the company.

As Augar and Harper portray (2008) that all these activities misrepresented the image of the bank in the public. Subsequently, before its failure there was neither time, nor space to do anything to save the bank.

The internal structure was completely weak, but from the outside it looked very strong. Given the poor work of the regulatory and rating agencies no loopholes could have been found on timely manner and therefore, no bailout strategy could have been developed.

Once the fraudulent behaviour was discovered, the company lost the trust from its collaborators and the public. Consequently, when it had short-term liquidity problems, no one really wanted to offer help to Lehman Brothers, so they had no choice, but to declare bankruptcy.

b) Risk exposure, lack of regulations and complex capital structure

With its too high leveraging Lehman Brothers entered into a signaling level of credit risk. Randall and McGee (2008) state that the allowed leverage level was 60% of its assets, however, the company leveraged over 90% of its assets.

With an aim to expand its business operations, Lehman Brothers took advantage of very risky investments, which expanded the already existing investment risk. According to Murphy (2008) and Kimberly (2011), independent analysts, one of these investments was the acquiring of Residential Mortgage Backed Securities. They state that the financial statements of this company failed to illustrate its objective financial situation: Residential Mortgage Backed Securities accounted for 8.3 billion dollar losses in the process of securitization leading Lehman Brothers closer to bankruptcy.

In addition, as Randall and McGee (2008) portray, Lehman Brothers decided to enter into the derivative market and to engage in speculations in order to decrease their substantial credit risk. However, by taking this step they entered into a trap. Once the prices of the underlying assets started dropping, there was almost no way out. The bank encountered trillions of losses due to a default in collateralized debt obligations.

Nonetheless, the engagement in these highly risky activities could have been stopped and excessive exposure to risk could have been prevented. However, the regulatory bodies lacked regulations and strong structure and therefore, their ability to prevent the crises was limited. In addition, they were not even able to apply most of the existing rules and regulations to Lehman Brothers because their capital structure was very complex and required too many in-depth analyses which gave the company additional freedom of action.

c) The global influence of the Lehman Brothers' collapse

The bankruptcy of Lehman Brothers caused serious economic problems worldwide. The value of the real estates diminished significantly on the real estate market. Farndale (2008) points out that the receivables from the derivatives lost billions of dollars in value. To be exact, 70% of the value of all receivables of Lehman Brothers depreciated. Many hedge funds lost the value, since they relied on Lehman Brothers, as the market leader in the financial world.

Most of the debts of Lehman Brothers were written off. This caused the value of the stocks of many US and foreign companies to drop on the exchange market. Farndale (2008) emphasizes that the derivative trading, the German Banks immediately experienced instability, reporting 500 million euros of financial loss. Blute (2010) states that UK investors experienced 1.5 to 1.8 billion pounds losses. Japanese banks lost more than 2.4 billion yens. Many other countries encountered significant losses which caused shock in their economies.

Consequently, one can notice that the entire world was negatively influenced by collapse of Lehman Brothers. This all could have been prevented if the signals would have been taken in consideration by the management team of the company, the regulatory bodies and the rating agencies.

5.2. Goldman Sachs

a) Fraudulent management behavior

The management team of Golden Sachs made similar steps to the management team of Lehman Brothers. Gordon (2015) emphasizes that they fabricated their financial statements in order to portray a good image about themselves on the market which was totally different of what was happening in reality. The richer the managers were getting, the more instable the holding was.

Goldman Sachs was accused for fraud, misrepresentation, intentionally omitting important facts about financial products. The company was selling mortgage securities created by hedge-fund firm and it was secretly betting in a sharp drop in the housing prices and market collapse . The bank had a power to drive the economy into crisis. These actions made the crisis even more severe and the losses devastating.

b) The influence of Goldman Sachs on 2008 financial crisis and its survival

Goldman Sachs survived the crises of 2008, but the main question to pose here is: how did they manage to do it!?

First of all, the company made enormous profits at the beginning of the crises. As Carney (2009) portrays while selling mortgage securities, the company secretly bet against the housing market. Goldman Sachs was playing double game and with good timing and excellent salesmanship as many external analysts portray, it managed to survive while the market was collapsing. Carney (2009) emphasizes that they managed to find investor who bought preferred stocks with a total value of 5 billion dollars. In addition, the company had close ties with the government given the fact that it was providing the US government with finances during the Second World War. Subsequently, they managed to obtain loan from the Federal Reserves in one day and that help them to overcome the crises.

Despite its survival, Goldman Sachs had also a negative impact on the world economic crises. The double game enabled them to stay in operations, but their clients encountered huge losses. The double game enabled them to stay in operations, but their clients encountered huge losses. Carney (2009) points out that Goldman Sachs sold \$40 billion in mortgage back securities, but omitted to tell the buyers that they are secretly betting that a sharp drop in U.S. housing prices will take place.

6. IS THERE A NEED FOR SEPARATION BETWEEN INVESTMENT AND COMMERCIAL BANKS?

One of the main conclusion of this research is, actually the question: Is there a need for separation between investment and commercial banks?

One of the main causes of the crises was the amendment of the Glass-Steagall Act in 1999 which allowed the bigger banks to function as both commercial and investment banks.

Ross (2015) refers to Mark Thornton, Frank Shostak, Robert Ekelund and Joseph Stiglitz who blame Gramm-Leach-Bliley for making these risky institutions too big to fail. According to Eichengreen (2015) many economists consider the risk toleration level of investment banks as not necessarily higher than the one of commercial banks because both, investment and commercial banks try to minimize risk in order to protect themselves and its clients.

However, despite the contra-argumentation, the history showed that the economy is exposed to greater shifts and problems when the two banking systems function under one roof. Their separation tends to lead to much greater economic stability and smoother flow of money.

Conclusions

Due to lack of control and supervision, the investment companies exercised enormous freedom and were profit oriented taking highly risky trades and investments. The hunger for additional profits encouraged the managers to engage in fraudulent behavior. These actions put them into a very difficult financial situation which did not affect only the financial market, but the entire US and world economy.

The inability of the regulatory body to follow the actions of Lehman Brothers, Golden Sachs and many other multinational corporations clearly illustrates a weakness into the legal system as well as the rules and regulations applicable to the companies from the financial sector.

According to many experts from the field of finance, if all rules and regulations were respected and applied properly, the crises wouldn't have been so severe because the companies would have been able to survive. Though, the gaps in the international standards would have still caused

destabilization in the economy.

From the entire analysis it can be concluded that the biggest world economic crises of 2008 was initiated by the collapse of the mortgage market, the extremely complicated innovative financial instruments, the bankruptcy of the big banks, the lack of rules and regulations in the banking industry and the underperformance of the regulatory bodies.

Given the freedom, instead of being an example on the market, these corporations started engaging into fraudulent behavior and illegal practices. They all fabricated their own financial statements in order to gain the public support and to increase their reputation and value in the society. The rating agencies supported the banks, pumping up their asset-values even more.

Consequently, having an enormous freedom and being preoccupied with profits, they neglected the fact that the situation might get critical. Most of them did not have back up scenario and when the real estate prices started diminishing they started encountering unexpected losses which they were not able to cover.

Everything was happening very fast and there was no space for intervention. The governments had limited funding and they were not able to offer much assistance to the corporations. The trading with derivatives expanded the crises worldwide, turning the US collapse into international collapse. Billions of dollars were lost; the crises took massive measures and drew the entire world economy into financial crises and the biggest recession in the history.

Having all that in mind once again we are coming to the question: Isn't there a need for separation between investment and commercial banks?

References:

1. Augar P. and Harper C., *The Greed Merchants: How Investment Banks Played the Free Market Game*, London, Penguin Group, 2008
2. Carney J. (2009). A “Secret”. *Business Insider*, 2009, Retrieved from: <http://www.businessinsider.com/sorry-folks-goldman-sachs-was-not-secretly-short-housing-during-the-bubble-2009-11>, (15 June 2016).
3. D’Arcy,C.(2009). Why Lehman Brothers collapsed? Retrieved from: <http://www.lovemoney.com/news/theeconomy-politics-and-your-job/the-economy/3090/why-lehman-lehman-collapes> (5 June 2016)
4. Eichengreen B. (2015). *Hall of Mirrors: The Great Depression, The Great Recession and the Uses and Misuses of History*. New York: Oxford University Press
5. Farndale N. (2008). *Lehman Brothers Collapse: How the worst economic crisis in living memory began*. *The Telegraph*. Retrieved from: <http://www.telegraph.co.uk/finance/recession/3917584/Lehman-Brothers-collapse-How-the-worst-economic-crisis-in-living-memory-began.html>, (12 June 2016).
6. Federal Deposit Insurance Corporation: *Laws and Regulations* (2014). Available from: <https://www.fdic.gov/regulations/laws/rules/1000-400.html> (1 June 2016).
7. Gordon G. (2009). *How Goldman secretly bet on the U.S. housing crash*. *McClatchy DC*. Retrieved from:
8. <http://www.mcclatchydc.com/news/politics-government/article24561376.html>, (15 June 2016).
9. Liaw T.K. (2012). *The Business of Investment Banking: A Comprehensive Overview*, 3rd ed. New Jersey, John Wiley and Sons Inc.
10. Kimberly, S. (2011). *Misconceptions about Lehman Brothers’ Bankruptcy and the role of derivatives played*. Retrieved from: <http://www.stanfordlawreview.org/online/misconceptions-about-lehman-brothers-bankruptcy> (15 May 2016)
11. Mayer C. (2011). *Housing, Subprime Mortgages, and Securitization: How did we go wrong and what can we learn so this doesn’t happen again?*

12. University of Yale. Retrieved from: http://www.law.yale.edu/documents/pdf/cbl/Housing_Subprime.pdf, (15 June 2016).
13. Murphy, A. (2008). An analysis of the financial crisis of 2008: Causes and solution: Retrieved from: <http://ssrn.com/abstract=1295344> (15.05.2016)
14. A. and Sufi A.(2009). House of Debt: How They (and You) Caused the Great Recession, and How We Can Prevent It from Happening Again. Chicago, The University of Chicago Press.
15. Morrison, A, D. And Wilhelm W.J. Jr. (2008). *Investment Banking: Institutions, Politics and Law*, London: Oxford University Press.
16. Randall T. and Mc Gee J. (2008). Wall Street Executives Made \$3 Billion Before Crisis. Bloomberg. Retrieved from: <http://baltimorenonviolencecenter.blogspot.mk/2008/09/wall-street-executives-made-3-billion.html> (15 May 2016)
17. Ross S. (2015, March, 27). Should commercial and investment banks be legally separated? Retrieved from: <http://www.investopedia.com/ask/answers/032715/should-commercial-and-investment-banks-be-legally-separated.asp> (3 June 2016).
18. Von Ah R. (2015). Derivatives (Forward, Futures, Options and Swaps), Zurich, AZEK. AZEK Inc.

UDC 657.6: 339.727.22(4-672 EU:497.7)
339.727.22(4-672 EU:497.7)
Professional paper

MITE MITEVSKI*

**AUDIT ON THE EU INSTRUMENT FOR PRE-ACCESSION
ASSISTANCE (IPA) – THE CASE OF THE REPUBLIC OF
MACEDONIA**

Abstract

The Instrument for Pre-Accession Assistance - IPA is a very important tool which helps candidate countries pave their way to the accession in the European Union. The benefits of this instrument are twofold: one is the financial aid which is made available and the second is the exchange of knowledge and experience between the institutions of the Member State and the beneficiary country.

The Republic of Macedonia, as a beneficiary of IPA funds since 2007, designed and established a comprehensive system of structures and authorities which are in charge to manage these funds.

Nevertheless, the importance of the national audit structures, external and internal audit authorities or bodies in this system, is not to be underestimated. Their work and opinion is highly valued by the IPA management structures when it comes to providing assurance that the IPA funds are properly used.

Considering its significance in the country, the audit of IPA funds has been chosen to be the main subject of this paper, the purpose of which is to analyze the organizational setup and the responsibilities of the audit structures, as well as to highlight their important role and contribution to good management of IPA funds. Second objective of this paper is to determine the main areas of improvement in performing audit on the IPA funds.

* Ph.D student at the Institute of Economics – Skopje, “University Ss. Cyril and Methodius” Republic of Macedonia, e-mail :mite_mitevski@yahoo.com

Key words: external audit, internal audit, public sector, IPA funds, IPA structures.

JEL classification: F35, M42

Introduction

The main objective of the Instrument for Pre-Accession Assistance (IPA) is to help the candidate and potential candidate countries in their progressive approximation to the standards and policies of the European Union, including the „acquis communautaire”, aimed ultimately at obtaining a legitimate membership in the EU. The IPA is the means by which the EU provides financial and technical support for the reforms in the candidate and potential candidate countries.

The Republic of Macedonia, as a candidate country for the accession to the European Union has been a beneficiary of IPA I (2007-2013) and IPA II (2014-2020) pre-accession funds¹.

IPA I (2007-2013) funds for our country had been budgeted to 619.3 million euros² divided between the following components³:

- o Transition Assistance and Institution Building;
- o Cross-Border Cooperation;
- o Regional Development;
- o Human Resources Development;
- o Rural Development.

IPA II is planned for the period 2014-2020 and amounts to 664.2 million euros⁴ financial aid for the country split into the following sectors⁵:

¹ http://ec.europa.eu/enlargement/instruments/funding-by-country/former-yugoslav-republic-of-macedonia/index_en.htm

² Multi-Annual Indicative Financial Framework (MIFF) for the Instrument of Pre-Accession Assistance (IPA) for 2012-2013

³ COUNCIL REGULATION (EC) No 1085/2006 of 17 July 2006 establishing an Instrument for Pre-Accession Assistance (IPA)

⁴ http://ec.europa.eu/enlargement/instruments/funding-by-country/former-yugoslav-republic-of-macedonia/index_en.htm

⁵ http://ec.europa.eu/enlargement/instruments/funding-by-country/former-yugoslav-republic-of-macedonia/index_en.htm

- o Democracy and governance;
- o Rule of law and fundamental rights;
- o Environment and climate action;
- o Transport;
- o Competitiveness and innovation;
- o Social development;
- o Agriculture and rural development and
- o Regional and territorial cooperation.

With the aim to ensure proper, effective and efficient implementation of the IPA funded projects within the public sector in the country an entire system of management structures and authorities has been established. All parties involved in this organizational structure are expected to provide for a higher degree of absorption of IPA funds and use them in accordance with the accreditation criteria. In the first part of this paper this organizational structure for IPA funds will be presented, thus making a comparison between the IPA I and IPA II instrument.

To ensure a higher level of security for the use of these assets in the country, a system of audit on IPA funds has also been established. The audit functions are shared between the Audit Authority and internal audit units within the beneficiary institutions.

The main role of the audit function is to ensure that the IPA funds are used properly, which is intended to be the main objective of this paper. Therefore we analyse several aspects which contribute to the effectiveness and efficiency of the audit structures, such as their proper organizational setup, their procedures, activities, and using of their outcomes.

1. IPA MANAGEMENT STRUCTURES AND AUTHORITIES IN REPUBLIC OF MACEDONIA

IPA management structures and authorities in the Republic of Macedonia were established in 2007. During the acquisition of accreditation and conferral of management powers under decentralised management of IPA I funds, and in the period of preparation for indirect management of IPA II, a number of relevant bodies were integrated into the organizational

structures of the public sector. The table below presents the IPA structures and authorities and their general responsibilities.

Table 1. IPA Management structures and authorities in The Republic of Macedonia

Structures and authorities	General responsibilities	IPA I	IPA II
The Competent Accrediting Officer (CAO)	The CAO is responsible for issuing, monitoring and suspending or withdrawing the accreditation of the NAO.	Applicable	Not applicable
The National IPA Coordinator (NIPAC)	NIPAC shall ensure the overall coordination of assistance under IPA.	Applicable	Applicable
The Strategic Co-ordinator*	The Strategic Co-ordinator shall ensure the co-ordination of the Regional Development Component and Human Resources Development Component under the responsibility of the NIPAC.	Applicable	Not applicable

* Only for III and IV Component IPA I

The National Authorising Officer (NAO)		<ul style="list-style-type: none"> - Bearing overall responsibility for the financial management of EU funds and responsible for the legality and regularity of the underlying transactions; - Responsible for the effective functioning of management and control systems under IPA. 	Applicable	Applicable
The National Fund (NF)		<ul style="list-style-type: none"> - Acts as central treasury entity; - In charge of financial management assistance of IPA, under the responsibility of NAO; - In charge of organising the bank accounts, requesting funds from the Commission, authorising the transfer of funds from the Commission to the operating structures or to the final beneficiaries and doing the financial reporting to the Commission. 	Applicable	Partially as part of the management structure
The Management Structure	The National Fund	Same/similar responsibilities with IPA I	Another organizational unit/entity	Applicable
	NAO support office	Generally assists the NAO in providing assurance for effective functioning of management and control systems under IPA		

The Operating Structures (including, units for internal audit of the beneficiary institutions and the Ministry of Finance)	The Central Financing and Contracting Department ^{2*} (CFCD)	Responsible for managing and implementing IPA programmes in accordance with the principle of sound financial management	Applicable	Applicable
	Beneficiary institutions **			
	The Managing Authority ^{3*4*5*}			
	The IPARD Agency***			
The Audit Authority	Generally responsible for verification of the effectiveness and sound functioning of management and control systems	Applicable	Applicable	

Source: Based on data from the Framework Agreements between the Republic of Macedonia and the European Commission for IPA I and IPA II

IPA funds authorities, such as the CAO, NIPAC and NAO are generally high-ranking officials in the Government or the state administration of the Beneficiary. The Deputy Prime Minister for European Affairs has been appointed to be the NIPAC in our country. NAO is a high-ranking of-

** For I- IV Components IPA I

*** For V Component IPA I and for Rural development programs under the policy area agriculture and rural development

ficial in the Ministry of Finance. Each of these authorities have their own support offices in their respective institutions.

Other IPA structures consist of separate institutions, or departments within the beneficiary institutions, or working groups responsible for management of IPA funds and implementation of projects.

Managing and implementing projects financed under IPA is a very responsible and complex process which involves a series of risks.

In order to reduce the risks and ensure a successful implementation of the process, in line with the principle of sound financial management, the governing structures have designed multiple levels of controlling and monitoring activities. These involve various ex-ante and ex-post control mechanisms, as well as monitoring and verification tools.

A significant role within the overall system for verifying the adequacy and regularity of the use of IPA funds is granted to the independent audit bodies, such as the Audit Authority and the Internal Audit Units in the beneficiary institutions.

2. AUDIT ON THE EU INSTRUMENT FOR PRE-ACCESSION ASSISTANCE (IPA) IN THE REPUBLIC OF MACEDONIA

2.1 Audit Authority

According to the Law on Audit on the Instrument for Pre-Accession Assistance⁶, the audit activities on the system for implementation, management and control of the IPA shall be performed by the IPA Audit Authority.

The Audit Authority is a budgetary institution managed by the General IPA Auditor, who is appointed by the Government of the Republic of Macedonia. It is independent from the NIPAC, the NAO, the management structure and the operating structures and is empowered with necessary financial autonomy.

The Audit Authority shall carry out audits on the management and control systems, on actions, transactions and on the annual accounts in line with internationally accepted auditing standards and in accordance with the Audit Strategy.

⁶ Published in the "Official Gazette of the Republic of Macedonia", no.66/2010 with amendments

In line with the provisions of the Framework and Sectoral Agreements and pursuant to the Law on Audit the IPA audit performs:

- o verification of the effective functioning of management and control systems under IPA and
- o verification of the reliability of accounting information submitted by the relevant institutions in the Republic of Macedonia to the European Commission within decentralized management of EU Funds.

Audit activities may concern the performance of activities, examination of procedures, transactions and the like, and are commonly divided in three different types of audit: audit on IPA system (system audit), audit on projects/programmes, (financial audit) and audit on the information technology (IT audit).⁷

The audits are performed according to the Annual Audit Work Plan.

The output of performing these audits is the Annual Audit Activity Report and the Annual Audit Opinion.

The Annual Audit Opinion assesses the effectiveness of the management and control systems under IPA and the compliance with the requirements put forward in different IPA regulations and acts. The opinion may be: Unqualified opinion, Qualified and Adverse opinion.

Also, the Audit Authority, shall submit an Annual Audit Opinion on the accounts and statement of expenditure of IPA I - Component V(I-PARD), submitted by the National Authorizing Officer to the European Commission, covering the previous financial year. This Audit Opinion, along with the Annual Audit Activity Report shall be submitted to both the European Commission and the Competent Accreditation Officer, at the latest by 30th April.

Annual Audit Activity Report, covers: funds used from the Audit Authority, review of all weaknesses detected in the management and control systems or findings on transactions identified during the performed audits compared against the Annual Audit Work Plan.

Annual Audit Opinion alongside the Annual Audit Activity Report shall be submitted to both the European Commission and the CAO, a copy

⁷ Law on audit on Instrument for Pre-Accession Assistance, Published in the "Official Gazette of the Republic of Macedonia", no.66/2010 with amendments, Article 19

of which shall be submitted to the NAO, at the latest by 31st December each year.

NAO is obliged, within 45 days from the receipt of the audit reports, to inform the General IPA Auditor of the Audit Authority on the undertaken measures, in relation to the findings and recommendations.

Therefore it is undisputable to conclude that the role, activities and outputs of the Audit Authority, are very important when it comes to assessing or verifying if projects financed under IPA are professionally and properly managed and implemented.

In order to ensure successful execution of the tasks and responsibilities of this institution, it is necessary to meet the following strategic goals⁸:

- o Maintaining functional independence - Continuously maintaining the functional and operational independence of the Audit Authority in carrying out audit on IPA management and control system, in accordance with the IPA Regulation and Framework Agreement between the Republic of Macedonia and EC.
- o Development of institutional capacities - Permanent maintenance of adequate institutional capacities and their development by providing appropriate funding, technical and human resources as prerequisites for fulfilling the Audit Authority's functions.
- o Ensuring quality of performed audit - Developing and improving the audit procedures according to IPA IR and recognised international standards of INTOSAI and IFAC and follow-up of the effects from conducted audits.
- o Information system and information technology - Setting out and developing information system of the Audit Authority, applying the information technology and its rational and efficient usage in performing the audit.
- o Development of communication system - Setting up a system for

⁸ Development Strategy of the Audit Authority for the period 2012-2014

communication and exchange of information with IPA administrative structures, national and international legal entities and publishing the work of the Audit Authority.

The implementation of these strategic objectives is preconditioned by the provision of the necessary financial resources for the Audit Authority and creating a social climate of awareness on the role and importance of the Audit Authority.

2.2. Internal Audit

In order to be granted the right to independently manage and implement IPA projects, the beneficiary country must make the necessary institutional adjustments and harmonization of the national legislation. According to the accreditation criteria the beneficiary should set up and ensure the functioning of an effective and efficient internal control system. This precondition was successfully fulfilled in our country, which enabled to perform internal audit on the IPA system in the country.

In this direction the beneficiary country should also ensure that regular specific monitoring is carried out by the internal audit, in order to provide the management with independent review of the respective systems.

Pursuant to the Law on Public Internal Financial Control⁹, the Internal Audit Unit shall perform internal audit on the public sector's entities, as well as the spending units, structures, programmes, activities and processes, also including those financed by the EU Funds. The audit shall also be performed on the legal entities and natural persons who use public funds for their operation.

In line with the IPA legal provisions, it is a minimum requirement that the Head of the IPA Unit in the beneficiary institution, submits an Annual Internal Audit Report on the IPA structure and activities within the institution.

NIPAC, NAO, the heads of management and operational structures and the beneficiary institutions should implement the recommendations listed in the Internal Audit Report. NAO and the Head of management structure are continuously informed on the progress of the implementation of the recommendations. The most significant internal audit findings are an

⁹ Published in the "Official Gazette of the Republic of Macedonia", no.90/2009 with amendments

integral part of the Methodology for the preparation of the NAO's Annual Statement of Assurance.

Internal audit on the IPA management structures and authorities is implemented by the following units:

- o Operations of NIPAC office are audited by the Internal Audit Unit of the Secretariat for European Affairs.
- o The Internal Audit Unit of IPA funds within the Internal Audit Department in the Ministry of Finance, yearly performs audit on the National Fund/Management Structure, Central Financing and Contracting Department and the Department for IPA, all structured within the Ministry of Finance. This internal audit unit yearly conducts several audits on these structures. The findings and recommendations which are presented in the reports have a significant impact on the preparation of the NAO's Annual Statement of Assurance. Most of the audits of this unit are audits on the system of internal controls and audits of the regularity of operations (compliance audits).
- o IPA related activities in the beneficiary institutions are audited by the internal audit units of the institution itself.
- o Operations of the Managing Authority are audited by the Internal Audit Unit of the Ministry of Agriculture, Forestry and Water Economy
- o The IPARD Agency has established its own Internal Audit Department.

Guided by the definition and the role of the internal audit, we can conclude that it is of utmost importance for the management to take into consideration the independent and objective opinion of the audit on the management and use of the IPA funds, since this inevitably contributes to establishing an effective and efficient internal control system.

In view of further developing and modernizing the function and the role of the internal audit in our country it is necessary to implement the following strategic objectives¹⁰:

¹⁰ Policy paper for development of public internal financial control in the Republic of Macedonia for the period from 2015 until 2017

- o Strengthening the capacity of internal auditors;
- o Establishing a sustainable system for training and certification of internal auditors and
- o Establishing a model for quality assessment of internal audit.

Conclusion

Fully fledged membership in the European Union is one of the top priorities of the Republic of Macedonia. IPA funds are the "wind in our back" (a stepping stone) on our way to achieving this goal.

Therefore, it is crucial that the financial and technical assistance received from the European Union is managed and implemented in accordance with the principle of sound financial management. To achieve this the country has created a comprehensive structure for management of these funds, which also includes an effective and efficient internal control system.

In order to verify that effective IPA management and control systems have been put in place and that IPA funds are used in compliance with the regulation, the country has also established external and internal bodies for audit on the IPA funds, such as the Audit Authority and the internal audit units.

Audit Authority is an entity which plays a significant role in ensuring proper management and implementation of IPA projects and use of IPA funds. The Annual Audit Activity Report and Annual Audit Opinion, as final annual outputs from performed audits of different types help the European Commission in shaping the overall assessment on the management and implementation of IPA projects in the country.

The role of the internal audit units within the beneficiary institutions is not to be neglected either.

Their activities are crucial in drafting the Methodology for the preparation of the NAO's Annual Statement of Assurance. Last, but not least are the findings of the internal audit which, on the other hand have an impact on the preparation of the Statement of assurance for the overall IPA system by the NAO.

In addition to the abovementioned, this paper also outlines some of the main areas for development of audit on the IPA funds. In this respect we may conclude that the country has taken all the necessary steps and measures to establish a functional audit system for the IPA funds. Never-

theless, like any other, this system has to be continuously promoted and updated. Therefore, in the future attention should be given to continuous improvement of some strategic areas, such as: maintaining the functional independence, developing and strengthening of institutional capacities and developing procedures for ensuring and verifying the quality of the audits.

References:

1. Agreement between the Government of the Republic of Macedonia and the Commission of the European Communities on the rules for co-operation concerning EC-Financial Assistance to the Republic of Macedonia and the implementation of the assistance under Component V (IPARD) of IPA, („Official Gazette of the Republic of Macedonia”, no.165/2008);
2. Council Regulation (EC) No 1085/2006 of 17 July 2006 establishing an Instrument for Pre-Accession Assistance (IPA);
3. Commission Regulation (EC) No 718/2007 of 12 June 2007 implementing Council Regulation (EC) No 1085/2006 establishing an instrument for pre-accession assistance (IPA) with amendments;
4. „Development Strategy of the Audit Authority for the period 2012-2014”, Audit Authority, Skopje, 2012;
5. Decree on Determining Mutual Relations between Bodies and Structures of the Decentralized Management of the First Four Components under the EU Instrument for Pre-Accession Assistance (IPA), („Official Gazette of the Republic of Macedonia”, no.132/2008);
6. Decree on establishing relations of organs and structures within the system of indirect management of the Instrument for Pre-Accession Assistance (IPA II), („Official Gazette of the Republic of Macedonia”, no.54/2016);
7. Framework Agreement between the Government of the Republic of Macedonia and the Commission of the European Communities on the rules for co-operation concerning EC-Financial Assistance to the Republic of Macedonia in the framework of the implementation of the assistance under the IPA, („Official Gazette of the Republic of Macedonia”, no.18/2008);
8. Framework Agreement between the Government of the Republic

- of Macedonia and the Commission of the European Communities on the arrangements for implementation of Union Financial Assistance to the Republic of Macedonia under IPA II, („Official Gazette of the Republic of Macedonia”, no.99/2015);
9. Law on audit on Instrument for Pre-Accession Assistance, („Official Gazette of the Republic of Macedonia”, no.66/2010 with amendments);
 10. Law on public internal financial control, („Official Gazette of the Republic of Macedonia”, no.90/2009 with amendments);
 11. Mitevski M., „State and Internal Audit in the public sector in the Republic of Macedonia“, master thesis, University “St. Cyril and Methodius”, Skopje, Institute of Economics - Skopje, March 2012;
 12. Multi-Annual Indicative Financial Framework (MIFF) for the Instrument of Pre-Accession Assistance (IPA) for 2012-2013;
 13. „Policy Paper for development of Public Internal Financial Control in the Republic of Macedonia for the period from 2015 until 2017“, Ministry of Finance of the Republic of Macedonia, Skopje, 2014;
 14. Regulation (EU) No 231/2014 of the European Parliament and of the Council of 11 March 2014 establishing an Instrument for Pre-accession Assistance (IPA II);
 15. Sectoral Agreement between the Government of the Republic of Macedonia and the European Commission setting out provisions for the management and implementation of Union financial assistance to the Republic of Macedonia under the IPA II in the policy area „Agriculture and Rural Development”(IPARD), („Official Gazette of the Republic of Macedonia”, no.38/2016);
 16. Audit Authority for audit of instrument for pre-accession assistance (IPA), <http://www.aaipa.mk/>;
 17. Central Financing and Contracting Department, <http://cfd.finance.gov.mk/>;
 18. European Union, <https://europa.eu/>;
 19. Ministry of Finance of the Republic of Macedonia, www.finance.gov.mk/;
 20. Official Gazette of the Republic of Macedonia, www.slvesnik.com.mk/;
 21. Secretariat for European Affairs, <http://www.sep.gov.mk/>

MARIJA MAGDINCEVA SOPOVA *

TANJA ANGELKOVA PETKOVA **

ZORAN TEMELKOV***

THE IMPACT OF SMALL AND MEDIUM SIZED ENTERPRISES (SMS) IN THE DEVELOPMENT OF SPORTS TOURISM IN THE MUNICIPALITY OF DOJRAN, REPUBLIC OF MACEDONIA

Abstract

Connection and similarities between tourism and sport are derived from the basic characteristic of the two activities which is “the need”. From the perspective of tourism needs, tourism is looking for satisfaction. Tourist need represent a longing to come to the phenomena and relationships that have attractive properties to see and experience, to be used, because for tourists they have a certain value.

Within the theoretical approach to the study of alternative forms of tourism, in this paper the object of study is the sports tourism as a form of alternative tourism and satisfying the tourist needs in Dojran. Separately, it is examining the connection between sport and tourism, two highly related socio – economic phenomena of modern society on the one hand and the impact on small and medium sized enterprises (SMS) in the satisfying the travel needs of the other hand.

Today with tourism are connected all the small sized enterprises, sports and health and many other alternative forms, especially active vacations with content recreational sports, entertainment, psychotherapeutic and etc. upon the basics of which the topic is detailed and fully processed,

* Assoc.Prof., Ph.D, University “ Goce Delcev”-Stip, Faculty of Tourism and Business Logistic-Gevgelija, Republic of Macedonia, e- mail: marija.sopova@ugd.edu.mk

** Assoc.Prof., Ph.D, University “ Goce Delcev” - Stip, Faculty of Tourism and Business Logistic-Gevgelija, Republic of Macedonia, e- mail: tanja.angelkova@ugd.edu.mk

*** Assoc.Prof., Ph.D, University “ Goce Delcev” - Stip, Faculty of Tourism and Business Logistic-Gevgelija, Republic of Macedonia, e- mail: zoran.temelkov@ugd.edu.mk

showing reliable data for the small sized enterprises, sports tourism and its development in general in the municipality of Dojran, Republic of Macedonia. Basics of the successful operation of enterprises are the constant introduction of new ways and forms of work and it is a recognized feature of small and medium sized enterprises (SMS).

The contribution of this paper consists in expanding the literature in this area and indicating the necessity of applying a synergistic approach in guiding the activities of small and medium sized enterprises (SMS) and contributing to the creation of the tourist offer and development of sports tourism.

Key words: enterprises, tourist destination, sports tourism

JEL Classification: L26,Z3, Z32

Introduction

Tourism represents an area that boosts the economic development and has a major role in the creation of the labor market, the establishment of enterprises in the tourist industry and thus the creation of the tourist offer. The improvement of operations and increase of the efficiency of operations is a challenge for any enterprise.

Tourism is one of the promising branches of the new millennium and all types of tourist activities get an important place in the local and national economy.

Republic of Macedonia is a traditionally tourist-oriented country. The growth of the tourism market, followed in recent years confirms that Republic of Macedonia's tourism is an active generator of business development. To increase the economic benefits of tourism, it is necessary to adopt a strategy for tourism development geared to sustainable development with an orientation to new innovative forms of tourism that will generate profits of all active entities.

Thematic tourism becomes one of the most important catalysts of development. Mainly based on the 3-E principles: entertainment, excitement and education , the tourist offer also includes the contests which combine these three elements. Dojran municipality has great potential for development of sports tourism through the use and combination of differ-

ent ways to create a tourist offer that will attract tourists.

The modern way of providing an adequate supply is associated with the operation of small and medium sized enterprises (SMS). The introduction of new forms of work, encouraging teamwork, entrepreneurial concept of corporate behavior and highlighting the importance of human resources for the operation of the enterprises, are the connecting factors that are associating them with small and medium sized enterprises (SMS). They have the ability to recognize the opportunities and at the right time and to utilize the received information's.

Representation of small sized enterprises in the field of sports tourism provides the prerequisites for the development of this tourism and application of innovative ways of organizing work and providing appropriate tourist offer.

1. TOURISM NEEDS

Knowing the tourist needs is a very important both from theoretical and practical aspect.

Psychologist Abraham Maslow¹ analyzes the human needs in hierarchical order, the needs from the lowest level to the needs of the highest level. Thus that he concludes that when a group needs is satisfied it stops being the main motivator of human behavior. That role took another set of needs that in a given moment are dominant.

Between the dependencies of tourism products is a direct consequence of the characteristics of tourist offer. The active participation of small and medium sized enterprises (SMS) in the field of sports tourism by constantly introducing of new forms of work and entrepreneurial concert of corporate behavior resulted in creating a competitive the tourism offer. The presence of small and medium sized enterprises (SMS) in the area of sports tourism expresses the orientation of entrepreneurs to innovative ways of organizing work and taking advantage of opportunities to create economic benefits.

Tourists need is a longing to come to the phenomena and relationships that have attractive properties to see and experience, to use them because they have a certain value for the tourists. Sports travel needs

¹ <http://www.simplypsychology.org/maslow.html>

are a sense of the tourist lack of significant phenomena and relationships through his pursuit of temporary change of a place of permanent residence by means of managing space and consumption to come to them because they represent a tourist value for him. It's about the specific needs that already are constituted as significant social needs, because the society has recognized them as such, since by now they are the target of organized and oriented social activity that seeks to satisfy.

Satisfying the sports tourism needs is the final result of specific tourist activity. Tourist activity begins at the moment when tourism needs will encourage the tourist movement, and end with some degree of satisfaction.

At the satisfaction of the tourist activity which represents the ultimate goal of all participants in the tourist activity are affecting numerous factors: spatial, economic, social and psychological aspects. Satisfaction depends on the number and quality of items in the geographical environment in which it is exercised, the size of the consumer, the relationships with the elements of the offer, interpersonal relations and the willingness and personal characteristics of the participants that allow meeting the tourism needs.

Satisfying the sports tourism needs is an active relation to the many participants, small and medium sized enterprises (SMS), state and local institutions and individuals that diversified its activities to meet the needs of the tourists.

2. SMALL AND MEDIUM SIZED ENTERPRISES (SMS) – A PREREQUISITE FOR THE DEVELOPMENT OF SPORTS TOURISM IN THE MUNICIPALITY OF DOJRAN

Small and medium sized enterprises (SMS), entrepreneurship and entrepreneurs are the basis of the modern market economy. Small and medium sized enterprises (SMS) are becoming a key factor in terms of creating a bigger opportunity for the owners of the enterprises and improving the situation in the local, regional community and beyond.

The area of small and medium sized enterprises (SMS), especially the field of small sector is a subject to continuous study and research. Small

sized enterprises represent an important segment in overall economic activity. This is the segment that constantly changes things, moves and develops. The emergence and development of small sized enterprises in the past twenty years are closely related to the expressed economic - development dimensions and are associated with entrepreneurship and entrepreneurial initiative. In sports, small and medium sized enterprises (SMS) are key factors for the growth of the tourism industry globally.²

The connection of modern tourism and sport can be perceived through the factors that initiate the development of tourism, sport and the economic benefit that is arising as a result of the development of tourism and sport.

The area of sports tourism is a field with high growth potential primarily as a result of consumer – tourists who are constantly in motion and constantly create new needs. The modern working concept requires enterprises to be efficient, operational and to create optimal tourist offer by encouraging development of sports tourism. Each enterprise must be able to simultaneously run three important things: he works to promote, to expand and innovate.³

As a tourist site, the development of the municipality of Dojran is in direct correlation with the development of tourism. In this tendency, there is an evident need of promotion and encouragement for new ways to develop tourism and improve existing processes. Because of the potential for development and the fact that almost none tourist offer exists in the area of sports tourism, the area is a potential segment for development in the municipality of Dojran.

The application of modern concept of work in the field of sports tourism aims on the availability of certain prerequisites which facilitate the way of practicing this concept. The development concept of sports tourism can be realized through constant monitoring of the work processes, evaluation of the needs of tourists, the supply, demand and providing conditions to meet the needs on time and place. The basic prerequisite for the application of this concept is the representation of small and medium sized enterprises (SMS) in the creation of the tourist offer through which will meet the needs of tourists.

² Burkart, A.J., Medlik, S. (1974). *Tourism. Past, Present and Future*. London: Heinemann

³ Standiven J., De Knop P., Drucker P. (2005), *Management in the new society*, Novi Sad

3. TAKING ADVANTAGE OF THE OPPORTUNITIES CREATED SMALL SIZED ENTERPRISES ACTIVE IN THE DEVELOPMENT OF SPORTS TOURISM

Creation of adequate supply in the area of sports tourism with the application of a modern concept of the work is carried out through the application of an innovative approach in shaping the supply of sports manifestation and events, creating attractive travel arrangements in the area of sports tourism, implementation of innovative organizational culture among tourism enterprises and modern management approach. Small and medium sized enterprises (SMS) change the philosophy of work and introduce the innovative concept of operations. Because of that, many enterprises respond rapidly to changing technical requirements and consumer demand through entrepreneurial behavior.⁴ Modern working conditions are characterized by dynamic development of the sport in terms of the mass involvement of subjects in completing the sports activities as well as from geographic representation of the sport. Sports tourism refers to travel, national and international which are realized in order to see the desired sporting events. Sports tourism means all forms of active and passive involvement in sporting activities in which you can participate random or organized, from commercial or non-commercial purposes and for which is required temporarily leaving the scene of residence.

Important prerequisites for fostering the development concept in the operation of small and medium sized enterprises (SMS) in the field of sports tourism is an entrepreneur – focused management that supports initiatives in operation and open communication among employees. The influence of small sized enterprises in the creation of the appropriate tourist offer is reflected through the continuous monitoring and application of new development opportunities depending on anticipated needs, appropriate selection of human resources and their placement in appropriate places, the ability to use the available development opportunities, capacity allocation and a combinational of available resources and minimizing the consequences of any failure in business activities. Small sized

⁴ Antonic, B., and Hisrich, R. D. (2004). Corporate entrepreneurship contingencies and organizational wealth creation, *Journal of Management Development*, No.23, pp. 518-550

enterprises have unique or distinctive advantage that is associated with efficient informal communications systems, high degree of adaptability to the market by introducing innovations relatively cheaper in operation and low bureaucracy.

The advantages in the operation of small sized enterprises or their strengths need to be used in order to enrich the tourist offer and development of sports tourism in the region of Dojran. In this regard it is necessary to encourage the process of creation of small sized enterprises in services based on Internet technology to promote the tourism offer, small sized enterprises - travel agencies for animation of tourists and offering daily engagements to fully meet the leisure tourists, creation of small sized enterprises that would offer a completely new line of products and services, sports and recreation facilities, small business rehabilitation services and treatment, spa and fitness centers.

4. SPORTS AND TOURISM

Sports and tourism are activities which in ancient times acted together so that sports tourism today is undoubtedly one of the most important industries which is characterized with increasing profits, without experiencing almost no aftershocks and repercussions of the global economic crisis. Modern tourism includes providing comfortable accommodation and healthy diet, but not neglecting the content of active leisure, recreation, sport, cultural relaxation with music and entertainment. The returning towards nature and reconnecting with tradition and their roots are pleasures that are increasingly required by the modern tourists.⁵

The modern tourists now, more often are looking to feel and experience the traditional values and natural beauties.

Today's tourists are much more curious, they want to explore. They are simply fed up with the main tourist offer and want something more. It is a new type of tourist – adventurers. They are interested in extreme sports. For them, a well spend a holiday is not one where they peacefully are lying on the beach, but rather one that they will be filled with much excitement and high adrenaline. Extreme biking, paragliding

⁵ <http://money.mnogoo.mk/mk/articles/Destinacii/alternativen-turizam-vo-makedonija>

are just some of the new tourist terms that have become topical in recent years in the municipality Dojran. Republic of Macedonia has all the natural prerequisites for the development of such tourism.

5. THE SPORTS TOURISM AS A SPECIFIC FORM OF MODERN TOURISM

Sports tourism is formed as a special form of tourist movement and one of the major structural changes of the modern tourism. It also means that tourist destinations in their bids must adapt to those changes, because these tourists bring specific behavior and habits. Sports tourism in the modern tourism is becoming an unavoidable part of the stay, and often is the main motive for short or long trips to a specific destination so it must be separated as a separate form of tourism.

Beside the factors of sports offer which influenced the development and establishment of this kind of tourism despite the existing recreational facilities and content, natural geographic elements and factors and their essential characteristics are of particular importance regardless whether they are basic or complex tourist offer. Namely, in tourism planning for sports tourism establishment of recreational facilities must be based on the properties and characteristics of natural geographic elements and factors, the natural resources of any one area. That the properties of these resources, tourists meet their sports - recreational needs wholesale and determine the shape and the way of tourist and economic valorization of space and influence the choice of sports and recreational facilities.

6. EFFECTS OF THE SPORTS TOURISM

Economic effects of sports tourism can be valorized as direct and indirect. Direct economic effects are achieved through travel or sports enterprises by selling and implementing sport and recreation services. They are measured by the difference achieved by the revenues and expenses of sport services and they are measurable in every tourist of a sports organization.

The indirect economic effects manifest in various forms of tourist trade and they are created by tourists that sport is their primal motive of arrival and stay in a particular tourist destination. Those are recreational athletes of all types and categories that are participating in various competitions, tournaments, recreational programs and various sports. Such programs are usually realized before the season and post season of which a special meaning is given.

7. SATISFYING TOURIST NEEDS THROUGH THE DEVELOPMENT OF SPORTS TOURISM IN THE REGION OF DOJRAN

The region of Dojran Lake is one of the most fitted regions for sports tourism in Republic of Macedonia, where all of the building and investing is mainly done by the Istatov Sports Centre.

Due to the favorable climatic conditions, especially in winter, in the municipality of Dojran there are conditions for basic preparations of sports teams. In New Dojran there is a grass football field, while in the motel "Istatov" there is a sports and recreation center with gym, playground, outdoor pool and sauna. The sports center "Istatov" is located at the entrance of Dojran, at a distance of 6 km from the Greek border.

This facility offers all kinds of sports preparation for teams from all sports. The sports center features a gym with standard dimensions in which you can play handball, basketball, volleyball and soccer. Also, there are two auxiliary football fields, a professional playground, fitness room, sauna for 15 people and a swimming pool. All indicated may be in function of sports tourism. It has 180 beds, 9 suites, 1 VIP room, 23 double rooms, 10 triple rooms and 2 quad rooms.⁶

Dojran as an interesting tourist destination with an altitude of about 700m, has conditions for the development of several types of tourism between who is the sports tourism. Overall, the climate is characterized by hot and dry summers expressed with high temperatures and mild and wet winters. Daily temperature with over 26°C in the area of Dojran is encountered over 120 days a year.⁷

⁶ <http://hotelimakedonija.com.mk/mk/Hotel/127/Hotel-Istatov-Dojran>

⁷ <http://www.dojran-info.com/>

Dojran has excellent opportunities for the development of sports tourism, which is especially expressed over the extraordinary climatic conditions that are suitable for the preparation of athletes especially in winter season. Sports tourism can be done in two ways:

- Sports tourism directly related to sports and recreation;
- Sports tourism is directly linked to the sport or tourists on holiday, as well as sports.

Although Dojran is a still small resort it still has facilities for development of sports tourism as hotels and sports grounds. This mainly refers to the sports center Istatov which is a complete hospitality hotel and sports and recreational complex.

Besides the Center Istatov, Dojran has several accommodation capacity like as private houses and hotels , which rented to tourists throughout the year and offer a total of 170 rooms and apartments for accommodation.

As part of the tourist offer of the municipality of Dojran is the sports tourism with certain sports events. As options for the development of this type of tourism would be:

- Rental of bicycles for tourists to perform cycling on marked paths like alongside the lake;
- Canoeing on Lake Dojran;
- Organizing competitions in volleyball, for tourist's recreation and participating in tourism activities of this type of tourism;
- Rental equipment for paragliding, where lovers of this sport would have the chance to enjoy the beauty of Dojran;
- The State Championship in triathlon as another reason to visit this place;
- Hiking in the newly built path along the lake shore;
- Competitions in fishing and preparing the best fish stew, etc.

At the shore of Lake Dojran they are prerequisites for equipment of more beaches that in the current terms are representing a limiting factor for tourism development. Besides the beaches of Old Dojran and New Dojran,

at the shore are estimated and locations of facilities which will significantly contribute to local economic development and improve the quality of life in the municipality.

Conclusion

Small and medium sized enterprises (SMS) are becoming a key factor in terms of creating greater opportunities for development of sports tourism and improvement of the situation at local, regional and national level. Small and medium sized enterprises (SMS) are important segment in overall economic activity in Dojran. This is the segment that constantly changes things, moves and develops. They are the carriers of economic development and are associated with entrepreneurship and entrepreneurial initiative. In sports, small and medium sized enterprises (SMS) are a key factor for the growth of the tourism sector in Dojran. The modern concept of operation requires enterprises to be efficient and create optimal tourist offer by encouraging the development of sports tourism. Development of alternative forms of tourism is resulting from modern tendencies in the world, hence the development of sports tourism.

Sports and recreational travel needs are striving to establish the psychophysical balance in any environment outside of the residence. This means that the specificity of the tourist recreation it consists in a feeling of lack of certain psychosocial content that tends to go into areas outside their place of residence or in environments where there is such content. Because of that sport and tourism have an important link between itself and as such represent a separate area. How quickly is implemented the idea of developing the sports tourism that much greater will be the contribution to the development of tourism in the municipality of Dojran.

Sports tourism in Dojran is still booming in the implementation. The rapid process of its development can bring about enormous positive impacts on tourism. Benefits from the presence of sports tourism as a form of alternative tourism are reflected in the massive attendance, the financial benefits of the use and satisfaction of visitors using a synergistic approach in guiding the activities of small and medium sized enterprises (SMS) in the creation of the tourist offer.

References:

1. Antoncic, B., Hisrich, R. D. (2004). Corporate entrepreneurship contingencies and organizational wealth creation, *Journal of Management Development*, No.23
2. Bartoluči, M., & Andrijašević, M. (1999). Sports recreation tourism. Animation in hotel-tourist industry. Opatija: Croatian Association of Hoteliers and Restaurateurs.
3. Burkart, A.J. Medlik, S. (1974). *Tourism. Past, Present and Future*. London: Heinemann
4. Cicvarić, A. (1990). *Economics of tourism*. Zagreb: The publishing company "Zagreb".
5. Drucker P. (2005). *Управување во новото општество*, Адигес, НовиСад
6. Relac, M. (1979). *Sportsrecreation in tourism*. Sports Forums, Zagreb.
7. Relac, M., & Bartoluči, M. (1987). *Tourism and sport recreation*. Zagreb: Informator.
8. Standiven J., De Knop P., Drucker P. (2005). *Management in the new society*, Novi Sad Sharpley R., Telfer D. J. (2001). *Tourism and development*
9. Hudson, S. (2002). *Sport and adventure tourism*
10. http://www.savremenisport.com/Osnove_Sport_i_turizam
11. <http://sportskiturizam.com/>
12. <http://tourism-tk.ba/index.php/sportski-turizam>
13. <http://dojran-info.com>
14. <http://www.dojranrezervacii.mk/>
15. <http://www.simplypsychology.org/maslow.html>
16. <http://hotelimakedonija.com.mk/mk/Hotel/127/Hotel-Istatov-Dojran>

Authors' Guidelines

General Guidelines

- The paper will be written entirely in English (following the **Editing Instructions**).
- All articles are subject to peer review and scientific categorization and should not exceed 4000 words. Based on that, the paper can be categorized as: 1) original scientific paper; 2) professional paper 3) reviews.

A soft copy of the manuscript is required to be sent to eis@ek-inst.ukim.edu.mk. **The authors are entirely responsible for the content of their article.**

Each author may submit a maximum of two papers per one issue (as single author and/or as co-author).

- All submitted manuscripts should not be previously published and not under consideration for publication elsewhere.
- Upon submission of manuscripts the editorial board will: 1) sends the paper to pear reviewer 2) informs the author about possible suggestions or comments on the manuscript that need to be revised or 3) informs the author that the paper has been rejected. Only positively reviewed manuscripts are published in the Journal. Provided the manuscript is refused, (the editor is not obligated to present reasons for refusal), the author may submit the paper elsewhere. Submitted manuscripts will not be returned to the author. Once the manuscript is accepted for publication, the author must not publish the paper in other journal.

Note

- The logical connection between the title of the article, abstract, key words, main content and conclusions should be respected.
- Articles that do not comply with all the requirements specified in the Editing Instructions will not be accepted for publication.

Admission fee:

85 EUR/paper

5.000 MKD/paper

The admission fee is payable after authors are notified that the paper is sent to a peer review

Beneficiary: Institute of Economics (University Ss. Cyril and Methodius-Skopje)

Bank account (national): 160010853278810

International Bank account (IBAN): MK07 1007 0100 0096 782

Bank name: Народна Банка на Република Македонија

National Bank of the Republic of Macedonia

Address: Bul. „Kuzman Josifovski Pitu, No. 1,

1000 Skopje, Republic of Macedonia

SWIFT code: NBRM MK 2X

Contact: Sretanka Gjorgjievska,
secretary of the Journal (sretanka@ek-inst.ukim.edu.mk)

URL: <http://www.ek-inst.ukim.edu.mk/>

Editing Instructions

NAME AND LAST NAME will be written with capital letters, left alignment, 12 points, bold, being followed by asterisks, and in the footnote the didactic and scientific degree, the position and place of work of the

authors e-mail are indicated (Times New Roman, 10 points) *

(12 points) <Blank line 12 point high>

(12 points) <Blank line 12 point high>

THE TITLE OF THE PAPER WILL BE WRITTEN WITH CAPITAL LETTERS, CENTERED, Times New Roman, 12 POINTS, BOLD

(12 points) <Blank line 12 point high>

(12 points) <Blank line 12 point high>

<Tab> **Abstract:** (Times New Roman, 12 points, Sentence case, bold, left alignment)

The text in the Abstract will only be in English and will have between 100 and 200 words, a single line spacing, justify alignment, Times New Roman, 12 points. (The abstract should summarize the content of the paper. Do not make references nor display equations in the abstract.)

(12 points) <Blank line 12 point high>

<Tab> **Keywords:** (Times New Roman, 12 points, Sentence case, a single line spacing, justify alignment, bold). Maximum 5 words, in English, Times New Roman, 12 points.

(12 points) <Blank line 12 point high>

<Tab> **JEL Classification:** (Times New Roman, 12 points, Sentence case, justify alignment, bold). Times New Roman, 12 points, (http://www.aeaweb.org/journal/jel_class_system.php).

(12 points) <Blank line 12 point high>

(12 points) <Blank line 12 point high>

Introduction (Times New Roman, 12 points, Sentence case, left alignment, bold)

(12 points) <Blank line 12 point high>

(The introduction of the paper should explain the nature of the problem, previous work, purpose, and the contribution of the paper. The contents of each section may be provided to understand easily about the paper.)

(12 points) <Blank line 12 point high>

* Assoc.Prof., Ph.D., University of Ss. Cyril and Methodius, Republic of Macedonia, e-mail

1. THE TITLE OF THE CHAPTER: Times New Roman, 12 points, , capital letters, bold, numbered with Arabic numbers, left allignment.

(12 points) <Blank line 12 point high>

<Tab> The text paragraphs of the paper will be Times New Roman, 12 points, justified allignment, single line spacing. The paper will be edited on A4 format (210 x 297), page setup, top/bottom 2,54 cm; left/right 2,54 cm.

The size of a <Tab> is 1,27 cm.

(12 points) <Blank line 12 point high>

1.1. Subchapter. Subchapters can be used in the text, numbered with the number of the chapter and a number showing the number of the subtitle within the chapter. The subchapters are Times New Roman, 12 points, Sentence case, bold.

(12 points) <Blank line 12 point high>

<Tab> **Conclusion:** (Times New Roman, 12 points, Sentence case, bold, left allignment)

The text in the Conclusion will be written in Times New Roman, 12 points, justify alignment, single line spacing.

CITATIONS: *Quotations and notes* should be elaborated as footnotes and marked successively with Arabic numbers¹. The scope of quotations and notes should be limited to 15 lines. Abbreviations such as “ibid”, “op. cit” can be used.

PRESENTATION OF THE MATHEMATICAL EQUATIONS

(10 points) <Blank line 10 point high>

The mathematical equations will be Times New Roman, 11 points, centred and numbered on the right with Arabic numbers between round brackets.

(10 points) <Blank line 10 point high>

$$X^2 + Y^2 = Z^2 \quad (1)$$

(10 points) <Blank line 10 point high>

PRESENTATION OF TABLES, GRAPHS AND PICTURES (12 points)

Title of the table, graph, picture or other illustration (Times New Roman, 12 points, Sentence case, bold, left allignment)

<Blank line 12 point high>

Tables, graphs, pictures and other illustrations should be presented in Ara-

¹ **Author’s surname, Initial of first name:** Title of book, Edition (only include this if not the first edition), Publisher, Place, Year, page (Times New Roman, 10 points, justify allignment, single space)

bic consecutive numbers. The references or data sources of the tables and graphs should be cited below, preceded by any additional comments or explanations. Tables, graphs, pictures and other illustrations are prepared in black and white techniques presented appropriately in the text. All graphs and illustrations and diagrams should be additionally submitted in their original electronic form (jpg, gif, xls, and alike).

<Tab> **References:** (Times New Roman, 12 points, Sentence case, bold, left alignment)

References should appear at the end of the paper, listed in alphabetical order by the names of authors.

References will be written with Times New Roman 12 points, justify alignment, numbered with Arabic numbers.

- For *books* the required elements for a reference are:
Author's surname, Initial of first name: Title of book, Edition (only include this if not the first edition), Publisher, Place, Year
- For *journal articles* the required elements for a reference are:
Author's surname, Initial of first name: Title of article, Full Title of Journal, Volume number (Issue/Part number), Year, Page numbers
- For *journal articles from an electronic source* the required elements for a reference are:

Author's surname, Initial of first name: Title of article, Full Title of Journal, Volume number (Issue/Part number), Year, Page numbers if available, Available at: include web site address/URL(Uniform Resource Locator), [Accessed date]

□ For *newspaper articles* the required elements for a reference are:
Author's surname, Initial of first name: Title of article, Full Title of Newspaper, Day and month, year before page numbers and column line.

□ For *websites* found on the world wide web the required elements for a reference are:

Authorship or Source: Title of web document or web page, Year of the document, Available at: include web site address/URL(Uniform Resource Locator), (Accessed date)

