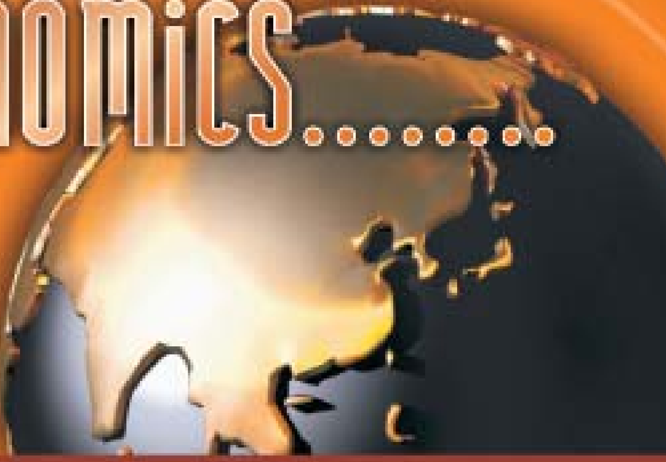
CEA
Center for Economic Analyses

CEA Journal of Economics



ISSN 1857-5269
UDK 33

Price: 300 MKD (5 EUR)

Volume 3
Issue 2
1-68 pages

Skopje, Macedonia
December 2008

CEA Journal of Economics

ISSN 1857-5269
UDK 33
Volume 3, Issue 2
Skopje, December 2008

Contents

CEA Journal of Economics
Volume 3, Issue 2
1-68 pages
Skopje, Macedonia
December 2008

Call for Papers

CEA announces a call for papers for publication in the seventh edition of the CEA Journal of Economics (Volume 4, Issue 1). The papers can come from any area of economics.

Although not strictly limited to them, please observe the following guidelines. In case of submitting theoretical papers, please include: abstract, introduction, extensive literature review, theoretical ramifications, conclusion and bibliography. In case of submitting empirical papers, please include: abstract, introduction, short literature review, methodology, empirical findings, conclusion with policy implications and bibliography.

Format: electronic version, A4, Times New Roman, no indentation, single space, one space between paragraphs, APA style, maximum 20 pages.

Deadline: 30 April 2009

Submit to: makmar2000@yahoo.com

UDC 338.439:635.63/.64(497.7) 339.564:635.63/.64(497.7) WHY TO USE THE GLOBAL VALUE CHAIN ANALYSIS: THE PROSPECTIVE AND THE INADEQUACY OF THE MACEDONIAN FRESH VEGETABLES FOR THE DEVELOPED MARKETS' CONSUMER

By Vesna Garvanlieva, MBA
CEA member

Abstract

The value chain concept represents a proven model for analysis for improvement of certain sector though better management and improved competitiveness, especially for the developing countries. This article tries to shortly present the fresh vegetable value chain in Macedonia and point towards the need for development of a national strategy for improvement of each value chain where there are potentials for improvement and increase competitiveness on an international level since the Macedonian fresh vegetable chain is part of a global value chain that needs to be supported by the policy makers in order to enhance the abilities of the local businesses to compete internationally or globally.

Key words: value chain approach, analysis, fresh vegetable, competitiveness, exports.

Introduction

It is a commonly accepted view that the agribusiness sector in Macedonia is one of the potential areas of further development, as well as it is one of the key export oriented sectors. Thus, it is reasonable to consider this sector as one of priorities of the national economy and an area where further investments should occur in order for the sector to have larger contribution to the national economic development.

Agriculture hunting and forestry, as a statistical category, in the last decade contributes with around 11%[1] to the national GDP. This number does not include the contribution of the food processing industry. If to these 11% we add the food processing industry, then the contribution of the agribusiness sector to the national GDP will add up to around 15% of the national GDP.

At the same time, the employment that this sector provides, ranges from around 60.000 to 75.000 which represents 12% to 15% of the total employment. This number does not include the significant number of seasonal labor that is engaged within the sector, taking into account the seasonality of the sector (especially fruit and vegetable production and processing).

1) Different publications of the SSO of R. Macedonia regarding 2001-2007

Out of the total national exports, the agribusiness sector (primary products and processed products) contributes with approximately 15% from the total US$ value exported.

All of these statistics provide enough information to consider the agribusiness in Macedonia as one of the noteworthy areas contribution to the national economy. However, aspiring to increase these values of export there are various variables that could direct the development of this sector.

To assess the agribusiness sector in a realistic and detailed manner it is vital to comprehend that within this sector there are abundant number of value chains that function differently and depend on many variables such as the structure of the value chain, the chain relations, the efficiency and effectiveness of each value chain, etc. In order to practice and complete a detailed analysis in accordance with the value chain concept the analysis should include tracing the product flow and identification of the value additions at different stages, identification of the key players and their relationships, identification of the businesses that contribute to the production and the enterprises providing service support, identification of all the bottlenecks preventing progress, and finally identification of the specific actions to improve the value chain efficiency and effectiveness[2]. Once this is identified the value chain should be put into a perspective that any value chain is part of a global value chain, and only improved local activities within this global value chain can result with more competitive local businesses on a global level, increased product value which stays within the country and higher income for the local population.

Having this in mind to assess the prospective and area for improvement each of the value chains should be considered in detail, and the dynamics of value chains should be assessed. However, this article will make an attempt to pinpoint the main areas for improvement and the potentials by taking the case of fresh vegetables value chain and will try to shortly elaborate why the value chain approach should be used for development of a national strategy for each agribusiness value chain and to be done by the policy makers though naming few of the problems of this chain faces in Macedonia.

The value chain concept is a concept that is used for decades and the developed world uses it and builds on (it and was first described and popularized by Michael Porter in the 1980s). However, this concept has been recently introduced on the developing countries such as Macedonia. As an approach it focuses on a certain sector or product to identify the competitiveness with the only aim to get more value from the goods and services and in our case to achieve higher exports not only by quantity but by value more importantly.

The world has seen inspiring successful stories from local businesses from the developing countries breaking into global markets (Pyke and Sengenberger, 1992; Nadvi and Schmitz, 1999) and their success is not based solely on the local relationships within the value chain. As it is with this case of the fresh vegetables, the customers are international and global and they represent a significant factor of success. "Enterprises are not exporting into an anonymous global market; often they feed into supply chains that are governed by powerful global actors. Value chain analysis demonstrates that the relationships with these global actors exert a major influence on upgrading and earning opportunities of local enterprises."[3]

If we take for a fact that the Macedonian economy, though the national policy makers, is aiming at increased exports it is inevitable to conclude that with such an aspiration there is a need of strategy that will focus on the export increase. As we gave a short explanation above each product and each value chain success and thus the export depend on different variables therefore development of national strategy for specific value chains will be necessary. The value chain approach is proven to be as a good base for development of an export strategy for specific value chain and such an analysis can assist the developing countries to improve their exports.[4]

2) Baker, D., 2006, Agriculture value chains: overview of concepts and value chain approach, FAO

3) Hubert Schmitz, 2005, Value Chain Analysis for Policy-Makers and Practitioners, International Labour Organization

4) Most of the fresh vegetables in UK are originating from Kenya flown ready for consumption in 48 hours (Governance and Trade in Fresh Vegetables: The Impact of UK Supermarkets on the African Horticulture Industry, Dolan, Humphrey)

The exports of the Macedonian fresh produce in this case the fresh vegetables are executed primarily by the local traders/exporters. Thus it is logical to conclude that this should be the main link in the chain that needs an organized and commonly accepted strategy. However, the traders by themselves may perceive that such national strategy may be irrelevant for them to follow, nevertheless the area they may be interested in to follow is to take an advantage of measures that may be motivating to export more, initiated by a national strategy.

The value chain concept promotes analysis that extends from R&D to the final disposal of the product and mapping this process is an essential to be able to complete a detailed analysis that will identify the bottlenecks and capture greater value on a national level.

We should be aware that the export markets in the developed countries such as the EU market understand and demands quality, quantity, traceability of the product, and dependability. These are factors that should drive the development of each value chain including the fresh vegetable value chain and the design of a national strategy for export improvement.

Development of such an approach means that is should be the policy-maker's responsibility to initiate such strategies however all the players in the sector and before all the private sector should be the leader in development of such a strategy and at the end feel ownership of such a model and the resulting measures. In order for such an analysis to take place first the main players need to be identified and the value chain mapped.

1. Methodology

The analysis uses some of the main findings in regards to the relationships between the fresh vegetable value chain links in Macedonia, from the research done by EPICENTAR International; Skopje for the USAID funded AgBiz Program, in Macedonia for profiling the fresh vegetable value chain in Macedonia. The profiling was based on a face-to-face interview with over 20 stakeholders within the value chain from all the direct and support activity players. In addition secondary data from the Agricultural Census 2007, State Statistics Office publications, and the National Customs Office were used.

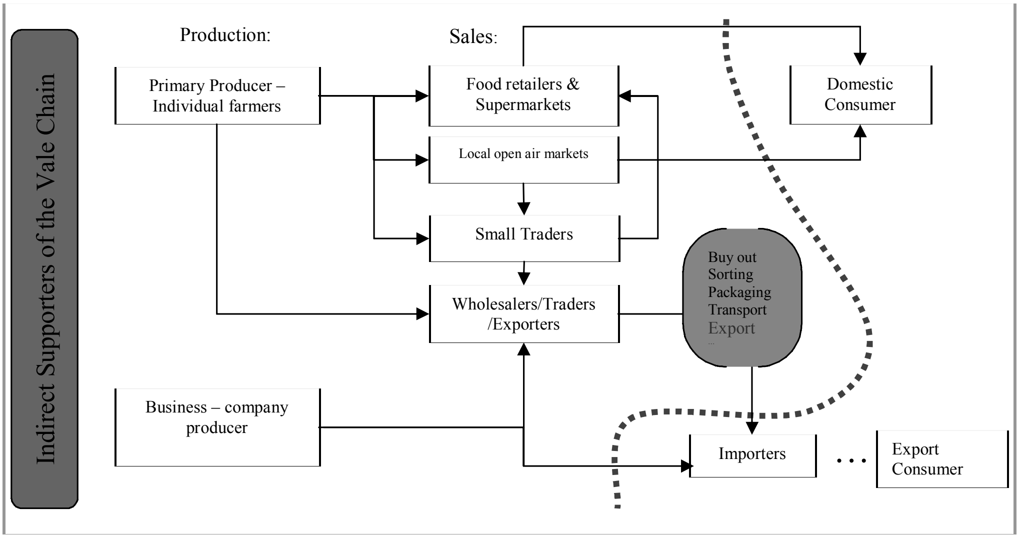
2. Fresh Vegetable Value Chain Structure and Organization

If we consider the fresh vegetable value chain of the Macedonian agribusiness sector then we have to identify numerous direct and indirect key players in the sector starting from the producers, the wholesalers, the retailers, and then it either ends up on the domestic market or the export markets' importers then to export markets' retailers and the final consumers.

The value chain is also influenced by indirect players who are affecting the chain, starting from the service providers (extension services, certification services), input providers, the government (through the policies and the subsidy programs), financial service providers, etc.

The value chain for the fresh vegetables starts with the production which is either done by individual farmers or agricultural companies. The number of the individuals i.e. farming households is by far larger than that of companies. According to the Agricultural Census 2007[5], vegetable production covers an area of 9% of the ploughs, gardens and home yards (which is 72% total agricultural land) i.e. 6,5% of the total agricultural land. Most of this area (57%) is sown with peppers, watermelons, tomatoes, cabbage, melons and cucumbers, which are the most significant fresh vegetable exports. 97% of the area is managed by individual farmers or 102.881 households and only 3% is managed by companies or by total of 50 legal entities.

5) State Statistical Bureau of Macedonia, Agricultural Census 2007



2.1.1. The producers

Having the above statistics, a very rough estimation of the average size of an individual farmer plot producing vegetable is around 0,21 ha, while average business plot producing vegetables is 12,86 ha.

This directs us to the fact that the production occurs on dreadfully small plot i.e. the national production occurs on an extremely fragmented agricultural land, thus the results are small quantities produced on a single farm. Consequently, it is normal to expect that the returns per farm are extremely small, since there is no mechanization, the production is manual, and the yields as well thus there are no economic justification. The value adding activities are expensive for such a small scale business and the activities with which the value can be added are difficult to implement by an average farmer. Then, there is a need for a motivating factor that will cause enlargement of the plots rather than fragmentation. This can be changed exclusively though the national agricultural policy and subsidy program that should motivate plot enlargement by subsidies distributed based on the yield or production quantity and quality rather that current subsidies based on area.

The individual farmers who are producing on small plots are rarely organized in full-performing associations or cooperatives that will function as sales organizers to increase the bargaining power of the farmers and to lead and promote change within the chain though spreading market demand information.

The farmers are currently producing varieties which they consider will be demanded by the buyers and consumers which most of the times are traditional and unfortunately outdated varieties not demanded on the export markets. Large part of the fresh vegetables exported will end up in the processing industries of the export markets.

The farmers are slow when it comes to variety change and production technology change which results with the outdated products not demanded on the export markets and by the final consumer.

The final consumer in the developed countries is picky and very clear about the size, color, and packaging of the product etc. And the partners within the export markets demand standards, traceability, dependability and quality.

However even if the farmers accept new varieties more easily they are not in a position to supply themselves with the adequate varieties since there is no modern and up-to-date propagation centre within the country that tests and promotes new vegetable varieties demanded on the developed export markets, and as small farmers who are not organized in a farmer's organizations with economic goals it is almost impossible to import varieties from other countries.

If we add to this the fact that almost none of the farmers possess post harvest storage facilities or other value adding facilities such as adequate premises and machinery for sorting, categorization and packaging of the produce, the problem with supplying adequate product becomes even more severe before even the product leaves the farm and thus the prices offered low by the next chain links are low.

Once the produce is prepared for sales from the farm to the next link within the value chain, other bottlenecks appear. Majority of the farmers are working with no contracts with the wholesalers. Large percentage of the sales is done on an incidental basis to the available and interested wholesalers once the product is off the field collected in a manner that is not in accordance with the demands of the buyers i.e. the final consumer. This means different producers different variety, different sizes, ripeness, no packaging, cleaning, sorting etc. This makes the farmer's bargaining power once again low and their risks high since they are dependent on the traders terms, moments before sales after the perishable produce has been harvested.

The results are disorganized sales with products which are not appropriate, not uniformed, neither can the farmer plan the sales neither the wholesaler/exporters can arrange specific sales quantities and qualities with the next link in the value chain since the availability nor quality of the products is known up to the last moment.

2.1.2. The Traders/Exporters

Knowing that the farmers are rarely equipped with any facility for value adding of the fresh vegetable production, it is the trader/wholesaler/exporter who is usually sorting, calibrating and packaging the products according to the needs and demands of the importers on the other side of the border i.e. the export markets.

The quantities of fresh vegetables which are ending up at the wholesalers which are most of the time exporters of the fresh producers are traded on the basis of arms length market relationships. The products are produced without reference to the needs of the particular buyers since the exporters from Macedonia are usually the last direct link in the value chain within the country. The vegetables are sold to importers in other countries since there are no links with the retailers who are selling the product to the final consumer. The products are sold to importers in the export market and the Macedonian companies lose track of what is the happening to the product from there on, this on the other hand indicates that the exporters have limited information along the chain on what is happening to the goods, what are the final consumer demands and wants and thus the opportunity to add further value to the product is lost. The fresh vegetable value chain is not perceived as a part of a much larger global value chain not being aware how to fit within the international flows. For example adding value by small packaging, preparation of ready salads etc. are products which achieve much higher price that the vegetable sold in bulk and is commodity, thus though is still far from the developments of this value chain.

2.1.3. The export markets

The fresh vegetables from Macedonia are exported mainly on the regional markets. This includes the ex-Yugoslav market which represents a traditional market for the exporters with established links. Then we have the remaining countries within the region (Greece, Bulgaria, Romania, and Albania) and finally the EU market (without the regional EU members).

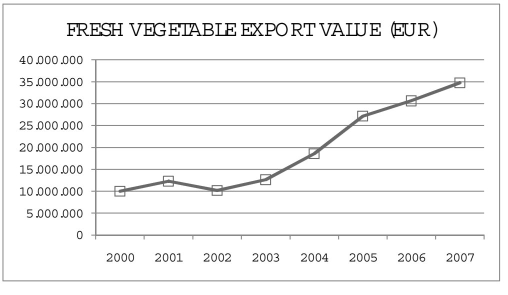
The exports of fresh vegetables from Macedonia indicate a strong trend of increase in quantity, especially during the last few years. Ex-Yugoslavia, considered as one market, is traditionally and is still the largest consumer of the Macedonian fresh vegetables. This market has "survived" due to several reasons. Firstly, the well kept relationships among partners which have been active during the last decades when Macedonia has been the main producer of agricultural products for Yugoslavia. Secondly, the consumers in this region are used and familiar with the Macedonia production therefore still consumes the fresh vegetables from Macedonia. This is still considered as a "steady" market for the Macedonian fresh products but these markets could easily be considered as a safe haven markets which provide security for the Macedonian exporters but at the same time stifle the need for change necessary for the more developed markets.

The regional market, besides the ex-Yu market, is another significant market which is comparable and very similar to the ex-Yu market.

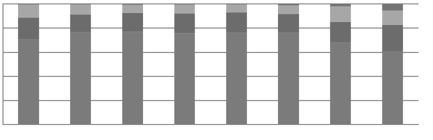
The European market is another destination of the Macedonian fresh produce which has been slightly increasing in the years from the last years. The European market is considered as more "demanding" and sophisticated is sense of the consumer needs. This market demands smaller packages; different varieties etc. which according to the exporters is still something to strive for. The reason why the Macedonian production is not still significantly "aiming" this market is due to the "security" on the ex-Yugoslav and regional market which is familiar and satisfied with the current products from Macedonia providing some security of sales (for now). At the same time the Macedonian fresh produce on the European market is exposed to a competition which is traditional and well established on this market especially from Spain, Turkey and Greece to an extend which are "domestic" producers with higher compliance with the consumer demand, subsidized production etc.

However, Macedonia should consider EU markets as a target for the future development especially considering the accession process of the Balkan countries into EU, the sophistication of the consumer that appears on the regional market, the potential competition, etc.

If we take the most significant exports of fresh vegetables are the exports of fresh tomato, pepper, cucumbers, watermelons and melons, cabbage from the figures bellow we can conclude that the exports in value are significantly increasing, however the ex-Yugoslav market is still consuming more than 60% of the total exports.



Source: Macedonian Customs Office Archive



Source: Macedonian Customs Office Archive

The figures above confirm and show that the ex-Yugoslav market is still the most predominant market where the fresh vegetables end under the assumption that these countries do not re-export the products to the EU. There is a trend that the ex-Yugoslav exported value is decreasing as part of the total exports while the other regional country's exports are taking larger parts in these exports. However the possibility that some of these countries such as Bulgaria, Greece, Romania are already members of the EU it could be assumed that part of this products at the end of the day get into the EU market as well however as other country's products.

This seems promising however, just for an illustration, if we compare the imports of fresh vegetables in the EU we can see that besides the pepper the other fresh vegetables coming from Macedonia within the EU does not exceed more that 0,5% of the total imports, showing that the Macedonian fresh vegetable is not known on the EU market and the penetration is still low.

European Union - Macedonian Imports % of the Total EU Imports							
	1999	2000	2001	2002	2003	2004	2005
Cabbages and other brassicas	0,10%	0,04%	0,61%	0,21%	0,16%	0,27%	0,33%
Cucumbers and gherkins	0,03%	0,22%	0,06%	0,05%	0,13%	0,10%	0,07%
Pepper (Piper spp.)	0,70%	1,23%	0,99%	0,31%	0,75%	2,14%	2,58%
Tomatoes	0,00%	0,04%	0,01%	0,01%	0,03%	0,02%	0,02%
Watermelons	0,19%	0,50%	0,45%	0,54%	0,26%	0,27%	0,51%

Source: FAOSTAT

3. Conclusion

The Macedonian fresh vegetable value chain has the potential to become more significant for the national economy. Within the short attempt to pinpoint some of the main issues in the fresh vegetable value chain it is obvious that a detailed analysis and mapping of this sector can contribute even more, with the intent to fit within a global value chain.

This article identified numerous problems which are ranging from the input supply, production, post- harvest, export etc. However it is crucial to be understood that the change within the value chain will not be achieved only by one player such as one farmer or one exporter. In order to achieve and keep most of the economic value of the product in the country it is necessary that a national strategy for each value chain is defined.

The production of the fresh vegetables is only one value adding activity and it is not the bulk raw vegetables that should be the final product. To improve the sector's performance the progress should be aimed at improving the input supply, the production methods, the subsidy politics, the transportation, the export policies, business support services, etc. All of these should be aligned and streamlined to functioning as one and fit within the global chain. The most money-making activities should be selected and kept within the country, the relationships between the domestic businesses and the global leaders should be information intensive relationships, and the arm's length market relationships left. The improvements will not be achieved only by one or two businesses; there is a need for enhancement on a larger scale by a national strategy which will facilitate the improvement of the whole sector that will create leaders.

In order to keep the value within our borders the next steps of the sector should focus on creation of a strategy which will activate and organize all the players in the sector supported by an institutional framework to:

- Streamline the production to the needs of the final consumers on the export markets
- Creation of direct links with the export markets retailers rather than solely importers
- Produce products with high value added for the developed consumer society providing products for immediate use etc.
- Continuity of supply and constant level of quality according to standards
- Traceability of the produce through special logistics systems (from the field to the retailer)
- Seedlings, exporters, importers and retailers together need to develop new varieties and extend the growing season
- Etc.

This all should lead to the conclusion that a value chain approach analysis is necessary for the improvement of the Macedonian agribusiness though fitting in the global value chains by development of a strategy which will be focused on specific value chains and developed through the private sector that needs to produce lead companies that will govern the value chain. The private sector on the other hand needs to internally upgrade their: processes (increase efficiency and effectiveness internally), product (new products, improvement of the products), function (increase the level of value adding by adding or changing the value adding activities within the companies). This way there will be more significant earnings and there earnings will be kept in the country causing further and more rapid development having in mind that the value chain approach is all about creating value and management of the processes.

References:

1. Baker, D., "Agriculture value chains: overview of concepts and value chain approach", FAO, 2006
2. Schmitz, H., "Value Chain Analysis for Policy-Makers and Practitioners", International Labour Organization, First publication, 2005
3. Bartlett, C., Ghoshal, S., Birkinshaw, J.,"Transantaional Management-texts, cases and readings in cross-border management", McGraw Hill, International edition 2003
4. Dolan, C., Humphrey, J., "Governance and Trade in Fresh Vegetables: The Impact of UK Supermarkets on the African Horticulture Industry" (http://www.colorado.edu/geography/class_homepages/geog_3662_s06/uk.pdf)
5. Agricultural Census 2007, State Statistical Office of Republic of Macedonia
6. Gross Domestic Product of Republic of Macedonia-annual editions for 2006, 2005, 2004, 2003, 2002, 2001, 2000, State Statistical Office of Republic of Macedonia

UDC 005.96
STRATEGIC HRM AND ORGANIZATIONAL PERFORMANCE: A REVIEW OF 'BEST FIT' - 'BEST PRACTICE' DEBATE

Irina Majovski, MSc
Integrated Business Faculty

Abstract

The assumption that human resources play strategic role in the success of a company has led to extensive research in the field of strategic HRM. This paper reviews the empirical work on HRM and organizational performance link. It focuses on the debate in strategic HRM literature between the contingency theory and universalism, which covers the largest body of the literature in this field.

Key words: strategic HRM, organizational performance, 'best practice', 'best fit'.

Introduction

Human resources have long been seen as a cost to be minimized rather than a potential source of value creation. However, nowadays, people and people management are increasingly seen as key elements of competitive advantage (Allen and Wright, 2006; Pfeffer, 1994, Boxall and Purcell, 2003). The new interest in human resources as a strategic lever, which has emerged in the last two decades, suggests that HRM contributes directly to the implementation of the operating and strategic objectives of firms.

With the advent of the resource-based view of the firm (Barney, 1991), strategic HRM research moved to a more internal focus. According to Barney's (1991) resource-based view, firms should look inward to their resources, both physical and intellectual, for sources of competitive advantage. Firms can develop sustained competitive advantage only by creating value in a way that is rare and difficult for competitors to imitate. Traditional sources of competitive advantage such as natural resources, technology, economies of scale etc. are not only easy to imitate but are also easily accessible, mainly because of the fast development of technology. Thus, human resource systems can become crucial source of sustained competitive advantage.

The resource-based approach is based on the assumption that competitive advantage is obtained if a firm can obtain and develop human resources that enable the firm to learn faster and apply its learning more efficiently than its competitors. (Hamel, Prahalad, 1989). As Barney (1995) underlines "human resources include all the experience, knowledge, judgment, risk-taking propensity and wisdom of individuals associated with the firm". In line with human capital theory, resource-based theory emphasizes that investment in people adds to their value in the firm. Thus, the challenge to organizations is, as Ulrich (1998) stated, "to ensure that they have the capability to find, assimilate, compensate and retain the talented individuals they need". A properly developed HR system creates value when it is incorporated in the operational systems of an organization in a way that it enhances the firm's capabilities. Such a system is difficult to imitate due to lack of understanding of the precise mechanisms by which the interaction of human resource practices generate value.

The assumption that company's human resources can play a strategic role in the success of an organization has led to extensive research in this field, in an attempt to set theoretical frameworks and empirical evidence of the impact of HRM on organizational performance. However, the mechanisms by which human resource management creates and sustains value are complex and are still not well understood. Many studies in this field, covering different HR practices and processes, different variables, and different industries, have led to an intensive debate on strategic HRM and performance link.

Strategic HRM and Organizational Performance

Strategic HRM is concerned with the strategic choices associated with the use of labor in firms and the ways in which HRM influences firm's performance. Wright and McMahan (1992) defined strategic HRM as "the pattern of planned human resource deployments and activities intended to enable the firm to achieve its goals". The assumption underpinning the strategic HRM is that people are the organization's most critical resource and that organizational success largely depends on them. So, if an appropriate set of HR practices and processes is developed and implemented in an organization it will subsequently lead to better organizational performance.

Based on this assumption, throughout the 20th century, there were a number of waves of interest in how to improve workplace performance, and substantial amount of research to establish a clear positive link between HR practices and organizational performance. One of the most important initiatives in recent time is associated with the idea of 'high-performance work systems' (HPWS), the term being introduced by Appelbaum et al (2000) and widely accepted by HRM researchers.

High performance work systems aim to make an impact on the performance of the firm through its people in such areas as productivity, quality, level of customer service, growth, profits. The practices and systems that are identified as supportive of high performance typically refer to more rigorous selection and better training systems to increase ability levels, more comprehensive incentives (such as employee bonuses and internal ladders) to enhance motivation, and participative structures (such as self-managing teams and quality circles) that improve opportunity (Appelbaum et al, 2000).

One of the streams running through the literature on HPWS is that these practices work much better when 'bundled' together (Ichniowski et al, 1996; MacDuffie, 1995). An organization's HR strategies, policies and practices are a unique blend of processes, procedures, personalities, styles, capabilities and organizational culture. Thus, only systemic interactions among these practices can increase organizational performance. Adding only one of the practices is likely to 'have no effect on performance' (Ichniowski et al, 1996; Purcell et al. 2003).

However, these high performance work systems vary significantly as to the number of practices included, the outcomes, and sometimes even as to whether a practice is positively or negatively related to high performance (Becker and Gerhart, 1996). For example, some models include only four or five key practices, while others include more than dozen (as for example, Pfeffer, 1994). The studies of HPWS also include a variety of outcome variables, such as profitability (Delery and Doty, 1996), productivity (Arthur, 1994; Huselid, 1995; MacDuffie, 1995), and broader array of benchmarks including quality, employee turnover etc. In addition, studies also differ in whether a practice is positively or negatively related to high performance. As Becker and Gerhart (1996) suggest in some studies high performance employment systems have low emphasis on variable pay (Arthur, 1994), while in others these systems have strong emphasis on variable pay (Huselid, 1995; MacDuffie, 1995). Also, some HR strategies that rely on internal promotions and grievance procedures are described as high performance practices (Huselid, 1995; Pfeffer, 1994), while in other studies these practices are included in more rigid HRM systems.

In addition to the above mentioned, Boxall and Purcell (2003) argue that the definition of the component of HPWS is also confusingly varied due to the absence of presenting the theoretical framework that supports researchers' perception of what practices to include. Most researchers base their perception on the AMO (ability, motivation, opportunity) theory of performance (Appelbaum et al, 2000). This theory translates performance into a function of employee ability, motivation, and opportunity to participate. In other words, employees are to perform better when they are able to do so, they have the motivation to perform better, and when they are provided an opportunity to perform better.

Several models of the relationship between HRM and performance have been developed (Schuler and Jackson, 1987; Guest, et al, 2000; Purcell et al, 2003); however, one of the most heavily cited in recent years is the People and Performance Model developed by Purcell et al (2003). Based on the assumptions of AMO theory 11 human resource practices that give meaning to AMO have been identified, as shown in Figure 1. In their longitudinal study of 12 companies in UK they reported clear evidence between HR policies and practices, levels of satisfaction, motivation, commitment and operational performance. The other key feature of the model is the role of line managers who need to implement the practices properly in order to have best effect on performance.

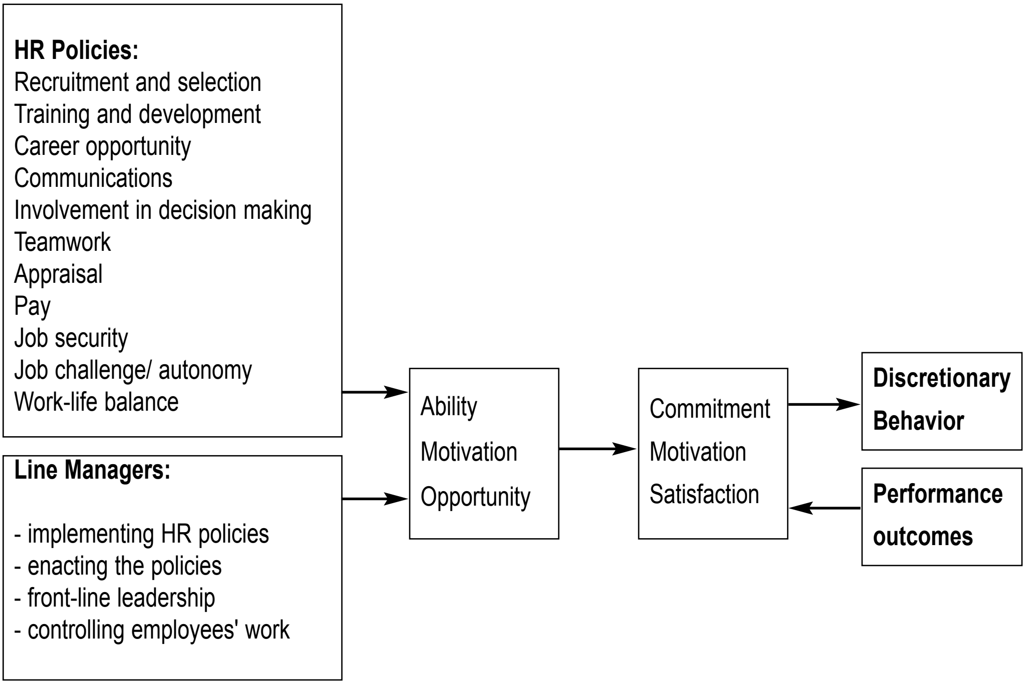


Figure 1. The People and Performance Model (Purcell et al, 2003), CIPD, adapted

In spite of the theoretical frameworks that have been developed and the significant amount of research that presents the link between HRM practices and firm performance, there are still several key questions that remain unanswered. In this regard, Allen and Wright (2006) argue that there is still a general lack of understanding about the concept of fit, and its role in the link between strategy and HRM. Secondly, there are still unanswered questions regarding whether HRM defined as a system of HR practices truly constitutes a resource as outlined by Barney (1991).

The 'best fit' - 'best practice' debate

Delery and Doty (1996) categorized the theories of strategic HRM and organizational performance in three modes: the universalistic, the contingency and the configurational.[6] The largest body of literature in the field of strategic HRM focuses on the extensive debate about the importance of contingency theory ('best fit') and universalism ('best practice').

The 'best practice' model advocates universalism, i.e. it is based on the belief that adopting and implementing a set of 'best practices' will lead to improved organizational performance. This approach received strongest support in many studies (Pfeffer, 1994; Huselid, 1995; Delaney and Huselid, 1996). These studies, across industries or within a specific sector, show that the organizational performance, measured by productivity, labor turnover, growth, market share or financial indicator, is better when more of the high-performance practices are used.

Pfeffer (1994), as one of the strongest supporter of the 'best practice' approach, identifies 16 'best practices' in companies that lead to higher productivity and profit across all types of organizations, some of them being employment security, selectivity in recruitment, incentive pay, information sharing, participation and empowerment, teamwork, training and development, promotion from within, and so forth. Other researchers (Guest, 1999; Patterson et al., 1997) have determined sophisticated systems for recruitment and selection, intensive and ongoing training, job design which ensures flexibility, frequent and comprehensive communication, grievance procedures, promotion, employee share ownership, as best practices.

However, Becker et al (1997) stress that high-performance work systems must be tailored carefully to a firm's individual situation to achieve optimum results.

In addition, Guest (1997) argues that in all studies (Huselid, 1995; Delaney and Huselid, 1996; Arthur, 1994; Ichniowski, Shaw and Prennushi, 1994; MacDuffie, 1995) where different types of fit were compared, the 'best practice' was invariably the one that received the strongest support. In this regard, Pfeffer (1994) underlines that the empirical support for contingencies is weak and thus the 'best practice' approach should be preferred.

As much as there is support to this approach, there is as well criticism. Firstly, there has been criticism on the variety of 'best practices' both in type and number (Becker and Gerhart, 1996; Dyer and Reeves, 1995). Secondly, the belief in individual 'best practices' is inconsistent with the emphasis on the internal fit in the resource-based view, which suggests the importance of complementary resources (Purcell, 1999; Becker and Gerhart, 1996), i.e. the HR practices can only in combination enable a firm to realize its full potential (Barney, 1995).

Moreover, some cross-national studies do not find any support to the universalistic approach based on national variations both in labor laws and cultural practices (Wever,1995; Appelbaum and Batt, 1994). However, Boselie, Paauwe and Jansen(2000), in their research of high-performance work systems in companies in Netherlands, found 12 out of Pfeffer's 16 'best practices' that are common in Dutch companies.[7]

6) Guest (1997) redefined the approaches as 'fit as an ideal set of practices', 'fit as strategic integration' and 'fit as bundles' among others, while Richardson and Thompson (1999) as 'best practice', 'best fit', and 'configurational' or 'bundles'.

7) The Dutch economy positively outperforms other EU countries on a number of economic performance indicators like employment, job creation, economic growth (Boselie, Paauwe and Jansen, 2000)

Boxall and Purcell (2003) argue that the 'best practices' have become ends in themselves, apparently disconnected from the company's goals in its specific context. In that context, Becker and Gerhart (1996) point out that the concept of best practices can be accepted for identifying the principles underlying the choice of practices, however human resource practices should be embedded in organizations in a way that they fit organization's needs. Purcell et al. (2003) in their research of people and performance link show that there is no universal 'best practice'. On the contrary, they argue that all successful companies have broad and integrated clusters of practices that are tailored to the needs of the organization.

The 'best fit' advocates that HR strategy will be more effective if appropriately integrated in its organizational and environmental context. This approach covers a range of models focusing either on linking HR strategy to the competitive strategy ('vertical' or 'external fit'), or on 'bundles' or 'clusters' or HR practices that are designed to fit and support each other ('horizontal' or 'internal fit').[8]

The basic assumption underpinning the contingency theory is that companies that have matched the HR strategy with the company's competitive strategy will report superior performance. The most well-known model of external fit was developed by Schuler and Jackson (1987), who offered a theoretical framework of the connections between competitive strategies, desired employee behaviors and particular HR strategies. Namely, they argue that HR practices should be designed to reinforce certain employee behaviors required by Porter's generic strategies.

There have been several studies that offered some support to the contingency approach (Miles and Snow, 1984; Schuler and Jackson, 1987; Delery and Doty, 1996; Youndt et al, 1996). Huselid (1995) found that companies that link HRM practices to strategy report higher financial performance, while Youndt et al. (1996) in their research of 97 manufacturing plants found that the fit between HR practices and strategy, in particular the quality strategy, provides the best results.

This approach does not lack criticism as well. Some scholars (Becker & Gerhart, 1996; Boxall & Purcell, 2003) argue that 'best fit' model raises questions about which are the most critical contingencies or elements in the organizational and environmental context. In addition, Boxall and Purcell (2003) underline that this model overlooks employee needs and prevailing social norms and legal requirements which are also part of the strategic goals of HRM. Therefore, a more sophisticated approach to the contingency theory would require considering the interaction between certain critical contingencies in the organizational context and the environment in which it operates, such as culture, operational processes and external environment.

In this regard, Boxall and Purcell (2003) propose a framework of major factors (contingencies), both inside and outside a company, that affect management choices in developing HR strategies. In particular, these factors are organized in two broad categories: economic and technological factors and social and political factors. See Figure 2.

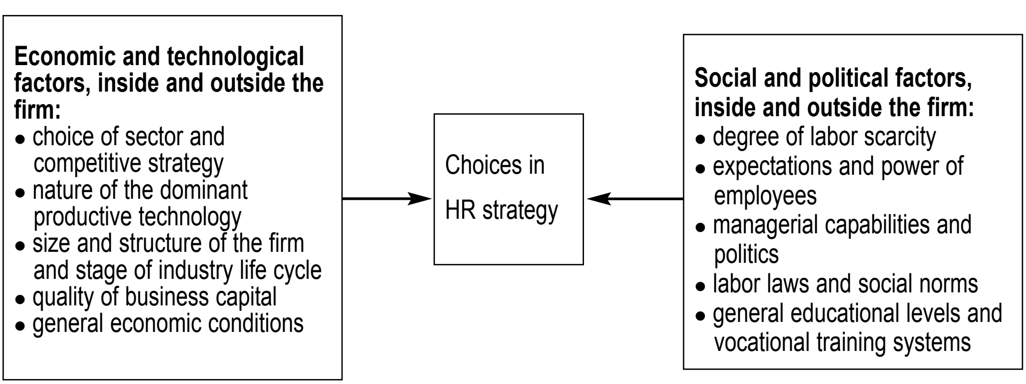


Figure 2. Major factors affecting HR strategies, Boxall and Purcell (2003)

8) According to Delery and Doty's categorization (1996), these are the contingent and the configurational modes.

The configurational approach or bundling conveys the assumption that companies with bundles of HR practices have higher level of performance. The idea is that practices within bundles are interrelated and therefore reinforce each other having greater impact on performance (Ichniowski et al., 1996; MacDuffie, 1995; Dyer and Reeves, 1995; Delery, 1998). The aim of bundling is to develop mutually reinforcing set of HR practices which jointly contribute to the attainment of organization's strategies.

Research has provided some evidence in favor of the configurational approach. Dyer and Reeves (1995) stress that employee performance is a function of both ability and motivation and that the logic of bundling is to enhance both. Thus, best results should be obtained when there are several ways to enhance employee abilities and skills and incentives to enhance their motivation. MacDuffie (1995) in his research of manufacturing plants that have flexible production found that bundles of internally consistent HRM practices are associated with higher productivity and quality.

Some researchers (Wright and Snell, 1998; Boxall and Purcell, 2003) agree that the concept of 'internal fit' is too simplistic, taking into consideration the paradoxical elements involved in managing people, and that strategic tensions among competing interests should be considered as well. Nevertheless, the combination of both vertical and horizontal alignment was a significant step in explaining how HRM could contribute to the accomplishment of strategic goals of companies.

Conclusion

The review of the research on strategic HRM and organizational performance clearly presents the complexity of the field. Guest (1997) argues that although there is empirical support for each of the three main approaches to HRM and performance, there is consistently stronger support for the internal fit or 'best practice' model. However, there is still lack of theory about the nature of HRM practices, and little consensus on what these are or the way they are linked.

To sum up, most researchers agree that the theory and the empirical research on the nature of HRM, the nature of the outcomes and the nature of the linkages need to be improved. As some scholars (Becker and Gerhart, 1996; Purcell, 1999) suggest, in order to reconcile the tension in this debate, it is necessary to make …"an analytical distinction between the surface level of HR policies and practices in a firm (which are influenced by the societal, sectoral and organizational context) and an underpinning level of processes and principles (the generic HR processes)", because, "…. both general principles and specific contexts play an important role in the theory and practice of strategic HRM" (Boxall and Purcell, 2003).

References:

Arthur, J.B. (1994) "Effects of human resource systems on manufacturing performance and turnover", Academy of Management Journal, 37, pp.670-87

Allen, M. R. and Wright, P.M. (2006) "Strategic Management and HRM", Center for Advanced Human Resource Studies, Cornell University, Working Paper 06-04

Appelbaum, E., Bailey, T., Berg, P. and Kalleberg, A. (2000) Manufacturing Advantage: Why High-performance Systems Pay Off, Ithaca, NY, ILR Press

Barney, J. (1991) "Firm resources and sustained competitive advantage", Journal of Management, 17(1), pp. 99-120

Barney, J. (1995) "Looking inside for competitive advantage", Academy of Management Executive, 9(4), pp.49-61

Becker, B. and Gerhart, B. (1996) "The Impact of human resource management on organizational performance: progress and prospects", Academy of Management Journal, 39(4), pp.779-801

Becker, B. E., Huselid, M.A., Pickus, P. S. and Spratt, M.F. (1997). "HR as a source of shareholder value: research and recommendations", Human Resource Management, 36(4), pp.39-47

Boselie, P., Paauwe, J. and Jansen, P. (2000) "Human resource management and performance: Lessons from Netherlands", Erasmus Research Institute of Management, Research Paper

Boxall, P. and Purcell, J. (2003) Strategy and Human Resource Management, Palgrave Macmillan, Basingstoke

Delaney, J.T. and Huselid, M.A. (1996) "The impact of human resource management practices on perceptions of organizational performance", Academy of Management Journal, 39(4), pp. 949-69

Delery, J. and Doty, D. (1996) "Modes of theorizing in strategic human resource management: tests of universalistic, contingency and configurational performance predictions", Academy of Management Journal 39(4), pp.802-35

Delery, J. (1998) "Issues of fit in strategic human resource management: implications for research", Human Resource Management Review, 8(3), pp.289-309

Guest, D.E. (1997) "Human resource management and performance: a review of the research agenda", International Journal of Human Resource Management, 8(3), pp.263-76

Guest, D.E. (1999) "Human resource management: the workers' verdict", Human Resource Management Journal, 9(2), pp.5-25

Guest, D.E., Michie, J. and Sheehan, M. (2000) "Effective people management: initial findings of future of work survey, Research paper, Chartered Institute of Personnel and development, London

Dyer, L. and Reeves, T. (1995) "Human resource strategies and firm performance: what do we know and where do we need to go?", International Journal of Human Resource Management, 6(3), pp. 656-70

Hamel G. and Prahalad, C.K. (1989) "Strategic intent", Harvard Business Review, May-June, pp.63-76

Huselid, M.A. (1995) "The impact of human resource management practices on turnover, productivity and corporate financial performance", Academy of Management Journal, 38, pp.635-70

Ichniowski, C., Shaw, K. And Prennushi, G. (1994) "The Effects of human resource management practices on productivity", Working paper, Columbia University

Ichniowski, C., Kochan, T., Levine, D., Oslon, C. And Strauss, G. (1996) "What works at work: overview and assessment", Industrial Relations, 35(3), pp.299-333

MacDuffie, J.P. (1995) "Human resource bundles and manufacturing performance: organizational logic and flexible production systems in the world auto industry", Industrial and Labor Relations Review, 48(2), pp.197-221

Miles, R. and Snow, C. (1984) "Designing strategic human resource systems", Organizational Dynamics, Summer, pp. 36-52

Pfeffer, J. (1994) Competitive Advantage Through People: Unleashing the Power of the Workforce, Boston, Harvard Business School Press

Purcell, J. (1999) "The search for 'best practice' and 'best fit': chimera or cul-de-sac?", Human Resource Management Journal 9(3), pp. 26-41

Purcell, J., Kinnie, N., Hutchinson, S., Rayton, B. and Swart, J. (2003) Understanding the People and Performance Link: Unlocking the Black Box, Chartered Institute of Personnel and Development, London

Schuler, R.S. and Jackson, S.E. (1987) "Linking competitive strategies with human resource management practices", Academy of Management Executive, 9(3), pp.207-19

Ulrich, D. (1998) "A new mandate for human resources", Harvard Business Review, Jan-Feb, pp.124-34

Wright, P.M. and McMahan, G.C. (1992) "Theoretical perspectives for strategic human resource management", Journal of Management, 18, pp.295-320

Wright, P.M. and Snell, S.A. (1998) "Toward a unifying framework for exploiting fit and flexibility in strategic human resource management", Academy of Management Review, 23(4), pp.756-72

UDC 005.962.13(497.7)
THE IMPORTANCE OF BALANCED SCORECARD AS A STRATEGIC MANAGEMENT TOOL AND ITS IMPLEMENTATION IN THE COMPANIES IN R. MACEDONIA AND WORLDWIDE

Eftimov Ljupco, Teaching Assistant, e-mail: eftimov@eccf.ukim.edu.mk
Eftimov Lucija, MBA Student, e-mail: lkolumbic@yahoo.com
Serafimoska Marina, Teaching Assistant, e-mail: marinas@eccf.ukim.edu.mk

Faculty of Economics-Skopje,
University "Ss. Cyril and Methodius",
R. Macedonia

Abstract

Robert Kaplan and David Norton have been, and remained among the most influential authors in the field of Performance Management and their Balanced Scorecard still is the most successful concept in this field. This paper describes the evolution of Balanced Scorecard distinguishing three main evolution phases in its development, concerning the strategic and performance management literature. The paper examines the results of BSC implementation in the companies worldwide, and compares with the results of its employment in Republic of Macedonia. Also suggest potential improvements for ensuring higher implementation rate in Macedonia.

Key words: *Performance Management, Balanced Scorecard (BSC), Republic of Macedonia*

I. Introduction

In the information age that we are living in, many companies and products live and die on information, and the most successful companies are the ones who use their intangible assets better and faster. Intangibles such as intellectual capital, customer and supplier relationship, product development and innovation, are nowadays the drivers of company life, much more then land, capital or labour [1]. But on the other hand, long period of time managers were trapped with archaic accounting tools, developed hundreds of years ago, with which was almost impossible to determine the company key success factors or to become aware of their value. What is even worse, in crisis periods for the companies, managers' attention was put on improving the efficiency of the physical assets only, by undertaking severe cost-reduction programs focused on future value-creating functions such as human resource training, new product development, innovation and market research.

Many have criticized financial measures because of their well-documented inadequacies, their back-ward looking focus, and their inability to reflect contemporary value-creating actions [2]. Managers' exclusive reliance on financial measures alone when making their decisions often leaded in failure to incorporate these "hidden value" drivers.

Once the need for new performance measurement tools was recognized, impressive attention was attracted, both among academics and practitioners. New research papers and articles on this topic are being published at a remarkable rate of one every five hours of every working day since 1994 [3]. To date there are more then 31 million web-sites dedicated to performance measurement and performance management, and hundreds of IT companies are offering different software solutions and applications for measuring and managing company performance.

Like in any rapidly growing research field we have been witnesses of the development of many new approaches and performance measurement frameworks, such as Performance Measurement Matrix [4], Performance Pyramid [5], Results-Determinants Framework [6], of course, Balanced Scorecard (BSC) [7], and most recently Performance Prism [8].

Only few of these measurement systems have drawn managers' attention just enough to initiate reach stream of their implementation. Balanced scorecard was definitely one of them. At first introduced as performance measurement reporting tool in the early 1990's by Robert S. Kaplan and David P. Norton, this approach relatively fast evolved in strategic management system with a clear ambition to go further toward an all-encompassing strategic and control system. Despite its unchanged fundament of four perspectives with limited number of measures classified and carefully linked with the strategy, many new elements and features represented its historical development (see Figure 1). This paper aims to describe the evolution of Balanced Scorecard distinguishing three main evolution phases in its development, concerning the strategic and performance management literature.

Table 1: Historic overview of the evolution of Balanced Scorecard

1992 "The BSC: Measures that Drive Performance" (HBR Article)	Balance between financial and non-financial measures Four perspective view
1993 "Putting the BSC to Work" (HBR Article)	Link measures to strategy
1996 "Using the BSC as a Strategic Management System" (HBR Article) The BSC: Translating Strategy into Action (book)	Four Management Processes -translate the vision -communicate and link -business planning and goals -feedback and learning Employment of causal chain
1999 The Strategy Focused Organization (book)	Higher focus on BSC as the center of the management system
2000 "Having Trouble with Your Strategy? Then Map It." (HBR Article)	Introduction of strategy maps
2003 Strategy Maps (book)	Broadening of the role of BSC in the strategic process with the concept of "strategy map" How to create, manage and communicate a strategy
2005 "The Office of Strategy Management" (HBR Article)	Establishment of a new corporate-level unit, an Office of Strategy Management (OSM) Primary responsibility: managing strategy

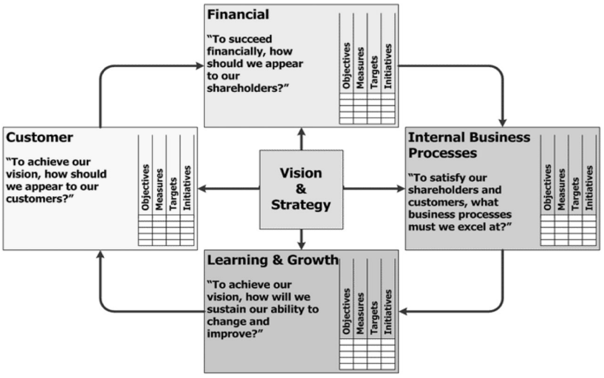
II. Balanced Scorecard as a performance measurement tool

As a result of a year-long research with twelve companies on the future of the performance measurement, Robert S. Kaplan and David P. Norton published the summarized results in their 1992 Harvard Business Review article: "The Balanced Scorecard: Measures that Drive Performance". BSC was the first original, consistent and logical approach that with its "4box" simplicity was providing balance between financial and non-financial measures, leading and lagging indicators and short and long-term objectives. The authors proposed to managers, in addition to traditional financial measures, to fill out the empty boxes with limited number of customized measures from three other business perspectives: Innovation and Learning, Internal Business and Customer Perspective. Each perspective's measures should provide answers to the performance questions: How do we look to shareholders? (Financial Perspective); How do customers see us? (Customer Perspective); What must we excel at? (Internal Business Perspective); Can we continue to improve and create value? (Innovation and Learning Perspective see Figure 2).

The definition of Balanced Scorecard was imprecise and focused on the selection of measures for each of the perspectives. The authors' precaution on managers' well-documented measurement assertiveness [9] was shown with the alert that they shouldn't put their focus on identifying what could be measured in the company, but on choosing only limited number of measures customized by using attitudinal questions related to the company vision and strategic goals. They endorsed that by "putting vision and strategy in the center of the measurement system" improved organizational performance can be expected, but only if appropriate changes in human behavior are made and necessary actions to achieve those goals are carried out.

Kaplan and Norton noted two very important preliminary findings of the employment of BSC:

Fig.1: The Balanced Scorecard links performance measures (from Kaplan & Norton, 1992)



1. BSC "brings together, in a single management report, many of the seemingly disparate elements of the company's competitive agenda…"

2. BSC helped to determine if improvement in one area was achieved by sub-optimization in another area.

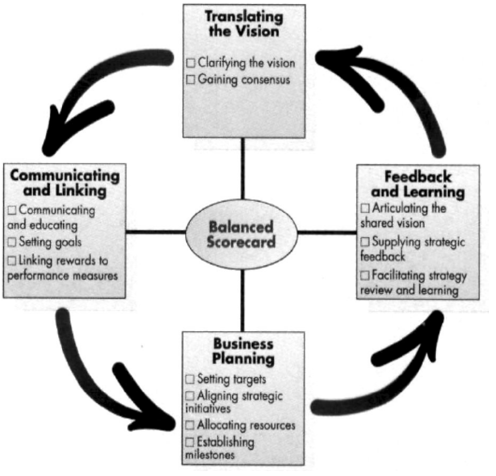
Definitely, BSC was the first original, logical and simple measurement system and had drawn great interest, both among academics and practitioners. But despite its popularity and great implementation rate, many difficulties associated with the design and implementation appeared, generally because of the vague definition, which lead to free interpretation, simple "causality" between the four perspectives that was not deeper explained and with no precise advices given about the design and implementation of the Balanced Scorecard. Associated literature confirmed the originality and utility of the concept [10], but also noted many imperfections in the initial design and recommended further improvements.

III. Balanced Scorecard as a new strategic performance management system

However, immediately after the first HBR article many managers employed BSC in their companies. Despite the implementation and design problems, most of them noted that not only that BSC provides a wider and more comprehensive picture of the company's future by putting their focus on the key drivers of future performance instead of past performance, but it also secures a framework for some core management processes such as: goal setting, resource allocation, planning and budgeting, strategic initiatives and feed-back and learning.

The confirmation of the strong link between performance measures and future desired company destination was initiation signal for the authors to enhance BSC and to identify its second evolution phase from performance measurement reporting tool to a strategic management system. Four new management processes were introduced in their 1996 HBR article "Using the Balanced Scorecard as a Strategic Management System": translating the vision, communicating and linking, business planning and feedback and learning (see figure 3).

Fig.2: Managing strategy:
four processes
(from Kaplan & Norton, 1996)



"Translating the vision" management process was intended to help managers with the crucial problem that "lofty vision and strategy statements don't translate easily into action at the local level" [11] by gaining consensus on how to clarify the vision and company strategy and by identifying strategic objectives in each perspective. "Communicating and linking" process was intended everyone in the organizations to become familiar with the company strategy and objectives and to ensure strategic alignment between the different business units and individuals working there. For that purpose departments and individual scorecards were introduced as a result of the cascade process of BSC. Third process known as "Business planning" was consisted of setting targets and milestones and synchronizing and aligning strategic initiatives and resources to them in order to enable achievement of the strategic objectives. The last one "Feedback and learning" was intended to provide a monitoring of the progress of the short-term departmental and individual results in each perspective against targets and to enable evaluation of the strategy.

Also further improvements were made on simple "causality" between the four perspectives, only mentioned in the first phase. Many BSC designs began to utilize linkages between the strategic objectives across the perspectives. These cause and effect relationships have been developed in order to identify the key performance drivers that ultimately will lead to execution of the strategy. The representation of explicit causality at first, between the measures known as "Strategic Linkage Model" and later in 2001 between the strategic objectives known as "Strategy Map", became an increasingly important element of BSC design. These improvements had rounded the picture of BSC as new strategic management system away from a simple performance measurement tool.

IV. Toward an all-encompassing strategic and control system

Fortunately, Kaplan and Norton didn't stop there. Astonished by the results from a research conducted in 1999 that "70% to 90% of effectively formulated strategies were poorly executed" [12] they started their own research on 250 companies that had already implemented BSC and were members of their Balanced Scorecard Collaborative.[9] They found out that "of 250 companies, 125 said that it is too early to tell the impact of the scorecard, and from the other 125, 19 reported to have achieved significantly better results, 80 said they saw some progress and 26 said they had limited or no better results" [13]. When they drilled dipper into to identify the major differences between the "good" and "bad" strategy executors, they concluded that companies who achieved solid results had better understanding for the importance of performance management processes or scorecard, had utilized strategy maps more, and had significantly more extended communication with their employees, which was a great confirmation of the practical importance of BSC if it is implemented correctly. Motivated by these findings they went even further in the improvement on the BSC. Several new ideas were introduced in their new books The Strategy- Focused Organization (2001) and Strategy Maps (2003).

"Destination Statement" was the first additional innovation in the BSC design. The authors had noticed that despite of the common understanding and defining of the company strategy, members of the management teams still had problems when began operationalizing it through selection of strategic objectives and targets and their linking in the system. As a solution to this problem the Destination Statement was developed to secure and to show a clear picture about what is company trying to achieve and what it is likely to look like at an agreed future date. This new element in the BSC design was intended to provide final consensus about these matters among managers before they will start to select the objectives and to articulate hypotheses of causality.

The second and probably one of the biggest enhancements of BSC had been done by introducing the "Strategy Map" concept. (See Figure 4) It was a logical architecture that defined the strategy by specifying the relationships between shareholders, customers, internal business processes and capabilities. A strategy map was providing a one page visualization of the strategy with precise overview of the objectives of each perspective and their integration and combination toward execution of the strategy. This enabled better communication through the organization, improved employees' understanding and awareness of strategy and allowed better execution and management of the strategy. "The most important broadening of the role of BSC in the strategic process is the concept of "strategy map" in which the scorecard is the primary basis, not just for articulating the strategy of the company, but also for conceptualizing how the strategy works in terms of underlying dynamics through which strategy drives performance" [14].

A prove to the previous statement is Kaplan and Norton's new article "The Office of Strategy Management" (2005) in which they suggested "establishing of a new corporate-level unit, an Office of Strategy Management (OSM)" [15] with prime responsibility for managing strategy by execution of nine processes: Scorecard management, Organization Alignment, Strategy Communication, Strategy Reviews, Initiative Management, Strategy Development and Update, Planning and Budgeting, Employee Alignment and Knowledge Management. The OSM should be consisted of 6-10 employees depending of the organization complexity and should report directly to the CEO. The OSM is intended to ensure that all previously uncoordinated, unaligned or disparate management processes to be performed in an integrated manner.

9) The Balanced Scorecard Collaborative was established in 1999 by Kaplan and Norton to provide support, training, education and research for the companies that are interested in the system - www.bscol.com

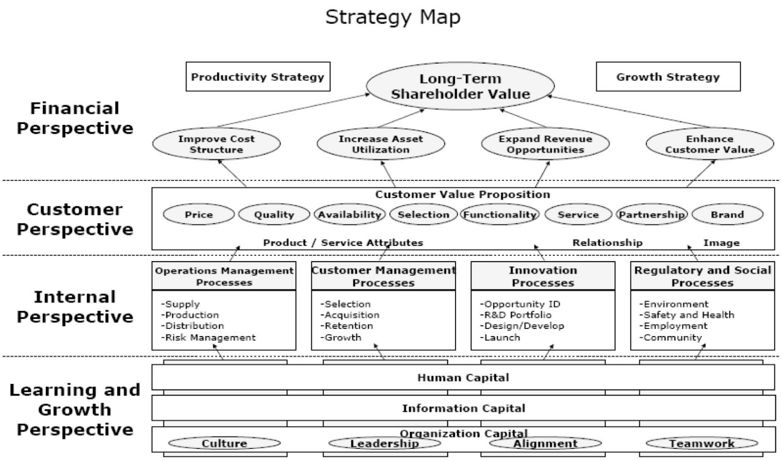


Fig. 3: Strategy Map (from Kaplan and Norton, 2003)

V. Reported results of Balanced Scorecard implementation in the companies worldwide

The Balanced Scorecard has been successfully implemented in almost all types of organizations: large, medium and small, production and services, public and private, profit or nonprofit organizations. Research shows that 60 per cent of Fortune 1000 companies have experimented with BSC [16], and U.S. Gartner Group predicted 60 per cent of all U.S. large companies had adopted BSC by the end of 2000, and 85 per cent of the companies will have performance measurement initiatives underway by the end of 2004 [17]. A Finnish survey found that 31 per cent of the responding companies had some kind of BSC system, and another 30 per cent were implementing one [18]. Also approximately 75 per cent of the European companies that had been surveyed had changed their measurement system in the last three years and are expecting to continue with the changes in the future [19].

Definitely, Robert Kaplan and David Norton have been, and remained among the most influential authors in the field of Performance Management. Their Balanced Scorecard still is the most popular concept in this field that has swept the business world. But despite its apparent popularity, only limited systematic and relevant research-based evidence on the BSC efficiency exists. Most of them are isolated successful company cases (Mobil, Siemens, Motorola, Hilton, BMW) that Kaplan and Norton collaborated with during the implementation process, or after as clients of their consulting firm. Nevertheless, there is no doubt that their research results are relevant, but because of the fact that they are inventors and promoters of the concept, and in order to avoid any suspicion that their results can be influenced by their work, we will refer only to other independent research done last few years. One of these is the research carried out by Lawson, Stratton and Hatch in 2003 on 150 manufacturing, service and governmental companies to explore the benefits that scorecard concept provides.[10] The results were that almost two-thirds of the surveyed companies agreed that significant benefits had been realized from using of scorecard system. They reported that as a result of appropriate alignment of the employee behavior and communicating the strategy through the organization, which are the basic objectives of scorecard system, they achieved "reduction in over-heads of 25% for the last three year, significant improvement in employee satisfaction and the highest sells and profit ever" [20].

Another case that confirms the benefits of the employment of BSC concept is the experimental study performed by Davis and Albright in retail bank. They found evidence of superior financial performance of the brunches that implemented BSC when compared to branches that didn't [21]. A clear relationship between

10) The authors use the term "scorecard system" to include both scorecard as control tool and process, or technique, of integrating the scorecard system into the over-all performance-achievement cycle of the firm.

non-financial measurement and financial performance was found in the study of a hotel chain performed by Banker [22]. Very interesting findings have been reported by Ittner and Larcker, probably two of the most influential researchers in the field of performance management systems. In their study of financial services companies in U.S., they concluded that companies using non-financial measures generally have higher stock market return and higher measurement system satisfaction [23]. In their next study on the importance on building and verifying causal models undertaken on 157 companies they noted that "Businesses that do not scrupulously uncover the fundamental drivers of their units? performance face several potential problems. They often end up measuring too many things, trying to fill every perceived gap in the measurement system" [24]. They confirmed that companies that use valid and well-established causal model as a base for decision making process in average have higher return then the other companies.

However, we shall feel irresponsible not to mention results from some other research. Apart from many successful cases of BSC users, and grate rate of its implementation among the companies worldwide, BSC implementation is not easy or naive process. First, recent studies showed that implementation of performance measurement systems such as BSC can last between 18-24 months [25]. Second, in another research on 15 companies in Northern Europe was concluded that only half of the companies have succeeded to implement BSC. The authors also noted that their results have been supported with similar findings in the research of Venkatraman and Gering: "there have been as many unsuccessful implementations as successful ones" [26].

VI. Results from BSC employment in Republic of Macedonia

During 2007 and 2008 we conducted a planned survey in order to explore the employment of the most widely used performance measurement tools and management techniques for improving business performance such as BSC. A structured questionnaire (previously pretested on a smaller subset of target respondents) was used as a research method on 52 Macedonian companies deliberate selected from almost all types of organizations: large, medium and small, production and services, public and private, successful and less successful.

The results show us that all of the surveyed companies have already defined company strategy. Most of them (nearly 81% of the companies) actively or partly have involved their employees in defining company's strategy, so we can conclude that in most companies employees are acquainted with it. Only 10% of the managers quoted that their employees didn't know the company strategy. Even though 75% of the managers are claiming they have defined specific goals and targets for each organizational unit or responsibility center and that they are following their achievement in the real time, still when they were asked to point out at least 3 most important operations or working processes for the future of their company, only 50% of them did it. This can be seen as a symptom that Macedonian managers in order to ensure themselves that are taking control over their companies, they are tracking many things, but not those essential for the company success. This allegation was confirmed with the results of the question about the number of financial or nonfinancial indicators they are using in everyday working. Most of the small companies' managers have noted that usually they are using between 6-10 key performance indicators, while medium-sized and large companies' managers underlined between 11-15 KPIs and more then 15 KPIs chronologically. Also nearly 82% stated that they would reduce their number if they can.

Although these results definitely are corresponding with the world most cited reasons for the evolution of BSC concept, still the Macedonian implementation results are not in accordance with the rest of the world. Only 6 from 52 companies or around 11.5% of the surveyed companies are using BSC as a strategic management tool for improving its business performance[11] (Table 2).

11) Five of this six BSC users are ranked by Euro Business Center - Skopje as one of the 200 Largest and Most Successful Companies in Macedonia by several financial indicators, gathered from authorized financial institutions in Republic of Macedonia.

Table 2. Balanced Scorecard Users in Republic of Macedonia

BSC users in Macedonia	Industry	Ownership	Company Size	1st Year BSC Influence on Company Profitability	Long Term Profit Expectations under BSC Influence
1	Telecommunications	Foreign investor	Large	Inconsiderably increased	Considerably increased
2	Telecommunications	Foreign investor	Large	Not changed	Considerably increased
3	Banking and Finance	Foreign investor	Large	Inconsiderably increased	Considerably increased
4	Production	Domestic investor	Medium	Not changed	Considerably increased
5	Transportation	Public owned	Large	Inconsiderably increased	Considerably increased
6	Consulting and Training	Domestic investor	Small	Not changed	Considerably increased

We have to admit that this BSC implementation rate (11.5%) is far from the US (around 85%) and European average (around 75%). But maybe more important is to determine the key reasons for such results. If we go further in our survey we can conclude that most of the managers have stated that are not familiar with this performance tool (20 managers) or they are interested in and would like to implement it but are not prepared because of the financial issues (8 companies), lack of know-how (18 companies) or lack of time (6 companies).

Of course the implementation time and efforts can significantly be reduced by using one of the many professional BSC software that are offered on the market, or by using help from academics, professionals and consultants. But definitely in order to achieve ultimate results that can be provided by the employment of the BSC, managers should be prepared to carry out many changes in their organizations such as: to implement the BSC throughout the whole organization, carefully to determine the key drivers of their success and to link them with the strategy, to secure better transparency, to be able to understand, discuss and educate their employees how managers derive their metrics and their inter-relationship, to focus their decision-making process primary on execution of the strategic objectives, to motivate the employees to strive for top performance results and many more. Only if companies are using BSC as a learning tool not just as a control tool they can achieve ultimate results.

The BSC enables a focus on long-term growth versus a short-term focus on quarterly or even monthly results. BSC extend or improve financial measures and its short-term focus on company's results and performance. Actually, BSC provide balance between long-term and short-term goals and contribute to their achievements. Gumbus and Lussier [27] have summarized six ways on which BSC helps an organization:

1. Promotes growth - due to focus on long term strategic outcomes, not just short-term operational results.
2. Tracks performance - individual and collective results can be tracked against targets in order to correct and improve.
3. Provides focus - when measures are aligned to a few critical strategies, the BSC provides focus on what is important to the company.
4. Alignment to goals - when you measure what is truly important to success, the measures become linked and support each other. Alignment occurs across the organization.
5. Goal clarity - the BSC helps respond to the question, "How does what I do daily contribute to the goals of the enterprise?"
6. Accountability - individuals are assigned as owners of metrics in order to provide clear accountability for results.

As BSC still continue to evolve as a flexible concept we would like to use the opportunity to suggest further research directions:

-What are the experiences of the employment of BSC in the companies from our neighboring countries such as Pliva, Ericsson Nikola Tesla, Podravka, Elektrokontakt, Megatrend? There are very few modest researches done in the field of performance measurement and management among these countries even though all of them strive to enter EU, known as highly competitive global market where most of their competitors have already done a lot of improvements.

If we, as academics, feel responsible for our economy results and for our companies' performance, at least what we can do, is to introduce to companies and whole business environment the latest achievements in this field and to explore that few cases of BSC employment, so we can present the results and attract attention of many others that are not familiar with this concept.

VI. Conclusion

Balanced Scorecard concept, when developed 14 years ago, significantly differed from any other performance measurement system and attracted impressive attention, both among academics and practitioners. Initially, it was introduced as performance measurement tool that can be successfully used to avoid financial measurements' short-termism by balancing it against a customer perspective, an internal business perspective and innovation and growth perspective. Linked in an integrated set of unique strategy objectives, translated through clearly defined metrics and targets, BSC enables company's strategic goals to be cascade down in the organization so any department or employee has its own set of measurable objectives. "The creation of a system of measurement that would enable companies to keep track of many dimensions in a systematic way is an incredibly powerful concept" [28], that in 1997 Harvard Business Review labeled it as one of the 75 most influential ideas of 20th Century. By putting the strategy at the center of the performance measurement system, BSC became an effective tool not just for articulating the strategy of the company, but also for conceptualizing how does it work, and soon had evolved into a strategic management system with a clear ambition for developing further toward an all-encompassing strategic and control system. As a concept which declares great flexibility and success, it should encourage the managers from our countries to consider employing the effective insights gained so far.

Republic of Macedonia is a country in transition. As each country that began with the process of privatization in late eighties, many processes lagging in Macedonian practice. Few years ago foreign investors started to invest in Macedonia. Now we have stock exchange with numerous foreign investors and it is reasonable that companies in RM should follow world trends in overall business operations and consequently to follow latest trends in performance measurement. From our up to now experience we can make general conclusion that only in companies with foreign investors, performance measurement approaches are practiced. As precede phase of performance measurement, companies have divided themselves into responsibility centers (cost, revenue, investment). Further, few companies even practice some performance measurement system but it is either focused on financial measures or its non-financial measures are not in relation with company's strategy and overall objectives. Other general conclusion that could be made is using of financial measures as means for measuring performance of responsibility centers and company in a whole. Such financial measures are included and calculated only for the requirements of internal reporting to managers. But, with entering foreign investments in RM, obvious is the trend in Macedonian companies to research for the most appropriate performance measurement system. Although, the sequence of things should be reverse, firstly to implement particular performance measurement system in order to prepare reliable information for investors and on that way to attract investors, the important fact here is that companies have started to look for "the best" performance measurement system and ways on which it could be implemented. In fact, foreign investors impose requirements to domestic companies to implement performance measurement systems. Although performance measurement in RM is in its early stage, actual is the effort from academicians and practitioners to stimulate and to help domestic companies to use reliable performance measurement and reliable reporting on it. Even more, in this period of financial and economic crises that Macedonian companies can also feel, the implementation of performance measurements systems is more essential and important. Companies have to be encouraged to invest in performance measurement systems and to implement them as a tool for detecting inefficiencies in their operations, price variances, analyzing customers needs, reducing costs and their better allocation, altering and innovating products etc. All of these opportunities help to be achieved two goals on which companies are most focused these days: improving companies' performance and better crises overcoming.

REFERENCES

[1] Bontis, N., Dragonetti, N.C., Jacobsen, K., and Ross, G., "The Knowledge Toolbox: A Review of the Tolls Available to Measure and Manage Intangible Resource", European Management Journal, Vol.17, No.5, pp.391-402, 1999

[2] Kaplan, R.S. and Norton, D.P., "The Balanced Scorecard-Measures that Drive Performance", Harvard Business Review, Vol. 70, pp. 71-79, 1992

[3] Neely, A.D., Business Performance Measurement: Theory and Practice, Cambridge University Press, Cambridge, 2002

[4] Keegan, D.P., Eiler, R.G. and Jones, C.R., "Are Your Performance Measures Obsolete?", Management Accounting, Vol. 70, No.12, pp. 45-50, 1989

[5] Lynch, R.L. and Cross, K. F., Measure Up! The Essential Guide to Measuring Business Performance, Mandarin, London, 1991

[6] Fitzgerald, L., Johnston, R., Brignall, S., Silvestro, R. and Voss, C., Performance Measurement in Service Business, CIMA, London, 1991

[7] Kaplan, R.S. and Norton, D.P., "The Balanced Scorecard-Measures that Drive Performance", Harvard Business Review, Vol. 70, pp. 71-79, 1992

[8] Neely, A.D., Adams, C. and Kennerley, M., The Performance Prism: The Scorecard for Measuring and Managing Business Success, Financial Times-Prentice Hall, London,2002

[9] Neely, A.D., Mills, J.F., Manufacturing in the UK-Report on a Survey of Performance Measurement and Strategy Issues in the UK Manufacturing Companies. Manufacturing Engineering Group, London, 1993

[10] Epstein M.J. and Manzoni J.F.: "The Balanced Scorecard and Tableau de Bord: A Global Perspective on Translating Strategy into Action", INCEAD Working paper, 97/63/AC/SM, 1997

[11] Kaplan, R.S. and Norton, D.P., "Using the Balanced Scorecard as a Strategic Management System", Harvard Business Review, January-February 1996

[12] Charan, R. and Geoffrey, C., "Why CEO's Fail?", Fortune, June 21, pp.68-78,1999

[13] Waal, A.,"The Future of the Balanced Scorecard: An Interview with Professor Dr. Robert Kaplan" Measuring Business Excellence, Vol. 1, No. 7, pg.30, 2003

[14] Grant, R.M, "New Directions in Strategic Management", Business Strategy Review, Vol.12 No.1, pp.61-67, 2001

[15] Kaplan, R.S. and Norton, D.P., "The Office of Strategy Management", Strategic Finance, Vol. 87, No.4, pp. 56-60, 2005

[16] Silk, S., "Automating the Balanced Scorecard", Management Accounting, Vol. 79, No. 11, pp. 38-44, 1998

[17] Neely, A. and Al Najjar, M., "Management Learning Not Management Control: The True Role of Performance Measurement", California Management Review, Vol. 48, No. 3, pp. 100-114, 2006

[18] Malmi, T., "Balanced Scorecard in Finnish Companies: A Research Note", Management Accounting Research, Vol. 12, No. 2, pg. 207, 2001

[19] Gates, S., Aligning Strategic Performance Measures and Results, N.Y: The Conference Board, New York, 1999

[20] Lawson, R., Stratton, W. and Hatch, T. "The Benefits of A Scorecard System", CMA Management, Vol. 77, No. 4, pp.24-26, 2003

[21] Davis, S. & Albright, T. "An investigation of the effect of Balanced Scorecard implementation on financial performance" Management Accounting Research, 2004

[22] Banker, R.D., Potter, G., Srinivasan, D., "An empirical investigation of an incentive plan that includes non financial performance measures" Accounting Review. Vol. 75, No. 1: pp. 65-92. 2000.

[23] Ittner, C., Larcker, D. and Randall, T. "Performance implications of strategic performance measurement in financial firms",. Accounting, Organizations and Society, Vol. 28: pp. 715-741. 2003

[24] Ittner, C. and Larcker, D. "Coming Up Short on Non financial Performance Measurement" Harvard Business Review, November: pp. 88-95. 2003

[25] Bourne, M., Mills, J., Wilcox, M., neely, A. and Platts, K. "Designing, Implementing and Updating Performance Measurement Systems", International Journal of Opertaions & Production Management, Vol. 20, No. 7, pp.754-771, 2000

[26] Olve, N-G., Petri, C-J., Roy, J. and Roy, S. "Twelve Years Later: Understanding and Realizing the Value of Balanced Scorecards", Ivey Business Journal, London, May-June, pg.1 2004

[27] Gumbus, Andra and Lussier, Robert N. (2006): "Enterpreneurs Use a Balanced Scorecard to Translate Strategy into Performance Measures", Journal of Small Business Management, 44 (3), pp. 407-425

[28] Bontis, N., Dragonetti, N.C., Jacobsen, C., and Roos, G., "The Knowledge Toolbox: A Review of the Tools Available to Measure and Manage Intangible Resources", European Management Journal, Vol. 17, No. 4, pg 396, 1999

UDC 336.717.15(497.7)

ASSESSMENT OF THE SERVICE QUALITY IN MACEDONIA'S BANKING SECTOR

Marina Topaloska, MBA

Abstract

Service quality and costumers satisfaction have been widely described as related constructs in the literature. Some of the scholars have even characterized them as a single construct. In high involvement industries, like banking, the quality of the service appears to be a prerequisite for success.

In cognizance to the relative paucity of studies on the banking industry in Macedonia, in the context of service quality, this paper attempts to contribute in this regard by focusing on the service quality issues in Macedonia banking sector. This was accomplished by applying the service quality measures developed by Parasurman et al(1985) .The current study focuses on retail costumers, thus, generalization to the corporate group should be done with caution.

Key words: *service quality, customer satisfaction, banking industry*

I. Introduction

Intensifying competition and rapid deregulation are significantly changing the banking environment throughout the world. Within this rapidly changing environment, banks are consistently seeking for profitable ways to differentiate themselves. To accomplish this, most of the banks are now turning their attention to customer satisfaction and service quality.

The objective of the research was threefold- (1) to evaluate the applicability of the five-dimensional service quality construct on measuring customer satisfaction (2) to investigate the service quality impact on price awareness (3) to determine how price awareness affects customer satisfaction.

This paper is divided into six sections. The first section presents brief literature review of the definition and measurement of service quality, and the academic findings on price. The second section deals with the questions of the research. The subsequent sections discuss the data collection, descriptive analyzes and purification procedures. (Section 3 to section 6).The final section proceeds with some conclusive remarks regarding the study, limitations, implications and suggestions for further research.

II. Literature review

2. 1 Service Quality

Traditionally, service quality has been given paramount attention in the banking sector, since they were offering products which are difficult to differentiate, thus, placing great value on customer relationship.. (Angur et al 1999; Allred & Addams.H,2000) As Soteriou. A & Zenios. S (1997) declared "customer-perceived quality as the driver of retail banking in the 1990s"(.p 5)" In today's rapidly changing environment, factors such as deregulation and increased competition have contributed even further to the importance of customer satisfaction and service quality for all banking institutions.

Great attention has been dedicated to the service quality concept and its impact on various aspects, most remarkably its apparent relationship with customer satisfaction. (Parasuraman,Berry, & Zeithaml,1985; Iacobucci et al,1995,) The vast majority of literature describes this concept as a matter of attitude, perception and subjectivity. As Zeichmal (1988) defines "it is the consumer's judgment about a product's overall excellence and superiority" (p.3). Thus, academics have been referring to this concept as a comparative function of customer expectations and perceptions of the actual service performance. (Parasuraman et al, 1994 p.146) When expectations exceed the actual service performance, there is an unsatisfactory perception of service quality. Customer satisfaction has been defined in similar terms "a function of the discrepancy between a consumer's prior expectations and his or her perception regarding the purchase"(Iaccobuci et al p.278,). The customer satisfaction literature, describes this model as "Disconfirmation Paradigm", whereas writings on service quality, have been referring to this model as "Gap Model".

On the other hand, there have been some researchers arguing that the analogous conceptualization of quality and satisfaction is not appropriate.(Parasuraman et al[12].,1985 p.16; Iacobucci et al) In addition, Iacobucci et al (1995) founded that there other service attributes that affect customer satisfaction, other than service quality: timeliness and price. (p.293)

Various service quality' measurement approaches have been developed over the years, which are still subject to controversy. For instance, the SERQUAL model developed by Parasuraman Zeithaml and Berry (1985), has been exposed to several criticisms regarding its validity (Cronin and Tylor 1994, Bahia & Nentel, 2000) For example, Cronin and Tylor(1992,1994) argued that measuring only performance is more suitable approach (SERVPREF) Nevertheless, the SERVQUAL model has been extensively adopted by researches, making its multidimensional approach widely supported throughout the literature. Thus, it has been accepted that customers evaluate service quality in terms of both: the process and the outcome of service received. (Allred.A & Addams.H,2000. pg 201). The model is a five dimensional construct of perceived service quality, with 22 items developed to measure the degree of discrepancy between customer's expectations and perceptions.

- Tangibles
- Reliability
- Responsiveness
- Assurance
- Empathy

In this sense, perceived quality is measured as a gap between expectation and the actual performance. The measurement is designed as a continuum ranging from best quality to totally unacceptable quality (Sachdev.S & Verma.H,2004,p.98).

2.2 Price awareness

Limited numbers of researches have been examining the importance of price awareness.

In a study conducted by Zeichmal.V,(1988), it was found that price awareness is of greater importance for services, durable goods and packaged goods, and that the level of price awareness tends to be greater for female, married, home-working woman.(p.11)

12) Parasuraman et al (1985) view satisfaction as a specific, shot-term phenomenon, and quality as long term, broad criteria

Furthermore, distinction between objective[13] and perceived price.[14] Was made in the literature.(Jacoby and Olson ,1977, cited in Zaithmal.V 1988) In addition, they suggest that people do not always remember the actual price, rather, they may encode price in their own-justified manner. However, for a consumer to have accurate internal reference price, customer attention, awareness and knowledge of prices appear to be considerably important. (Zeithmal.V ,1988) It has been argued that priming affects both categorization and judgment and that only judgment about price is affected by priming effects.(Herr.P,1989. p.69)

Lichtenstian et al(1988) suggested that price acceptability is influenced directly by price consciousness and product involvement, or indirectly trough the formation of price-quality inferences.(p.249) Both, priming and price acceptability emphasize the importance of knowledge structures in memory and judgment. (Kangis. P and Passa.V,1997 p.106) In many cases, "customers may decide to forgo reconsideration or even first consideration… and simply retrieve the attitude they formed during the first processing… "(Charttopadhyay. A and Alba. J, 1988 p.5)

All of these concepts are correlated, and should be taken into consideration when evaluating the effects of price.

2.3 Price as indication of quality

Considerable research has been dedicated to the relationship between price and quality.

(Zeithmal, 1988 and Herr.P,1989). However, scholars suggested that this relationship is: nonlinear in nature (Peterson,1970 p.526) , personal construct (Sharpo,1973 p.289) and usually weak (Zeithmal,1988 p.11) Other studies have shown that price is used as quality cue to a greater degree when brands are unfamiliar than when they are familiar (Zeitmal 1988 p.10)

3. Research question

The aim of the project is to establish the extent to which (a) service quality affects customer satisfaction in Republic of Macedonia's banking sector (b) the influence of the five dimensional service quality construct on price awareness (c) to determine the relationship between price awareness and customer satisfaction.

Hypothesis 1: There is a positive relationship between any of the service quality dimensions and customer satisfaction.

The research hypotheses were stated as follow:

- H 1 (0) Tangibility positively affects customer satisfaction
- H 1 (1) Reliability positively affects customer satisfaction
- H 1(2) Responsiveness positively affects customer satisfaction
- H 1(3) Accuracy positively affects customer satisfaction
- H 1(4) Empathy positively affects customer satisfaction

If any of the research hypothesis is supported, that hypothesis 1 will be accepted. This is based on foundation that service quality can be considered as a one-dimensional construct(Cronin and Taylor, 1994) and on the premise that not all service quality dimensions are important to customers(Verma.H and Sachdev. S,p. 105) We expect Hypothesis 1 to be acceptable , based on the literature , where the two constructs have been widely accepted to be interrelated . (Parasurman et al 1988.pg. 16)

Hypothesis 2: Service quality will impact the awareness that customers have regarding the bank charges.

The hypothesis is expected, based on the literature indication that customers refer to price as a cue of quality

13) The actual price of a product
14) The encoded price of the consumer

Hypothesis 3: Increased level of price awareness will positively affect customer satisfaction.

The hypothesis is expected, based on the premise that informed customers are more satisfied with the service of the bank. (Passa and Kangis,1997,pg.117)

4. Methodology

The collection of the original data was conducted among the costumers of the two largest and well-known banks in the area of Skopje, Macedonia. The data for the study was obtained trough a questionnaire. The survey procedure was divided among the two researchers, each distributing 50 questionnaires in two different banks.(total of 100 questionnaires) among the costumers of "Komercialna Banka" , which was one of the selected banks and the costumers of "Tutunska banka."

The questionnaire consisted of three sections, obtaining data on personal information, customer evaluation of the five quality dimensions and overall satisfaction.

The first section of the questionnaire consisted of demographic questions, determining consumer's age, sex, marital status, education and income.

The second section of questionnaire, was measuring service quality, identified by the five dimensional variables. It was decided, evaluations to be based on SERVQUAL model (Parasuraman et al. 1985), as a concise multiple scale with good reliability and validity, measuring perceived service quality. For clear and simple measurement, the instrument was shortened from 22 to 20 attributes. Each item of service quality was measured on a seven-point Likert scale." A seven-point scale ranging from "strongly agree" (7) to "Strongly Disagree" (1), with no verbal labels for scale points 2 trough 6, accompanied each statement. "(Parasuraman et al,1985, p.17)

This scale evaluated five dimensions of quality: Tangibility, Reliability, Responsiveness, Assurance and Empathy. The items concerning the variable of tangibility were adjudged by the features such as appearance of the personal, physical facilities and tidiness of the branch. Reliability was defined by the ability of the bank to perform its statements accurately, and its on-time performance of service. Responsiveness was determined by the willingness of personnel to help customers, to organize queries and to prompt service. Assurance variable was defined by the knowledge and courtesy of employees and adequacy and of explanations of services offered. The empathy variable represented the individualized attention the bank's to its customers, the convenience of opening hours and the provision of information on interest rate charges.

In the last section, respondents were asked more generally to indicate their overall level of satisfaction with their bank, as well as their price awareness before receiving the service.

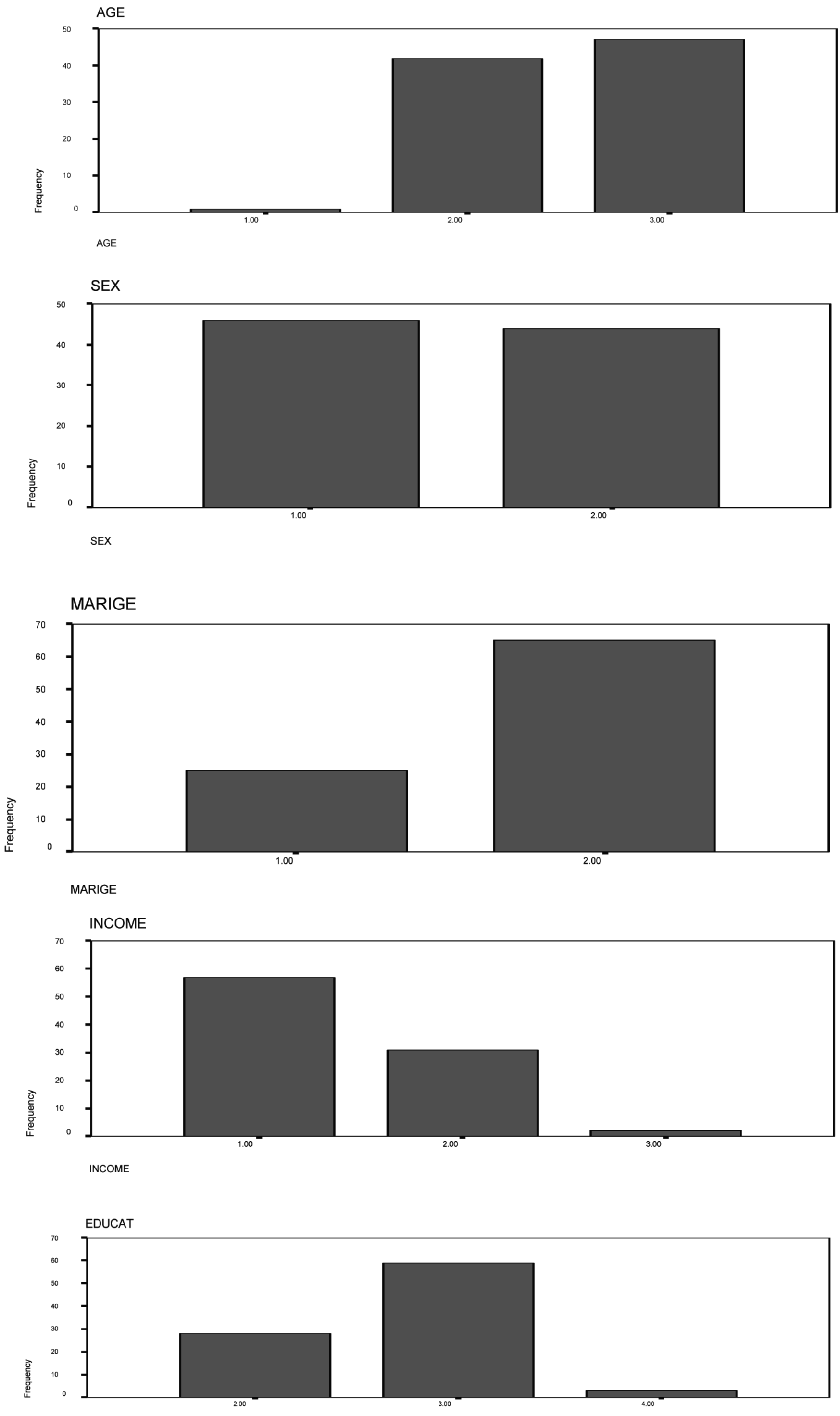
5. Descriptive analyzes

5.1 Demographic Data

The respondents in the survey had the following traits:

- The majority (89 respondents) were in the age range of 18-65. Of this group, 47 were in the age between 41-65, whereas the other 42 were in the 18-40 age group.
- There were almost as many women (44 respondents) as man (46). Of this, 25 respondents were reported as single, whereby 65 of them were married.
- There were almost as many women (44 respondents) as man (46). Of this, 25 respondents were reported as single, whereby 65 of them were married.
- When asked about their income status, 57 of the surveyed reported earning bellow 500€ per month, 31 reported in the category of 500-1500€, only 2 described themselves as earning from 1500-3000€, there was no responded earning more than 3000€
- In terms of educational level, 28 of the surveyed have finished high-school, 59 reported as B.A graduates, and 3 of them have taken master or another degree.

Figure 1: age, gender, income, marital status, educational level of respondents



5.2. Measures

The findings from the survey indicate that from all service quality questions, highest mean values were found for the items representing the following dimensions Please refer to the model presented below.

	Item	Mean Value
Assurance	The clarity and adequacy of explanations	5,2000
Responsiveness	The willingness of the stuff to help	5,1556
Tangibility	The availability of adequate equipment	5,1222

This results signify the areas in which customers valued the bank's performance most satisfactory. In addition to this findings, highest score for each of this questions was: assurance(6 with 28,9) responsiveness(6 with 28,9) and tangibility(5 and 6 with 25.6%).

In contrary to this, lowest mean values were reported for the items representing responsiveness and tangibility

	Item	Mean Value
Responsiveness	(3) The availability of immediate service for older client	3,2278
	(2) The willingness to help, without the client asking for it	3,4489
Tangibility	(2) The simplicity level of the documentation procedures	3,5222

These results indicate the areas in which the customer evaluated the performance of the bank at the lowest level. Highest percentage of the respondents assessed each of this question with: responsiveness-question 3 (2 with 26,7%) responsiveness-question 2 (3 with 26,7%) and tangibility (4 with 21,1%).

The conflict of these findings, in the area of tangibility and responsiveness, may further affect the establishment of clear relationship among this dimensions and the dependent variable. Also, this may create difficulties in the finding clear factor patters for the particular dimensions.

Figure 2: Frequencies, means, and standard deviations of measures

Label	Frequency (% of cases) 1	2	3	4	5	6	7	Mean	St. Dev.
Q1 Tang 1		3.3	15.6	16.7	26.7	31.1	6.7	4.8667	1.2913
Q2 Tang 2	12.2	17.8	18.9	21.1	17.8	11.1	1.1	3.5222	1.5881
Q3 Tang 3	2.2	8.9	5.6	20.0	22.2	32.2	8.9	4.8333	1.5009
Q4 Tang 4		6.7	7.8	15.6	25.6	25.6	18.9	5.1222	1.4443
Q5 Rel 1	5.6	4.4	10.0	12.2	27.8	26.7	13.3	4.8556	1.6184
Q6 Rel 2		10.0	8.9	21.1	24.4	28.9	6.7	4.7333	1.4046
Q7 Rel 3	5.6	10.0	10.0	17.8	21.1	15.6	20.0	4.6556	1.7999
Q8 Rel 4	11.1	13.3	20.0	31.1	13.3	8.9	2.2	3.5778	1.5064
Q9 Res 1	1.1	2.2	13.3	11.1	25.6	28.9	17.8	5.1556	1.4214
Q10 Res 2	7.8	20.0	26.7	21.1	11.1	12.2	1.1	3.4889	1.4934
Q11 Res 3	12.2	26.7	16.7	23.3	10.0	8.9	2.2	3.2778	1.5796
Q12 Res 4	7.8	13.1	30.0	11.1	18.9	13.3	5.6	3.8222	1.6597
Q13 Assu 1		2.2	14.4	11.1	24.4	28.9	18.9	5.2000	1.3837
Q14 Assu 2		6.7	11.1	23.3	32.2	15.6	11.1	4.7222	1.3494
Q15 Assu 4	1.1	5.6	13.3	14.4	22.2	25.6	17.8	4.9889	1.5324
Q16 Emp 1	2.2	10.0	13.3	17.8	21.1	27.8	7.8	4.6000	1.5564
Q17 Emp 2	3.3	8.9	13.3	18.9	20.0	25.6	10.0	4.6000	1.6062
Q18 Emp 3	3.3	10.0	15.6	21.1	25.6	14.4	10.0	4.3889	1.5700
Q19 Emp 4	3.3	6.7	8.9	23.3	24.4	24.4	8.9	4.6778	1.4978
Q20 C. S. 1	3.3	8.9	11.1	22.2	26.7	18.9	8.9	4.5222	1.5304
Q21 P.A. 1	2.2	15.6	17.8	27.8	17.8	15.6	3.3	4.0333	1.4569

Tangibility

For the tangibility dimension, highest response percentage was found for item 3 (32,2% answered 6) ,whereas lowest percentage was found for question 2 (1.1% answered 7). For the first item highest percentage of cases answered 6(31,1) and lowest part of them answered 2 (3,3%). For the second item, highest percentage of respondents answered 4 (21,1%) and lowest part of them answered 7 (1,1%) In the third question, largest part of respondents answered 6 (32,2%) and lowest percentage (2,2%) rated 1. In the final question, 25,6 % of respondents rated 5 and 6 equally, whereas 6,7% answered 2. The low correlation among responses, might latter on affect the relationship we expect to emerge.

Reliability

In the reliability construct, greatest response was found for item 4 (31,1% answered 4), which was also found to have least response rate.(2.2% answered 7) For the first item, 27,8% answered with 5, and only 4,4% answered 2. In the second question, highest percentage circled number 6 (28,9%) and 6,7% circled number 7. In the third item 21,1% responded with 5, and 5,6% responded with 1. In the final item, 20 % answered 3, and only 2,2% answered 7. We can see good correlation among answers in this dimension, in the sense that all of the greatest percentages were distributed among the upper-range of the scale, however, the final question may problematical latter on.

Responsiveness

In the responsiveness variable , highest score was reported for item 4 (30% answered with 3), whereas lowest score was found for both item 1 and 2 equally(for item 1, 1.1% answered with 1, and for item 2, 1,1% answered 7) In the first question, highest percentage answered with 6 (28,9%), and lowest percentage circled number 1 (1,1%).In the second question, 26,7% responded with 3, and 1,1% responded with 7. In the third question, 26,7% replied with 2, whereby 2,2% answered with 7. In the last question, 30% responded with 3, whereas 5,6% answered with 7. Due to the weak correlation in response between the first item and the other three items, difficulties in finding a clear factor pattern might emerge.

Assurance

In the assurance dimension, highest response percentage was found for item 2(32,2% responded with 6), and the lowest response percentage was reported in item 2(2,2% answered with 2).In the first question, 28,9% circled the number 6, whereas 2,2% circled the number 2. For the second item, 32,2% answered with 5, and 6,7% answered with 2. The third item was found as invalid measurement in the factor analyzes. In the fourth question, 25,6% responded with 6, and 1.1% responded with 1. It can be seen that highest response was found for the upper-range of the scale, indicating a good internal consistency of the dimension.

Empathy

For the empathy construct, highest score was registered in item 1 (27,8 % answered with 6), whereas lowest reply was found in item 1 (2,2% responded with 1) In the first item, 27,8% responded with 6, and only 2,2% responded with 1. In the second question, 25,6% answered with 6, and 3,3% answered with 1. In the third item, 25,6% replied with 5, whereby 3,3% answered with 1. In the last question, 26,7% circled number 5, and 3,3% circled the number 1.

6. Results

In order to determine wheatear the five factor conceptualization of service quality is valid in Republic of Macedonia's banking sector, the data was tested into the statistical soft-were package SPSS and checked for any incorrect entries. The service quality data has been analyzed into three stages: by conducting factor, reliability and regression analyzes. To avoid any irregularities (e.g negative eigen values), irrational questioners were excluded from the analyzes, at the end of which, 90 questionnaires were retained.

6.1 Study Purification, First Stage

Examining the dimensionality of the 20 item scale was the first task, and was accomplished by factor analyzing the different scores of each item.

The 5 factor solution was tested with the use of orthogonal rotation. (VARIMAX) Each dimension was considered on separate bases, and every item was factor analyzed. When a particular dimension was providing for a single factor solution, the additional variables composing that dimension were retained. Variables which had insufficiently high loading on more than one factor, were eliminated.

As shown in Table 1, clear factor pattern emerged, since all of the originally five dimensions were providing for a single factor solution. One of the items had high loading on more than one factor, thereby implying that the factors may not be independent from each other. (assurance 3) When this item was removed, the remaining items assigned to each dimension, consistently had high loadings (> 0.5) on only one of the factors extracted. At the end, five factors with eagen values greater than 1 were recognized, all of which had more than one item with a clear pattern of loading. All of this suggests that service quality in Republic of Macedonia's banking sector might have five fairly unique facets.

Figure 3: Summary of results from the factor analysis

Rotated Component Matrix[a]

	Component				
	1	2	3	4	5
TANG1	.371	6.139E-02	-5.02E-02	.708	3.153E-02
TANG2	.288	.185	3.226E-02	.716	7.635E-02
TANG3	5.264E-02	3.309E-02	.150	.813	-1.12E-02
TANG4	-5.09E-02	4.361E-02	.257	.788	.137
REL1	.834	.120	.138	.158	.247
REL2	.814	.252	-6.10E-03	6.215E-02	.117
REL3	.713	.215	7.957E-02	.196	.180
REL4	.721	.162	.192	.144	3.032E-02
RES1	.177	.630	.157	4.990E-02	.337
RES2	.254	.858	.146	-1.56E-02	.153
RES3	.157	.858	3.588E-02	.125	6.927E-02
RES4	.178	.874	4.031E-02	.148	.142
ASSU1	.477	.210	-5.10E-02	7.845E-02	.618
ASSU2	.260	.356	-4.30E-02	.204	.681
ASSU4	7.839E-02	.145	.270	-2.48E-03	.807
EMP1	.255	-1.97E-03	.774	8.648E-02	6.237E-02
EMP2	5.076E-02	6.733E-02	.807	.134	.146
EMP3	-4.40E-02	8.875E-02	.817	6.582E-03	-3.32E-02
EMP4	9.127E-02	.129	.786	.152	6.031E-02

6.2. Study Purification, Second Stage

Because of the multidimensionality of the service quality construct, coefficient alpha needs to be computed separately for each dimension to ascertain the extend to which items making up each dimension shared a common core. (Parasuraman et al, 1985 p.19)

At the second stage, Cronbach's α was calculated to test the reliability of each factor. "A Cronbach's α analyzes led to the deletion of poor items and the improvement of the internal consistency of some factors" (Parasurman et al,1988, p.20) In addition, constructs which are exceeding the recommended alpha value of 0.7, exhibit higher degree of reliability. However, researchers have accepted the lowest reliability of 0,59 and the highest reliability of 0,97 (Karankitikorn. O. 2004, p.8). Table 2 shows the reliability indicators of each of the factors. As it can be seen, the alpha value for each dimension is exceeding 0.7, indicating a good internal consistency among items within each dimension.

Figure 3: Summary of results from the Reliability analyzes

Factor	Chronbach's α	Items
1. Tangibility	0.7957	Tang 1 Tang 2 Tang 3 Tang 4
2. Reliability	0.8533	Rel 1 Rel 2 Rel 3 Rel 4
3. Responsiveness	0.8826	Res 1 Res 2 Res 3 Res 4
4. Emphaty	0.8240	Emp 1 Emp 2 Emp 3 Emp 4
5. Assurence	0.7260	Assu 1 Assu 2 Assu 4

6.3 Study Purification, Third Stage

At the final stage, regression analyzes will be applied to determine the relative importance of each service quality dimension. Critical ratios will be used to evaluate the statistical significance. Parameters which have a critical ratio greater than |1.96| will be considered significant. Based on this criterion, the regression model equation $U = a + b_1x_1 + b_2x_2$ needs to be resolved, in order to determine the relative impact of each statistically significant dimension on predicting the value of the dependent variable.

Hypothesis 1

To begin with, the relationship between service quality and customer satisfaction was tested This was done by regressing the average score for each of the dimensions on the overall customer satisfaction score obtained from each individual surveyed. Table 3 explains the regression coefficients of t-value, significance and standardized beta coefficients.

Only three of the dimensions-Reliability, Assurance and Empathy - were found to have statistically significant relationship with customer satisfaction. No significant relationship was found between the other two dimensions (Tangibility t<|1.96| Responsiveness t<|1.96|) and customer satisfaction. Results indicate that although service quality is a five-dimensional construct, only three of its factors are relatively important determinants of customer satisfaction in Republic of Macedonia's banking sector. The regression equation for the relationship between service quality and customer satisfaction is $U = -2.569 + 7.803X_1 + 2.931X_2 + 2.706\,X_3$.

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-1.325	.516		-2.569	.012
	MREL	.687	.088	.594	7.803	.000
	MRES	7.182E-02	.084	.062	.857	.394
	MEMP	.221	.075	.184	2.931	.004
	MTANG	2.918E-02	.088	.022	.333	.740
	MASSU	.274	.101	.205	2.706	.008

In terms of relative importance, the results show that reliability is the most critical dimension, followed by empathy and assurance.(responsiveness and tangibility have lowest importance) This findings are in compliance to Parasuraman et al (1988) categorization of importance, in the sense that reliability was found to be most importance dimension. However our findings did conflict in the empathy dimension, since they categorized it as the least important dimension. Nonetheless, our findings were in accordance to Verma. H & Sachdev. S (2004) categorization of importance, whose findings indicated that empathy is the most important dimension in the banking sector. (p.109)

Hypothesis 2

In our study, no support was found for hypothesis 2, implying that there is no significant relationship between service quality and price awareness. (Table 4) This signifies that while the bank may be improving its service quality, price awareness will stay unaffected. Thus, we reject hypothesis 2 on the basis that no significant relationship was found existent.

Coefficients[a]

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1	(Constant)	3.557	.892		3.990	.000
	MREL	.125	.152	.113	.820	.415
	MRES	.111	.145	.101	.768	.445
	MEMP	-5.80E-02	.130	-.051	-.445	.657
	MTANG	.125	.151	.099	.828	.410
	MASSU	-.166	.175	-.131	-.950	.345

a. Dependent Variable: P.A

Hypothesis 3

We reject hypothesis 3, on the basis that no significant relationship was found between price awareness and customer satisfaction. In addition, the increased level of price awareness does not influence the level of customer satisfaction. However, given that the error of significance is small and the t-value is close to the critical ratio |1.96|, it may be argued that to some extent, price awareness does affect customer satisfaction.

Coefficients[a]

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1	(Constant)	3.766	.472		7.975	.000
	P.A	.188	.110	.179	1.702	.092

a. Dependent Variable: C.S

7. Conclusion

7. 1 Discussion

The purpose of this small-scale project was to investigate three considerably important questions. Each of the three assumptions is demonstrated trough the models bellow.

- how service quality affects customers satisfaction in Republic of Macedonia's banking sector
- whether improvements in service quality will lead to increased price awareness
- what impact does price awareness have on customer satisfaction

model 1- relationship between service quality and customer satisfaction

model 2-relationship between service quality and price awareness

model 3- relationship between price awareness and customer satisfaction

The five-dimensional service quality framework has been considerably supported trough out the literature. The purpose of this paper was to assess the applicability of alternative measures of service quality in the context of the banking sector in Republic of Macedonia. The study was based on a survey conducted among the customers of the two largest banking institutions in the country, at the end of which 90 respondents were evaluated.

The overall findings of this project, supported the relationship between service quality and customer satisfaction. Thus, our study support the foundation in the literature, in the sense that customer satisfaction and service quality are found to be interrelated constructs even in a developing economy as it is the case of Republic of Macedonia. (Inacobucci. D et al,1995)

In order to test the generalizability of the five factor structure, the service quality data has been analyzed into three stages. At the first stage, factor analyzes were conducted to asses the dimensionality of the 18 items. The results supported the five dimensional concept of service quality recognized in the literature. (Parasuraman et al, 1988) At the second stage the internal consistency of each dimension was examined with the use of reliability analyzes, upon which completion, all of the five dimensions were found to be reliable constructs. At the 'regression analyzes' stage, three of the service quality dimensions were found to have statistically significant impact on customer satisfaction. In addition, reliability, empathy and assurance are the most important facets of service quality, when customer satisfaction is evaluated. The other two dimensions were found to have statistically weak relationship with customer satisfaction. However the low significance of the tangibility and responsibility dimension, might be a consequence of the low correlation among responses, indicated earlier in the study.

The literature has founded identifiable but weak relationship among price awareness, service quality and customer satisfaction (Kangis. P & Passa.V, 1997) Scholars have identified that the strength of the price-quality relationship is considerably weaker in the case of services than for physical products.(Zeithmal.V 1988, p.8) In our study where service quality was considered as a dependent variable and price awareness as independent, no relationship along any of the dimensions was found to be statistically significant. Some researchers have stated that price is an indicator of quality when no other cue of quality is available and when brands are unfamiliar (Zeithmal.V 1988, p.10) Thus, with most of the banks offering brand and service differentiation as part of their strategy, the price dimension becomes more difficult to assess.

Similarly, the relationship between price awareness and customer satisfaction was found to be statistically insignificant, although someone may identify the existence of weak correlation. These findings are in compliance to Kangis. P and Passa. A (1997) research, who found that price awareness has weak relationship with customer satisfaction, although it might have some bearing ,when the possible influence of other factors is weak. The intangibility of the service and the fact that it varies with each encounter makes it difficult to use price as an indicator of customer satisfaction. (Kangis.P and Passa.A ,1997.p.113) Nevertheless, we might agree that when a customer views the service as homogenous, price awareness may play an important role in their decision-making. (Kotler. P, 2001 p.383).

7.2 Limitations

The study should be seen as a preliminary one, characterized by some limitations.

A certain limitation is that the scale construction is entirely based on "expert" opinions and published literature. Consequently, additional items which might be of particular importance to the banking sector, were not included in the study. It is important to note that primary qualitative research with bank customers needed to be a priority.

Second, the study is limited to one industry, thus, generalizing the findings beyond the banking industry may provide invalid results.

Further limitation is the small sample size employed in the study, which implies that the results may not be appropriate indicators for the overall market situation. Moreover , the sample was composed only from retail customers, as a result of which the study is not applicable for the corporate customers group.

Limited resources and time were another constrain, affecting the quality of the data collected.

Finally, limited number of financial institutions ware included in the study, as such, caution should be exercised in generalizing these results to the overall banking industry.

7.3 Managerial Implications

Understanding of what quality means to the customer, should be a focal point of attention to managers. There are several factors that managers can use to improve the service delivery process and to establish long terms relationships with customers. Most decisive factor, is the ability of the bank to accurately deliver the promised service. Reliable service has the strongest effect on the intention to stay in relationship, and thus on future revenues. Service guarantees are an efficient instrument in showing the company capability of delivering valuable service, and thus, it signifies the company's customer commitment, trough which it can differentiate itself from competitors. The other factors which add value to the service are related to the human factor of the organization. In addition, although customers are becoming more and more technologically savvy, they are also demanding more and more personalized service and skilled employees from service providers. (Angur.M, 1999, p122) Training programs and reward systems are some of the strategies that banks can use to ensure effective personnel commitment.

In this highly competitive environment, it is critical for banks to start viewing quality from customer perspective, rather than evaluating it from their own point of view. (Zeithmal.V,1988 ,p.17) Thus, continues research is necessary, to identify the most important dimensions of quality, required by the customer. Nonetheless, because of the changing nature of customer perceptions, banks must consistently adopt their product and marketing strategies to this changes. Concurrent with the efforts to improve perception, they should also adjust to customer expectations. Advertising can serve to narrow the gap between the expectations and perceptions of customers.

For tangible products, there is a long-lasting perception that higher price means better quality. However, as Kangis. P and Passa. V (1997) imply this situation is different in the banking sector. (p.111) Their intangibility and high heterogeneity makes this relationship less supportive. Price might be considered as a shot-term determinant, when other things are being equal. One thing is certain, more informed customers are more loyal towards a bank. (Kangis. P and Passa. V ,1997.p 117) Thus, communicating the information of charges more clearly , might have an impact on attracting and retaining rs.

To sum up, what might be important of one group of customers may be unimportant for another. Some people are concerned about price while others are not (Kangis. P and Passa.V ,1997,p 117) Thus, managers must spend time on determining the variability of the customer base.

References:

[1] Allred, A& Addams, H. (2000) Service quality at banks and credit unions: what do their customers say?. Managing Service Quality [online], 10 (1) pg.201. Available from:http://search.epnet.com/login.aspx?direct=true&db=buh&an=3833154 [Accessed 27th April 2008]

[2] Anguer, M. et al.(1999) Service quality in the banking industry: an assessment in a developing economy. International Journal of Bank Marketing [online], 116 (123), 17th March 1999.EBSCO DATABASE [Accessed 15th April 2008]

[3] Bahla. K, & Nantel. J, (2000) A reliable and valid measurement scale for the perceived service quality of banks. International Journal of Bank Marketing [online], 18 (2), pp.84-91. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=3394616 [Accessed 20th April 2008]

[4] Chattopadhyay. A & Alba. J, (1988) The Situational Importance of Recall and Inference in Consumer Decision Making. Journal of Consumer Research. [online], 15, June 1988, pp.1-12. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=4657749 [Accessed 20th April 2008]

[5] Herr. P, (1989) Priming Price: Prior Knowledge and Context Effects. Journal of Consumer Research. [online], 16, June 1989, pp.67-76. Available from:http://search.epnet.com/login.aspx?direct=true&db=buh&an=4664810 [Accessed 15th April 2008]

[6] Inacobucci, D. et al. (1995) Distinguishing Service Quality and Customer Satisfaction: The voice of the Customer. Journal of Consumer Psychology [online], 4 (3), pp. 277-303 EBSCO DATABASE, [Accessed 3rd May 2008]

[7] Karankitikorn. O, (2005) A Comparative Study of Service Quality of Thai Airways: Domestic Flights vs. International[online].The Institute of International Studies, Ramkhamhaeng University. Available from:http://www.ru.ac.th/tem/info/Contents%20of%Journal%20Opas%5B1%5D.doc [Accessed 15th April 2008]

[8] Kotler, P. & Armstrong, G. (2001)Principles of Marketing. 9th edition. Prentice-Hall, Inc. USA

[9] Lichtenstein. D. et al.(1988) Correlates of price Acceptability. Journal of Consumer Research.[online], 15, September 1988, pp. 243-251. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=4657237 [Accessed 4th May 2008]

[10] Nikolov, M et al. (2008) A simple queuing statistical model for the banking system in Macedonia. CEA Journal of Economics [online], 3 (1) pg.5-8. Available from: www.cea.org.mk [Accessed 5th September 2008]

[11] Parasuraman, A. et al. (1985) A Conceptual Model of Service quality and its Implications for Future Research. Journal of Marketing [online], 49, (1,2).pg 41-50. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=5001773 [Accessed 4th May 2007]

[12] Peterson. R, (1970) The Price-Perceived Quality Relationship: Experimental Evidence. Journal of Marketing Research. [online], 7 (4),November 1970, pp.525-528. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=5002078 [Accessed 20th April 2008]

[13] Parasuraman, A. et al. (1993) Research Note: More on Improving Service Quality Measurement. Journal of Retailing [online], 69 (1), Spring 1993, pp.146. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=4671057 [Accessed 3rd May 2008]

[14] Passa. V, & Kangis P, (1997) Awareness of service charges and its influence on customer expectations and perceptions of quality in banking. The Journal of Services Marketing.[online], 11 (2), pp.105-117. EBSCO DATABASE

[15] Sachdev. S, & Verma. H, (2004) Relative importance of service quality dimensions: a multisectorial study. Journal of Service Research [online], 4 (1), April-September 2004, pp.94-113. EBSCO DATABASE, [Accessed 28th April 2008]

[16] Shapiro. B, (1973) Price Reliance: Existence and Sources. Journal of Marketing Research. [online],x, August 1973, pp.286-294. EBSCO DATABASE [Accessed 28th April 2008]

[17] Soteriou, A.& Zenious, S. (1997) Efficiency, Profitability, and Quality in the Provision of Banking Services. [online] Wharton Financial Institution center, Cyprus, 92-97,pg. 5 Available from: http://fic.wharton.upenn.edu/fic/papers/97/zenios.pdf [Accessed 25th April 2008]

[18] Taylor. S, & Cronin J, (1992) Measuring Service Quality: A Reexamination and Extension. Journal of marketing [online], 56, July 1992, pp.55-68. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=9211164404 [Accessed 28th April 2008]

[19] Zeithaml, V.A. (1988) Consumer Perceptions of Price, Quality, and Value: A Means-End Model and Synthesis of Evidence. Journal of Marketing [online], 52, July 1998, pp.2-22. Available from: http://search.epnet.com/login.aspx?direct=true&db=buh&an=6354303 [Accessed 3rd May 2008]

UDC 338.124.4:336.7(100) 338.124.4:336.7(100)]:336.76(497.7) THE EFFECTS OF THE INTERNATIONAL FINANCIAL CRISIS AND THE GOVERNMENT'S INTERVENTIONS

Meri Boskoska, MSc.

Faculty of administration and management of information systems in Bitola
University "St. Klement Ohridski"- Bitola
meribb@yahoo.com

Abstract

The stock exchanges have a great role in the efficient function of the financial system of the country because they represent the mechanism for properly direction of savings and for stimulating the investment that, in matter of fact, represent the base for the greater economic development. The events on the stock exchange are one of the basic factors for set up the scenes and for transmission of the actual financial crisis all around the world.
The actual financial crisis that escalated as a result of the "mortgage-crisis" in the USA spread very quickly in the countries all over the world and caused problems not only in the financial sector, but in the real sector in different countries.
The aim and the purpose of this paper is to represent the situation of the global financial market at the moment and to analyze to which degree the Macedonian financial market is vulnerable to these external financial shocks.

Key words: *International financial marker, Macedonian stock exchange, financial shocks, banking sector, financial crisis, government intervention, liquidity.*

Introduction

The stability and the efficiency of the financial system in every country, above all, depend on the way that the banking sector and the securities market function. Namely, the banks are the major mediators of the citizens' and companies' savings. In today's conditions of inefficient banks the saving is taken in a wrong way and aridly in the aspect of the entire economic development. The stock markets also, have a great role in the efficient functioning of the financial system of the countries because they represent the mechanism for directing the savings and stimulating the investments that is actually, the basis for achieving bigger economic growth. In the paper's continuance an analysis is made- that is to say- how the irregularities in the functioning of the banking sector in one country can be the reasons for appearance of a major economic crisis that via securities market grew into global financial chaos.

1. Development of the American financial crisis

The experience related to the appearance and influence of the financial crisis shows that the eventual disturbances in the securities market can cause serious consequences on the financial stability in one's country. In the past, the events and the happenings in the world's financial stock markets were the reason of appearing and overthrowing the consequences of the modern financial crisis all over the world. These kinds of events that are happening currently are characteristic for the American financial market and they caused very bad and difficult situation that hasn't been noticed since The World's Economic Crisis in the 30's of the last century.

The American financial crisis began as a mortgage crisis, but it spread in the USA's banking sector and in a short period of time in other countries in the world. Namely, we talk about the credit's crisis which began on 9th of August 2007 when the prices of the credits started to rise severely. The American corporations couldn't withstand the competition in the industrial production because the labor's price was high, and the businesses began to use the cheapest ways of making money. The banks offered loans, not for production investments, but for spending credits using the citizens' estates as a guarantee. In this process of financing, the banks realized the biggest incomes through issuing credit cards and small amount of loans. According to this trend, the western banks and the advertising companies engaged in this process and the result was a boom in the spending credits.

In the period between 2004 and 2006 the prices of the real estate, especially the houses raised quickly which was a serious problem for those who bought a house for the first time. The creditors solved this problem in such a way that they lowered the criteria for loans' guarantees. First, the creditors made a mix of the new loans with bad quality with quality mortgages and bonds, and then they put them in debt packages and were selling them to the investors all over the world. That process is actually turning the mortgage loans into securities.

The credit's policy of the American banks caused a debts' rise in the households so they owed as much as the American economy can produce in a year. The biggest part of the means was used for investments in the real estate market and it resulted in creating a bubble in that market that in the end had to blow.

The blowing of the bubble in the real estate market and the rise of the unpaid mortgage obligations, actually, meant that less and less number of owners of the houses were in a position to pay off their monthly obligations. The institutions on Wall Street couldn't pay off the mortgage securities that were used as a guarantee for the bigger debt to be supplemented with new investments. These institutions were stuck with those securities with suspicious value, so they had to get cash or to sell those stocks. With this kind of action the prices of these securities were reducing much more. Faced with such huge debts and the fall of there assets, the banks rarely gave credits or they fully gave up of issuing them and by doing that the whole financial system was close to destruction.

The fall of the American financial sector is a serious threat that can cause a recession not only in the USA, but in great number of countries all over the world, that actually is happening at the moment.

a. The situation in the American financial system and government interventions

Thankfully to the process of the globalization, which is one of the channels for transferring the crisis effect, the negative consequences of the financial crisis were felt not only by the developing countries but by the developed countries too. That was the case with the American financial crisis, which, almost overnight, the crisis began to affect the other parts of the world. In these kinds of dramatic conditions a question is being asked- What do the responsible people from the developed countries undertake to reduce and eliminate the influence of the financial crisis?

The decision of the Federal Reserve's to leave The Lehman Brothers Bank to bankrupt aroused series of chaotic events. During this period, in only 96 hours, strange things happened on the American market. What happened actually? Lehman Brothers Bank is the fourth biggest investment bank in the USA which because of the debt of 613 billion dollars had the need of capital enlargement. This bank was in such position that the prices of the shares fell continuously and no one was ready to buy it without the government approval and guarantee. This bank hadn't got any other solution than to bankrupt. Also, Merrill Lynch, a bigger investment bank was forced to sell itself to The Bank of America. Table 1 present the major banks that have crumbled or been bought out during the global financial crisis.

Table 1. Banks affected by the global financial crisis - 2008

Bank	Date	Status	Website
Fannie Mae	07 Sep	Nationalized	Fannie Mae
Freddie Mac	07 Sep	Nationalized	Freddie Mac
Lehman Bros	15 Sep	Collapsed	Lehman Bros
Merrill Lynch	15 Sep	Taken over	Merrill Lynch
AIG	16 Sep	Part-nationalized	AIG
HBOS	17 Sep	Taken over	HBOS
WaMu	25 Sep	Collapsed and sold	WaMu
Fortis	28 Sep	Nationalized	Fortis
Bradford & Bingley	29 Sep	Nationalized	Bradford & Bingley
Wachovia	29 Sep	Taken over	Wachovia
Glitnir	29 Sep	Nationalized	Glitnir
Hypo Real Estate	06 Oct	Rescue package	Hypo Real Estate
RBS	13 Oct	Part-nationalized	RBS
Lloyds TSB	13 Oct	Part-nationalized	Lloyds TSB

Source: http://news.bbc.co.uk/2/hi/business/7644238.stm, December 2008.

On the other side, the market pressures forced the federal reserves to take over the biggest insurance company (American Investment Group- AIG) in order to avoid its bankruptcy. Although, this insurance company had the largest market value of approximately 239 billion dollars, this wasn't the reason for its rescue. The government approved its rescue giving the reason that if this company collapsed, the financial market would undergo catastrophe, because it secures the biggest part of the commercial and life insurance in the USA. AIG caused systematic risk because of the bad work in working out the insurance deals that led to losing its fortune and wealth and then losing its independence too (Figure 1). The previous events happened just two weeks after Fannie Mae and Freddie Mac were saved by the government as well as after the saving of Bear Steams 1[15].

15) After the taking of Fannie Mae and Freddie Mac by the American government, there was an opinion in the public that the same will happen with the Lehman Brothers. That was exactly the problem. If the government did that, then they would confirm that they created the so called- moral risk and that the government itself was behind all the risky financial activities that were undertaken on the financial market. This decision will not end the credit crisis, but will put an end to a decade of moral risk. (www.economist.com, November 2008).

Figure 1.

The lost of AIG's independence

Source: www.economist.com, November 2008.

But, the AIG rescue didn't calm down the investors because the greatest crash of the American bonds happened the next day, even though they are considered to be the safest investments. The same situation was recorded in 1941, when the world was at war, and the USA was still recovering from the depression. In such circumstances the need for the gold grew up and simultaneously its price increased too. The gold world market tried to please every need, but there were less and less reserves.

The American financial investments that faced the bankruptcy as well as those which were close to that if they weren't saved by the government, had huge problems because of the lack of capital. This problem was the result of the high stockholders' incomes as well as the new banks' debts in order to supplement and fill in the investments.

The world financial market participants were in fear, because the world markets are at crisis, the trading on the world stock market decreases, the investment banks lose their trust and so on.

The American federal reserves and part of the European central banks reacted to these financial disturbances by "injecting" billions of Euros in a form of short term credits in order to stabilize the global financial market and to improve the liquidity. However, this wasn't their final intervention, because they continued to take over numerous measures to bring back the stability of the world financial market. In such a way, The American senate adopted the proposal given by the Bush's administration to save the financial sector. According to this plan, the American government set aside 700 billion dollars to secure the system. With the approved funds, the Ministry of finance will purchase the property that isn't liquid from the banks' balance and from other financial institutions and with such strategy the credit market wouldn't be blocked and the global fall of the stock market would be ended. But, the investors welcomed this decision with great attention because of the uncertain effect of the influence that this President's plan can have on the global finance market.

It is understandable that the government takes measures, but that can't improve the economy overnight. It is also very clear that the American economy needs time to recover its trust in the financial institutions and to escape from the financial crisis.

2. The influence of the American financial crisis on the international financial system

The process of financial globalization encourages the effects of the American financial crisis to spread out side of its borders. Also, the American financial crisis reflected on the shares' prices of the Asian stock market, and huge losses suffered one of the major Japanese and Australian banks that financed Lehman Brothers. Except for Asia, the crash was felt in other European countries.

This financial crisis was felt in Iceland, where in the previous period of time, the three biggest banks were being nationalized and they collapsed because they were not in a position to pay out depositors. The stock market collapsed too and the national currency lost almost half of its value. The losses of the financial sector in Iceland will be greatly felt in England and in Wels, because they invested great deal of funds in the banks that faced crash.

The consequences of the financial chaos weren't felt only in the English municipalities; they were also felt in the English bank sector. Namely, the British bank "Bradford and Bingley" had serious problems as a result of the global financial crisis and that's why the government decided to nationalize it. Before this bank, "Northern rock bank" was nationalized and the powerful bank group HBOS that consists of "Halifax bank" and "The bank of Scotland" had to be immediately saved from a bankruptcy, by being taken over by a smaller bank called "Lloyds TSB Bank".[16]

In the early days of October, in spite of the taken measure, the British government brought a decision to invest approximately 65 billion dollars to recapitalize the eight biggest home banks and apartment's association that, actually is their partly nationalization. This plan is much more different from the American one because the British government buys the banks' shares, while the American financial plan is to ransom the basic funds of the banks that are badly produced.

In addition to that, the bank "Hypo Real Estate" that finances only commercial projects and public construction is the first German victim of the financial crisis. As a first step was that the German government and the banking sector agreed to get 35 billion dollars to save Hypo. But, soon after this plan, the larger number of the banks declared that they withdraw from that action because they confirmed that Hypo's problems were much deeper and elementary.

The German government and the banking sector gave a new plan, that is to say they would give extra 15 billion dollars to the bank, except for those 35 billion dollars and that the state guarantees for those money.

Slovenia wasn't saved from this financial disturbance too. The stock index lost its value almost half of the worth in six months and was driven back to the same position that was two years ago. The consequences were felt in various segments as: the banks' portfolios were weakened, the stock markets, funds, the investors lost over 10 billion dollars, and Slovenians buy houses and cars rarely… The experts in this country suggest that first the banking sector should be stabilized, than the economy in the country.

In regard to the previous data and facts, the next section represents how international financial institutions and governments react to the global financial turmoil that spread in many countries in the world.

2.1. The role of the international financial institutions and government interventions in resolving the problems of international financial crisis

In today's conditions of globalized world, we are witnesses how, apparently, a distant financial crisis can spread very quickly in other countries in the world. For solving such problems that were caused by the actual financial crisis a global, coordinative, flexible and fast reaction is necessary. This must be done by the international financial institutions and the government in the countries affected by the financial crisis.

All these events show us that the European governments cannot stop the so called domino effect of the American financial crisis, but they take over some steps to amortize there consequences. Among those steps, except for injecting fresh money in the banking sector, an agreement for minimal guarantee of the private deposits was agreed. These deposits in the European Union are 50 000 Euros, but some of the members of the European Union are determined to enlarge that sum to 100 000 Euros. Some of the governments, as the Slovenian decided to fully ensure the deposits so they cannot be taken by the other banks in the European Union.[17]

16) www.sfgate.com, November 2008.
17) www.one.org/international, December 2008

The leaders of the most industrious developed countries (G-20), on the common meeting, agreed that the prior thing to do in this moment is to recapitalize the banks that are in crisis. The countries that are members of the Union will guarantee the mutual credits to 2009; every country will decide the amount of funds that will give for these purposes.

The measures that the some governments undertake are not enough for resolving the consequences that were caused by the world's financial crisis and for returning the trust in the financial institutions. To this kind of actions must be added the activities of the international financial institutions. In such contest, will be mentioned the involvement of International Monetary Fund, the World Bank, as well as The Basel's committee for bank supervision[3] of the international financial market.

IMF offered financial help of hundreds of billions dollars to the member countries that can urgently get credit to stabilize their financial systems. World Bank joined to these financial packages that are approved by IMF, and at the same time they were giving the fact that a greater help will be needed by the developing countries. They have bigger problems with the financial crisis and they have to strengthen their financial systems.

The World Bank reacts to such needs through undertaking a wide range of activities that can be grouped in three groups: supplies financial help in the developing countries offers advices and technical help and forms partnerships with other organizations.[3]

In November 2008, the Basel's committee for banking supervision, for surpassing the basic weaknesses that were produced as a result of the crisis in the financial markets, announced a detail strategy that will refer to improvement of the regulation, supervision and controlling the risk in the banks that work in the international capital market. The basic activities of this strategy are the following:[18]

- strengthening of the risk capture of the Basel II framework (in particular for trading book and off-balance sheet exposures);
- establishing extra smoothing of the shocks in the plan for the capital that can be used in the period of crisis periods;
- supplementing the measures for estimation of the risk in order to maintain the strength of the banking system;
- strengthening the supervisory function for estimating the liquidity of the banks that work in the international capital market;
- strengthening the process of controlling the risks;
- promoting the global supervision.

The building of a stabile and efficient financial system is a complex and long-lasting work, and we should into account different institutional structures that exist in some countries.

For realizing this aim in the countries where there is a financial instability a help will be needed: first, they should see the weaknesses of their financial systems; second, to develop a strategy that will handle with the existing financial weaknesses and third to secure a technical help for implementing the chosen strategy.

The global influence of the actual financial crisis, in smaller or bigger degree, is already felt in Republic of Macedonia. Because of that, in the continuance we will briefly review that problem.

3. The influence of the financial crisis on the Macedonian capital market

In the research carried in the area of the financial crisis a conclusion can be made that a common characteristic of the modern financial crisis is its quick transmission out of the borders of the country in which it firstly appeared. Actually, the best example for that is the recent American crisis that reached a global proportion. In its beginnings, there was thinking that the influence from this crisis will be felt by the American

18) www.bis.org, December 2008.

financial market and the bigger European investment banks whose working activities were closely related to this market. But, the real happenings showed that the crisis gained such proportions that grew into a world's crisis whose consequences were felt in many countries in the world, directly or indirectly.

According to the fact that the Republic of Macedonia is European country, the danger of spreading the financial crisis in our country disturbed the Macedonian public. The frequent asked questions were: Can the financial crisis influence on the financial sector and will be taken some preventive measures in order to stop it?

Even though the influence of the global financial impact reflected on the Macedonian capital market, but still, the impact is much smaller than the impact that the other European and Asian countries endured. The experts think that it is the result of the psychological reaction of the investors that is a common thing in case there is no trust in the global financial market. The fear that appeared influenced on the drastic lowering of the shares' prices, because there was bigger offer than request of the capital. After this crash, the leaders of the stock market together with the bond commission took over certain measures to control the stock market's transactions, that is to say, the prices were limited to +/- 5% instead of the present +/-10% of the base price and in that way the crash on the market was lessened. But the following week these limits of the prices were suspended as a reaction to the stability of the stock market.

The current situation on the Macedonian stock market shouldn't be alarming considering the fact that there are not a great number of foreign investors that in a case of bigger disturbances will withdraw their capital out of the country. The Republic of Macedonia is a free market, but financial closed economy and there are no lawful possibilities to invest in the foreign stock markets or to buy real estates in other countries. So, the undeveloped capital market that is considered to be shortage in normal conditions is at the moment an advantage, because the financial sector will be isolated from the current happenings.

According to the experts, the situation in the banking sector in Macedonia isn't alarming yet, basically because the global banks that endured great losses from the current financial crisis aren't present in our banking sector. Also, the bankers calm down the citizens that their bank deposits are safe because they are regulated by the leading European banks where the regulations are stricter than the American ones. Namely, we talk about commercial and not investment banks and on the other hand the deposits are ensured by the saving deposit's fund. Because of this, and because of the fact that the Macedonian banks haven't got loans from the European banks that are in a middle of crisis, the situation in the Macedonian banking sector isn't alarming.

Anyway, we should mention that there are some indirect effects that global financial crisis cause in the banking and real sector in our country. In the banking sector this effects can be felt by the bigger interest rate of the credits on one hand and on the other hand, there is a bigger interest rate of the savings deposits which is an easier way for the banks to get to Euros other than to take credits in a foreign banks where the financial crisis is still up to date. In the real sector the metallurgic and textile organizations are facing the negative effects of the financial crisis. The demand for there products on the European markets are falling and they react by firing there workers so the unemployment in the country is rising.

The current situation of the global financial market draws to important questions and according to the answer the stability of the market depends: Are there any financial holes that we should be careful of and are we on the beginning of a new period of regulation? There is no doubt that there will be greater pressures for a supplementary regulation. What we actually need is a regulation that will really work and function. According to the second question it is necessary a bigger attention to be paid on the use of the credit cards because they aren't ensured, in another words, the clients haven't got an obligation to put in money when they open a new account and the enlargement of the interest rates is a measure that for the creditors will mean bigger problem in returning the debts to the banks. We cannot predict the future with certainty, but one thing is sure that the greed for money is the major guilt, the lost investor's trust will be difficult to bring back, in other words- a longer period of time is needed to stabilize the situations on the world's financial market.

a. Recommendations for keeping the stability of the Macedonian financial market

From the previous research can be concluded that the Republic of Macedonia will feel the negative influences of the global financial crisis. These happenings raise the question, which activities should be undertaken to balance and amortize the influence of this so called "financial virus "?

The preventive measures for protection of the Macedonian financial market and the real economy can be done in the following way:

- Making the conditions for crediting of the public and the business organizations more severe;
- Carefully formulating and efficiently taken strategies for taking and controlling with risks;
- Application of the principles in working of the banks which is especially important for the citizens' trust;
- Application of the measures that will guarantee the deposits of the savers so there wouldn't come to a situation of withdrawing them from the banks;
- Application of the corporative directing in the banks that will define the relationships with the auctioneers and supervising boards;
- Greater supervision of the internal and the external supervisors;
- Bigger role of the National Bank of Republic of Macedonia in naming and election of the manager teams and other organs for which the bank has got authority
- Carefully selected politics for controlling of the interest's and currency's risk;
- Greater cooperation between the government and the business organizations from the business sector in order to find a solution for eventual problems that they face or will face in the future as a result of the financial crisis;
- Taking over the measures for enlarging the employment;
- Measures for lessening the trade deficit and so on.

The focus over the previous structural references by the responsible doers in the state will enable a stabile financial system that will influence on making bigger economic growth, enlargement of the competition in the economy, reduction of the unemployment, bigger living standard for the citizens and creating conditions for faster integrating of the country in Euro Atlantic structures.

Conclusion

In conditions of globalized world, the probability is greater, the disturbances in particular market segment or in one country to spread in other regions or countries and to produce financial crisis. The global financial crisis, that began in the USA, in short period of time spread in the countries all over the world causing painful consequences in their economies. Although, the Republic of Macedonia is a minor participant in the international financial market, yet, the consequences of the global financial crisis is already felt in the financial and real sector in our country. Because of this, the influence of the financial crisis shouldn't be ignored. On the contrary, a careful following of the events is necessary and taking over preventive measures for protection of the Macedonian financial market and the real economy.

References:

1. Business; the first economy newspaper in Macedonia, year 2008.
2. Milkovic, Dejan (2007), "Megunarodne finansije", Centar za izdavacka delatnost Ekonomskog fakulteta u Beogradu.
3. Petkovski, Mihail, "Finansiski pazari i institucii". Faculty of economics, Skopje, 2004, p. 219.
4. Soskic, Dejan I Zivkovic, Bosko, "Finansiski pazari i institucije", Faculty of economics, Beograd, p.249, 2006.
5. www.bis.org
6. www.economist.com.mk
7. www.ft.com
8. www.kapital.com.mk
9. www.one.org/international
10. www.sfgate.com

UDC 338.124.4:336.7]:336.711(100)
GOVERNMENT AND CENTRAL BANK MEASURES IN TIME OF FINANCIAL CRISIS

MSc Neda Popovska Kamnar
neda@mol.com.mk

PhD candidate
University "Cyril and Methody"
Economic faculty-Skopje

Abstract

This paper presents the measures which the governments and the central banks are implementing in order to protect their countries from the latest global financial crisis. The first part of this paper is describing the causes of the financial crisis and the global reactions to the economic turbulences. The second part presents the measures of the main institutions in United States, Europe, England and also Sweden, Germany and Portugal, in order to improve the liquidity on their financial markets. In the third part are presented the measures by the governments and central banks of the emerging and Balkan countries.

Keywords: *financial crisis, measures, governments, central banks*

Introduction

Despite of different definitions and approaches to financial crisis, its main feature is unbalance between supply and demand for money. The liquidity is evaporated quickly because available money is withdrawn from banks forcing them either to sell other investments making up for the shortfall or to collapse. The financial crisis 2007 initially started in United States as a sub prime mortgage crisis, (the value of securitized mortgages was falling quickly), causing a liquidity crisis on the financial market. Global financial interconnection helped the financial crisis 2008 to escalate, and to transfer on the European ground, hitting the biggest European banks, markets and companies. One of the main reasons of the mortgage market collapse in USA was lack of regulation on the financial derivates market and on the financial agreements based on the high government securities for banks risk. It was a result of a period of aggressive risk-taking on the subprime market. As the financial crisis went to become deeper and deeper, it was clear the market couldn't solve the problems, and the governments and central banks intervention was inevitable. But still, after numerous direct measures introduce on the highest level, the financial crisis is not decelerated. The latest predictions are not optimistic truly -the crises will not slowdown till 2010.[19] The situation is becoming worse: few months ago the prognoses were mid-2009.

19) Regional Economic Outlook, IMF, october 2008

The consequences of the global financial crises

The global financial crises beginning from American market on July 2007 produced shockwaves enough to overwhelmed with economic problems the other countries of the world. It put the biggest financial institutions on their knees, and made the governments facing the biggest challenges since the last big Economic Deprecation 1929-1933. In less then a year we witness the biggest economies in the world, Europe, USA, Japan go in to recession. So far, the total estimated cost of interventions of all natures across developed economies amounted to around 8,600 billion dollars, half of which to be attributed to the U.S.[20] It was common to all: the capital markets had to deal with illiquidity, dropping asset prices and withdrawing of investments. The governments were faced with the failure of the supervision frameworks, finding themselves on the crossroad, how far to go in using a budget money in order to cover the wrong decisions of the private financial institutions

In the last year, the governments have not fight with the instability of the credit markets and bailing out the banks from bankruptcy only. They have had to find measures to stabilize the real sector dealing with big problems like output slowdown, high levels of inflation (mainly caused by the food and energy highest prices), increasing unemployment, budget deficit…. In the developed countries mostly the prediction for

	Real GDP growth				CPI inflation			
	2006	2007	2008	2009	2006	2007	2008	2009
Europe 1/2/	4.1	3.9	2.6	1.4	3.6	3.6	5.8	4.2
Advanced European economies 1	3.0	2.8	1.3	0.2	2.2	2.1	3.5	2.2
Emergening European economies 1/2	7.0	6.8	5.7	4.3	7.5	7.5	11.5	9.2
European Union	3.3	3.1	1.7	0.6	2.3	2.4	3.9	2.4
Euro area	2.8	2.6	1.3	0.2	2.2	2.1	3.5	1.9
Austria	3.4	3.1	2.0	0.8	1.7	2.2	3.5	2.3
Belgium	2.9	2.8	1.4	0.2	2.3	1.8	4.6	2.8
Cyprus	4.0	4.4	3.4	2.8	2.2	2.2	4.6	3.5
Finland	4.9	4.5	2.5	1.6	1.3	1.6	3.9	2.5
France	2.2	2.2	0.8	0.2	1.9	1.6	3.4	1.6
Germany	3.0	2.5	1.8	0.0	1.8	2.3	2.9	1.4
Greece	4.2	4.0	3.2	2.0	3.3	3.0	4.4	3.1
Ireland	5.7	6.0	-1.8	-0.6	2.7	2.9	3.5	2.4
Italy	1.8	1.5	-0.1	-0.2	2.2	2.0	3.4	1.9
Luxembourg	6.1	4.5	2.3	1.8	2.7	2.3	3.7	1.8
Malta	3.1	3.7	2.8	2.3	2.6	0.7	3.7	2.2
Netherlands	3.4	3.5	2.3	1.0	1.7	1.6	2.9	2.6
Portugal	1.4	1.9	0.6	0.1	3.0	2.4	3.2	2.0
Slovenia	5.7	6.1	4.3	3.7	2.5	3.6	5.9	3.3
Spain	3.9	3.7	1.4	-0.2	3.6	2.8	4.5	2.6
Denmark	3.9	1.7	1.0	0.5	1.9	1.7	3.4	2.8
Sweden	4.1	2.7	1.2	1.4	1.5	1.7	3.4	2.8
United kingdom	2.8	3.0	1.0	-0.1	2.3	2.3	3.8	2.9
New EU countries 1/	6.6	6.3	5.0	3.5	3.3	4.1	6.4	4.4
Bulgaria	6.3	6.2	6.3	4.2	7.4	7.6	12.2	7.0
Czech Republic	6.8	6.6	4.0	3.4	2.5	2.8	6.7	3.4
Hungary	3.9	1.3	1.9	2.3	3.9	7.9	6.3	4.1
Poland	6.2	6.6	5.2	3.8	1.0	2.5	4.0	3.3
Romania	7.9	6.0	8.6	4.8	6.6	4.8	8.2	6.6
Slovak Republic	8.5	10.4	7.4	5.6	4.3	1.9	3.9	3.6
Estonia	10.4	6.3	-1.5	0.5	4.4	6.6	10.2	5.1
Latvia	12.2	10.3	-0.9	-2.2	6.5	10.1	15.9	10.6
Lithuania	7.9	8.9	3.9	0.7	3.8	5.8	11.3	6.2
Albania	5.4	6.0	6.1	6.3	2.4	2.9	4.0	3.0
Belarus	10.0	8.2	9.2	8.0	7.0	8.4	15.3	9.6
Bosnia and Herzegovina	6.9	6.8	5.5	5.0	6.1	1.5	8.5	5.2
Croatia	4.8	5.6	3.8	3.7	3.2	2.9	7.0	4.9
Macedonia	4.0	5.0	5.5	5.0	3.2	2.3	8.5	3.0
Moldova	4.8	4.0	6.5	6.5	12.7	12.4	13.7	9.7
Montenegro	8.6	9.7	7.5	5.0	2.1	3.5	9.2	5.2
Russia	7.4	8.1	7.0	5.5	9.7	9.0	14.0	12.0
Serbia	5.6	7.1	6.0	6.0	12.7	6.8	10.7	7.5
Turkey	6.9	4.6	3.5	3.0	9.6	8.8	10.5	8.4
Ukraine	7.3	7.6	6.4	2.5	9.1	12.8	25.3	18.8

Source: IMF, Regional Economic Outlook, october 2008
1/Average weighted by PPP GDP
2/ Montenegro is excluded from the aggregate calculation

20) EU10 Regular Economic Report, October 2008, World bank

2009 is that the output will decline, in some cases negative, but the inflation rate will be stabilized. In the emerging countries the output grow in 2009 is expected to be positive, but lower than earlier, but still facing the problems with high inflation and credit expansion. Also, the influence of the finance crises in the countries with large external financing needs (Romania, Bulgaria, and Hungary) is through the slowdown in global demand in the EU countries and the tightening of the financial conditions.

As a result of sharply decreasing of the demand in advanced countries and worsening of credit conditions to emerging countries, in November, IMF produced new numbers for the global growth. According to the newest predictions, the global growth will continue to slow down to 3,7% in 2008 and 2,2% in 2009. The revised forecasts growth for 2009 in advanced countries to be negative 0,3 and for emerging and low income countries to be 5,1%.[21]

The governments and the central banks are facing many challenges in this global economic downturn. The new regulations, measures, bailout state-aid packages are passing on daily bases, with the hope that the liquidity on the markets will be improved. The central banks measures were mainly focused on improving the liquidity problems, through credit lines, reversed repo auctions, state bonds as collateral and etc. The governments adopted highly expenses packages to help private financial institutions, which lately also include help to the vulnerable sectors of the industries (examples of car industry, productions of steel and etc). The USA government adopted 700 billions dollars package to buy troubled financial assets while UK approved 50 billion pounds bank bailout package. The government of Japan offered stimulus package of 5.1 billion dollars, after the country went in their first recession in seven years. Also, the Bank of Japan, slash the interest rates for first time in seven years by 20 basic points, to 0.3%. The latest news are saying that the European commission unveiled an economic recovery plan, which will total 200 billions euro, or 1.5% of the EU member's GDP. Most of the money will be supplied by member state, and around 30 billions Euros will be provided by certain actions of European Union. This package will be implemented in 2009 and some measure would continue into 2010.

There were many discussion should the government use budget money gathered through the taxes in order to bailout the private institutions from their huge deficits. But, it looks that they didn't have much choice. Those institutions were just "too big to fail", which means that their failure would influence the economy of the country, the rate of the employment, and the domino effect on other smaller companies will happened. For example, UK government in their bailout package, helped the financial institution like "HBOS" which have total assets of 838 billions Euros (in 2007) "Lloyds TS" with total assets of 444 billions Euros and "Bradford and BIngley" with total assets of 65 billions Euros. Also, European government helped "ING" with total assets of 1,370 billions Euros. In the following tables is presented the government assistance in the biggest financial institutions, where the financial crises had a huge influence on their assets and rising debts.

United States	$ Bn
Fannie Mae and Freddie Mac	200
Wachovia	12
Citigroup	25
JPMorgan Chase	25
Bank of America	20
Merrill Lynch	5
Wells Fargo	25
Goldman Sachs	10
Morgan Stanley	10
Bank of New York Mellon	up to 3
State Street	up to 3
Total	**338**

Source: Financial Times

Europe	€ Bn
Fortis	11.2
Hypo Real Estate	50
Glitnir	0.6
Dexia	6.4
Landsbanki	n.a
Kaupthing	n.a
UBS	3.9
ING	10
Credit Agricole	3
BNP Paribas	2.55
Societe Generale	1.7
Credit Mutuel	1.2
Caisse d'Epargne	1.1
Banque Populaire	0.95
KBC	3.5
Commerzbank	8.2
Total	**104.3**

United Kindom	£ Bn
Bradford and BIngley	18
Royal Bank of Scotland	20
HBOS	11.5
Lloyd TSB	5.5
Total	**55**

21) World Economic Outlook Update, IMF, november 2008

World leaders recently gathered at the summit of Group of 20 in Washington, to address the economic crisis in the world, and concluded that it's necessary to speed up the regulatory reforms, to support the global growth and to avoid protectionism. From the summit G-20, the countries decided to create new short-term liquidity facility and to review the instruments and facilities. Also, they agreed that the fiscal stimulus is essential to restore global growth, decrease the inflation risk and provide the room for easing the monetary policy. In the future it's necessary to strength the role of IMF in the contents of providing macro-financial policy. G-20 agreed that the countries should restrain from raising new barriers to trade and investments during the next year, because their very important for the growth of the countries.

In November 2008, IMF wasn't very optimistic about the future developments of the financial crisis. The chief economist of IMF said that the global financial crisis is set to worsen and that the situation will not improve until 2010. He also urged central banks around the world to cut interest rates, lowering close to zero as possible. IMF promised to help Latvia, after assisted Iceland, Hungary, Ukraine, Serbia and Pakistan, but pointing out that it is not able to solve all financial issues. The IMF had spent a fifth of its 200 billion euro fund in a period of two weeks.

The government and central bank measures

What kind of measures did the governments and the central banks proceed in the last year? The governments of the developed countries were trying to bring back the confidence and liquidity into the markets, and saving the biggest financial institutions from drawing in the same time. Their agenda has stimulations of the output grow and the protection the working places of millions people in the industry too. The emerging countries were more focused on the stabilization the inflation, reduction the credit expansion pressure and regulation the trade deficit. "Never is everything so black". Some analysis for these countries comes to conclusion, that the weak connection between their banking systems and the world financial markets, contribute in limiting the effects of the financial crisis

The government of the United States of America presented their bailout program which cost 700 billion dollars and with purpose to purchase bad assets, to reduce the uncertainty of value of the remain assets and to restore confidence in the credit markets. At the beginning, 250 billion dollars went for the purchase of bank stock, giving the infusion of cash to the financial institutions and 40$ billion dollars as an investment in troubled insurance giant American International Group. This brought many discussions about the credibility of this plan, because almost half of the money of the bailout program was spend, before any problematic assets were bought. But, the government is not giving up!

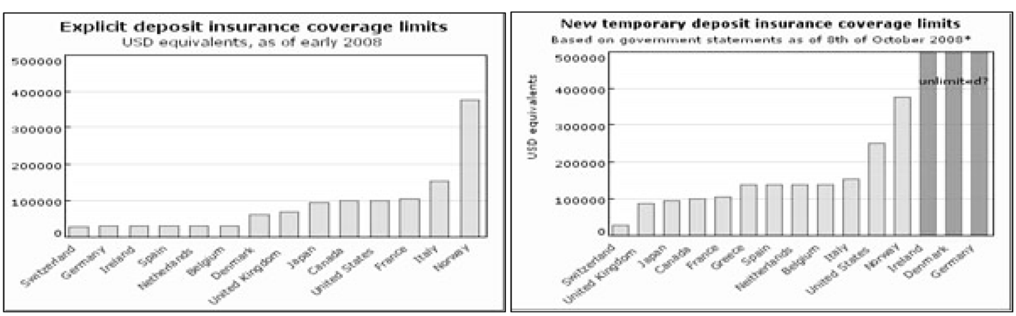
The lattes news from USA is that the government unveiled new programs that will provide 800 billion dollars to help the credit markets. According to this, the Federal Reserve created the Term Asset-Backed Securities Loan Facility (TALF), a facility that will help market participants meet the credit needs of households and small businesses by supporting the issuance of asset-backed securities (ABS) collateralized by student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration (SBA).Under the TALF, the Federal Reserve Bank of New York (FRBNY) will lend up to $200 billions on a non-recourse basis to holders of certain AAA-rated ABS backed by newly and recently originated consumer and small business loans. The department of the Treasury, Federal Deposit Insurance Corporation and the Federal Reserve put into place several programs designed to promote financial stability. They make available new capital to the institutions, increase the guarantees on bank deposit accounts and provide backup liquidity to banks. There is also a plan by the federal housing finance agency for speeding up the process for renegotiating thousands of delinquent loans held by the two mortgage giants (Fannie Mae and Freddie Mac).

The latest "institutional saving" by the U.S government was made for banking giant Citigroup after its shares plunged by more than 60%. The US Treasury is set to invest $20 billions in return for preferred shares in Citigroup. The Treasury and the Federal Deposit Insurance Corp will also guarantee up to $306 billions of risky loans and securities on Citigroup's books. The plan follows a $25 billions injection of public funds in the bank in October. Citigroup announced 52,000 job losses worldwide, on top of 23,000 job cuts previously. Citigroup has lost more than $20 billions in the past year because of the global financial crisis.

The government of Great Britain announced the recapitalization of the UK banking system of at least 50 billion pounds and together with the liquidity support from the Bank of England and the new quarantine scheme is planning to bring back the confidence in the financial system. According to this, at least 200 billion pounds will be made available through the Special Liquidity Scheme, which will allow banks to swap illiquid assets of sufficiently high quality for Treasury Bills in certain time period. Also, the responsibility for losses on their loan stays with the banks. The bank will continue to conduct auctions to lend sterling for three months and US dollars for one week, against extended collateral. Also, to provide liquidity insurance to the banking system, the central bank introduce Discount Window facility which is intended for eligible banks and building societies which may borrow gilts, for up to 30 days, against a wide range of collateral in return for a fee, which will vary with the collateral used and the total size of borrowings.

Unfortunately, the Basel principles for supervision appeared inefficient in preventing and solving the financial crisis. The measures introduced with this supervision framework showed their weakness in certain sectors of the capital markets, not able to perceive the early signs of trouble. As a result of this, The European commission made changes in the Directive for bank capital requirements, with aim to reduce the risks in borrowing and lending and increase the power of supervision. So, with the new rules, the banks are limited to lend beyond a certain limit to any one party, so they can have enough capital to protect from risk and to protect their depositors. The changes in regulation were made in order to improve the quality of bank's capital, the management of the liquidity risk and the management of securitized products.

The other changes were made in the Directive on Deposit guarantee scheme in order to improve the deposit protection and to bring back the confidence in the banking system. With the new amendment of this Directive, the minimum level of coverage for depositors will be increased within one year from 20.000 euro to 100.000 Euros and initially to 50.000 euro in the intervening period. The payout period in the event of bank failure will be reduce from 3 months to 3 days. According to estimates, about 65 % of the deposits are covered with the current regime, and with the new improvements in the regulations, will cover around 80% (with coverage of 50.000 Euros) and 90% (with coverage of 100.000 Euros) of deposits. Several EU countries (Germany, Ireland, Greece, and Slovenia) have moved to protect all bank deposits.[22] But, there is a time lag. The new regulations will be realized in 2010, which means that they will not help in the current financial instability.



Source: OECD, organization for economic co-operation and development

European commission approved state aid packages to Germany, Hungary, Portugal and Sweden which proved capital measures and quarantines to the institutions, but in the same time, protect the state for other expenses. Each of the approved packages will be monitored by the authorities in order to see the affectability of the proposed measures.

22) See reference 1

The rescue package of Germany consists of recapitalization scheme which will introduce new capital to banks and insurance companies in exchange for share; guarantee scheme which will provide new issuance of short and medium term debt in return for market-oriented remuneration and temporary acquisition of assets which means that this assets will be bought back after 36 months without the state making a loss.

The rescue package for Portugal provides guarantees to financing operations of eligible credit institutions. The guarantee scheme provides state quarantines for financing agreements and emission of non subordinated short and medium term debt of solvent credit institutions. The total budget of the scheme is 20 billion Euros. The scheme is for all solvent banks in Portugal and it will be available till the end of 2009.

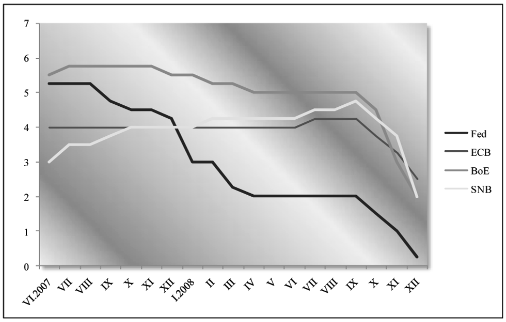
To support the institutions that have problems in financing, the rescue package proposed from European commission for Sweden was consists of quarantine scheme covering new issuances of short and medium term non-subordinated debt. The amount of total debt to be covered is around 150 billions euro and concerns instruments with maturity of maximum three years. Debt covered by the quarantine will be acceptable by the Swedish Central bank as equivalent to government bonds.

In order to restore financial systems of the countries and bring back the investor's confidence in the markets and economy, the successful cooperation between the governments and central banks is necessary. Using their monetary instruments and establishing different facilities for liquidity, central banks are taking an active role in the process of recovering the global economy. A detail structure of the central banks measures are presented in the following table:

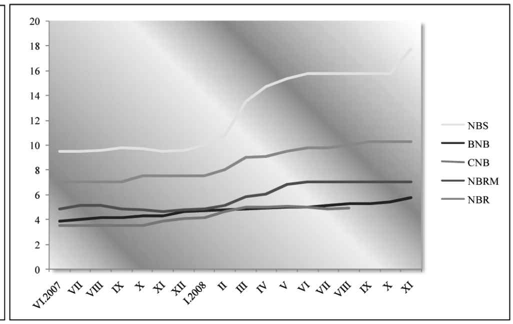
Feb.07	ECB	Renew the supplementary longer term refinancing operations
Mar.11	FED	Introduces a Term Securities Lending Facility (TSLF)
Mar.16	FED	Announced the introduction of a Primary Dealer Credit Facility (PDCF)
Mar.28	ECB	Supplementary 6 months longer-term refinancing operations
Apr.21	BOE	Launched a Special Liquidity Scheme
May.02	ECB, FED, SNB	Expansion of their liquidity measures
	ECB	Increase the amount of US dollars liquidity provided to the counterparties of the Euro system to 25 billions od dollars in each bi-weekly auction
	FED	Increase in the amounts auctioned to eligible depository institutions under its biweekly term auction Facility from 50 billions to 75 billions of dollars
	FED	Increase in existing temporary reciprocal currency arrangements with the ECB and SNB.
Jul.30	FED	Introduction of longer terms to maturity in its term auction facility
Sep.14	FED	Changes in the collateral and in the schedule of Term Security Lending Facility auctions
Sep.17	BOE	extension of the drawdown period for its special liquidity scheme
Sep.18	BOE, ECB, Fed, BoJ, SNB	Measures to address the pressure in the US dollar short term funding markets
	BOE	Lend each day US dollar funds overnight against eligible collateral (repo operations)
	BOE	Swap line with FED
	ECB	adding an overnight maturity to its operations providing US dollars funding to Euro system counterparties and by increasing the amounts offered in the Term Auction Facility operations
	FED	180 billions of dollars expansion of its temporary swap lines
Sep.19	FED	Extending loans to banking organizations to finance their purchases of high-quality asset-backed commercial paper (ABCP) from money market mutual funds
Sep.26	FED, BOE, ECB,SNB	Introduction of operations to provide US dollar liquidity with a one week maturity
Sep.29	ECB	Special term refinancing operations
	FED, ECB	Doubled their swap lines from 120 to 240 billions of dollars
Oct.03	BOE	Extension of the collateral eligible in its current weekly sterling three-months repo operations
Oct.07	FED	Creating Commercial Paper Funding Facility
Oct.08	BOE	Recapitalization of the UK banking sector
Oct.13	BOE,ECB, SNB	Tenders of US dollar funding at 7,28 and 84 maturity at fixed interest rates for full allotment
Oct.15	ECB, SNB	Measures to improve liquidity in short-term Swiss franc money markets
Oct.16	ECB, MNB	Agreements on repurchase transaction which provide a facility to borrow up to 5 €bn
Oct.21	FED	Creating Money Market Investor Funding Facility
Oct.23	ECB	Changes in the framework for implementation of monetary policy in the euro area
Oct.27	ECB, DNB	Swap line of 12 billions of Euros

*ECB-European Central Bank, FED- Federal Reserve Bank, BOE-Bank of England, SNB-Swiss National bank, BoJ-Bank of Japan, MNB-National bank of Hungary, DNB-National bank of Denmark

One of the main instruments of the central banks to low the borrowing costs and stimulate the financial markets is the referent rates. The Federal Reserve Bank starting from July 2007 has reduce the referent rate for 5 percentage points (from 5,25% in July 2007, to 0,25% in December 2008), the European central bank from 4% in July 2007, to 2,5% in December 2008, and the referent rate in United Kingdom was reduce from 5,75 in July 2007 to 2% in December 2008. The expectations are that the referent rates will be reducing in the future, in order to stimulate the financial markets. On the other side, most of the central banks of emerging countries increase their referent rates in order to tighten the financial conditions, cause of their battle with high inflation rate.



Fed-Federal Reserve Bank, ECB-European central bank; BoE-Bank of England; SNB-Swiss National bank



NBS-National bank of Serbia,; BNB-National bank of Bulgaria; CNB-National bank of Croatia; NBRM-National bank of Macedonia; NBR-National bank of Romania

The financial crises had the biggest impact on the developed countries, which banks and financial institutions are part of the global financial markets. The influence of the financial crisis in emerging and Balkan countries was mostly in the real and external sector.

From all of the countries in the region, the most affected from the financial crises was Hungary. The purpose of the proposed measures from European Commission was to help in fiscal consolidation of the country, to reform the fiscal governance and to support market liquidity. Hungary received a loan from European community of 6.5 billion Euros under the European Community facility for medium-term assistance in conjunction with IMF assistance to the amount of 12.5 billion Euros and World bank-1 billion Euros. Also, under the agreement with the ECB, Hungarian government and central bank introduced two-way daily swap tenders and overnight FX swap facility providing euro liquidity. The National bank of Hungary signed agreement with primarily dealers of government securities and offered to provide liquidity in the form of secured loans to banks and primary dealers in the exchange of continuous bid-offer prices at the stock exchange for all publicly issued foreign-denominated government securities. The National bank introduced two new lending facilities: a weekly tender for two-week (fixed-rate secured loans, without a limit on the amount) and a regular tender for six month (variable-rate secured loans, for a pre-specific amount). Also, the National bank increases the referent rate from 7.75% in July 2007, to 11.5% in November 2008.

In Romania, the banks had to face increasing of their external costs. Also through the monetary tightening, the central bank manages to moderate the credit expansion, and limited the influence on the aggregate demand which stimulate the rate of inflation. In order to improve the liquidity management on the interbank money market, the central bank reduce the minimum reserve requirement ratio on leu denominated liabilities of credit institutions to 18% from 20%, and leave unchanged the existing minimum reserve requirements ration foreign currency denominated liabilities. On this way, the banks can have less money on the account in the central bank and more money on disposal (around 500 million Euros). Also, the central bank increases the referent rate from 7% in July 2007, to 10.25% in November 2008. The government proposed a package which includes lowering taxes and injecting over 10 billions Euros in the economy over the next four years. After the announcement of certain industries that they will lay off more than 800 employers because of the decreasing of production, government proposed a bonus of 1000 Euros for each job created for unemployed people.

In order to limited the effects from the unfavorable developments in financial markets the central bank in Slovakia decide to announce a decree which ensure that in the management of assets and liabilities of the banks and branch offices of foreign banks, their mutual ratio corresponds to ongoing liquidity in accordance with the circumstances and anticipated economic indicators from the date of the euro changeover in the Slovak republic. In order to stimulate the investors, the Central bank decided to reduce the referent rate starting from 4.25% in July 2007, to 3.25% in November 2008. The government proposed a program of 26 steps for protecting the Slovakian economy from the financial crisis. The program is consist of more effective use of EU funds, loans for small and medium-sized businesses, support for applied research and innovation, public spending cuts, a committee to monitor the impact of the global crisis, a push to influence the pricing policies of energy companies and preferential treatment for domestic suppliers. The government isn't planning to increase or decrease taxes or social insurances contributions. Also, to unsure the confidence in the banking sector, the protection of the money deposits in the Slovakia banks is 100%, instead of previous 90%.

Around 90% of the financial institutions in Estonia are owned by Swedish and Danish banking groups which mean that every measure which is taken in these two countries will influence the Estonia banking sector. Also, every step that the government or the central bank will take in order to protect the banking system in Estonia from the financial turmoil it will be a subject of cross-border consideration. Still, the main institutions of Estonia, the Central bank, Ministry of finance and Financial Supervision Authority have signed a specific cooperation memorandum to manage financial crisis and laid down the basis for joint creation in the even of financial crises. Also, the central bank increased the risk weights attributed to housing loans when calculating capital adequacy and increase the amount of guaranteed deposits up to 50.000 euro per customer per financial institutions. The government is preparing a preventive package with possible scope of state guarantees and loans which will be efficient in shortest period.

The global financial crisis had partly impact on the real and external sector in Macedonia. The main reason is that our production companies are very dependent from the European market where in this last months the demand is on the lowest level. The latest measures from the government were in direction of normalizing the situation in the real sector. Those measure include: four-year standstill and writing off liabilities of firms on the basis of contributions for mandatory health insurance and if they were regularly maintained, the debt will be written off completely, writing off interest rates on personal tax, profit tax, VAT, property taxes and pension insurance benefits under the condition that bonds fully pay the main debt, payment of tax debt in installments, gain taxation only if it is allocated in dividends, reduction of customs fees primarily for commodities, lower taxation of farmers. The total amounts of the measures are 330 million euro. The measures also encompass cutting down the duty tariffs which refers to raw materials for trade, economy, and information society. The measures taken by the Central bank were in direction of slowing down the credit expansion and reducing the inflation rate. In order to tighten monetary conditions, the central bank increased the referent rate few time since the beginning of financial crisis (from 5, 13% in July 2007, to 7% in November 2008). Also there was a decision about compulsory deposit by the bank in NBRM which means that if the bank register high growth in the households credit than the allowed growth rates (compared the end of every month, to end of May), the bank need to deposit a certain percentage of money at the central bank.

The slower world economic growth had impact on the countries which output grow is very dependable from their export and foreign investments. So, Serbia had downgraded its economic growth forecast for 2009 to 3.0 percent from an earlier estimate of up to 7.0 percent. Also, it freezes the increase of salaries and pension, and decrease the material expenses of the administration. Recently, the government of Serbia had agreed a 518 million dollar line with the International Monetary Fund. This 15-month standby arrangement would be available for Serbia to draw on if needed amid the financial turbulence. On the other hand, the central bank nil the reserve requirements on new external borrowing by banks to offset the increase in price of foreign credits. Also, through the change in the composition of required reserves (higher share of dinars), the central bank release foreign exchange liquidity to banks. The deposit insurance level was raised to 50,000 Euros, and the tax on interest income and foreign currency deposits is going to be abolished in 2009. In order to ease the inflation pressure, the central bank decided to tighten the monetary conditions through the increase of referent rate to 17.5% in November(from 9,5% in July 2007).

One of the most unique measures for protection from the financial crises was proposed by the government in Croatia. In order to decrees the spending, the government banned buying Christmas and New Year presents, as well organizing lunches base on this events. This interesting proposal brought disagreements between the president of Croatia and the government, cause of their different opinions about the limitation of savings. Also, the government freezes the salaries for the next time period. On the other hand, the central bank abolished marginal reserve requirement, in order to return 355 millions Euros and 129 millions dollars to the banks and to ensure additional foreign currency liquidity. Also, the vault cash is excluded from reserve requirements (to neutralize surplus liquidity preventing it from creating inflation pressures); amendments to the decision on the purchase of compulsory CNB bills broadened the calculation base for subscription of compulsory CNB bills in cases where the growth of placements to residents exceeds the permissible rate (to slow down the banks lending). Croatia's Central Bank has lowered its compulsory reserve rate for banking institutes operating in Croatia from the present 17% to 14%, thus releasing almost 11 billion euro to the sector to help tackle the first solvency problems due to the global financial crisis.

The central bank in Bosnia and Herzegovina decide all credit lines that the commercial banks are drawing from abroad, not to be calculated in the reserve requirements, with aim to stimulate the inflow of capital from the domestic banking system. Also the rate of reserve requirement is reduced from 18% to 14%, which will help to 4% of the banks to get additional liquidity of 727 millions kuni.

In Slovenia, the central bank introduce amendments of the regulation for credit risk losses of the banks with aim to reduce the original own funds deduction item in the collective assessment of financial assets. With this measure, it will be set aside 8 billion Euros for credit institutions if the market situation doesn't improve. Also, it was adopted an amendment to the Regulation on Credit Protection relating to certified real estate values. It extended until the end of 2009 the transitional period in which banks may also take valuations by court-appointed values. Because of the declining in the amounts of tolar cash being exchanged for Euros, Central bank adopted a regulation which from 1 January 2009, tolar cash may only be exchanged commission-free at the main counters of the Bank of Slovenia. The Slovenian government's aim is to maintain guarantees for the deposits of natural persons at banks and because of that it will implement a state guarantee, without a limit on the amount, for the insured deposits of natural persons and micro and small companies at banks in Slovenia.

The central bank of Montenegro make a decision for using the reserve requirements from the commercial banks for a period longer then one day, which will allow the banks to use up to 50% from the resources from the reserve requirements. Also, there is a new decision for approving short-term loans to the banks for the period not longer than 30 days. The central bank will approve these loans according to proportional participation that the banks have in the total assets of the banking sector. In ordering to protect the banks in the situation of credit expansion, which means to have enough capital to cover their costs and risks, the central bank made some changes in the decision for minimum capital standards. According to this, the banks which have annual growth rate of credits above 60% will have to have solvency coefficient at least 10%, and if the loans are larger than the coefficient of solvency should be around 12%. Decision for the minimum standards for management of the credit risk, have some new limitations for the credit activities of the banks. This decision is mostly for the larger banks, because their credit expansion can have negative impact on the economy. So, the bank that have net-credits in the balance sheet above 200 millions euro can have annual rate of growth of the credits of 30% comparing with the end of the previous year, and if the net credits are 100-200 millions than the growth is 40% and to 100 millions the growth is 60%.

Conclusion:

The world economy is facing with very serious challenges. How to answer to the crisis in the moment, in which there is not enough knowledge about the crisis dimensions and consequences for monetary and real sector as well. What kind of package of direct and indirect measures will be suitable to this period, enough efficiently to fight with current consequences and to stop further deepness of the crisis? After a long period of development in developed and emerging countries, the stability of the financial system is priority among measures. Each country is going to take measures which are efficient weapon against the crisis, not worrying too much about the level of government intervention in the market issues. The disadvantage of the Balkan countries especially Macedonia in having less developed financial systems maybe it will turn in their advantage because it means not enough globalize financial flows and absents of whole open door for entering all consequences of multidimensional crisis. But, the package of measures in these countries must have power to act fast, urgently, promptly and efficiently with determined goals towards stabilizing the financial sector. In contrary, the real sector will suffer the most.

Literature:

1. Agustin Villar: Is financial stability policy now better placed to prevent systemic banking crises?, working paper no 28, Bank for International settlements, 2008

2. Basel Committee on Banking Supervision: Bank Failures in Mature Economies, working paper No.13, BIS, April 2004

3. Claudio Borio: Assessing the Risk of banking crises, BIS Quarterly Review, December 2002

4. Commission of the European communities: From financial crisis to recovery: A European framework for action, Communication from the commission, October 2008

5. Committee on the Global Financial System: Central bank operations in response to the financial turmoil, CGFS papers, No 31, Bank for International settlements, July 2008

6. Daniel C. Hardy and Alexander F. Tieman: Innovation in Banking and Excessive Loan Growth, working paper no 08/188, IMF, July 2008

7. Dennis J.Snower: How to Solve the financial crisis, the basic principles for a rescue plan, University of Keln, October 2008

8. Elia Karakitsos: The lessons from the current crisis for Macro-theory and policy, University of Cambridge, 2008

9. European central bank: Annual report 2007

10. European central bank: Financial Stability Review, June, October 2008

11. European central bank: Research bulletin No7, June 2008

12. European commission: Proposal for revision of bank capital requirements rules, October 2008

13. European commission: press info for state aid of the certain countries.

14. European commission: Proposal to increase minimum protection for bank deposits, October 2008

15. Franklin Allen and Elena Carletti: Financial system: shock absorber or amplifier?, working paper no 257, BIS, July 2008

16. Horst Siebert: An international rule system to avoid financial instability, Kiel Institute for the World economy, working paper 1461, November 2008

17. Hui Tong and Shang-Jin Wei: Real Effects of the Sub prime Mortgage Crisis: Is it a Demand or a Finance Shock?, working paper 08/186, IMF, July 2008

18. IMF: Regional Economic outlook: Europe, World economic and financial survey, October 2008

19. International Monetary Fund: Food and fuel prices-recent developments, macroeconomic impact and policy responses, September 2008

20. Laurent Clerc: A primer on the sub prime crisis, occasional papers no.4, Banque de France, February 2008

21. Luc Laeven and Fabian Valencia: Systemic Banking Crises: A New Database, working paper 08/124, IMF, September 2008

22. Olivier J. Blanchard: The tasks Ahead, working paper 08/162, IMF, November 2008

23. Saurina Jesus, Persaud D. Avinash: Will Basel II help prevent crises or worsen them?, Finance and Developments, quarterly magazine of the IMF, June 2008, volume 45

24. web pages of the central banks

25. World bank: EU 10 regular economic report, October 2008

26. World bank: The unfolding crisis, Implications for Financial Systems and their oversight, World bank Financial system and Development economics departments, October, 2008

27. www.ec.europa eu/economy-finance/focuson

28. www.ecb.int

29. www.europa.eu.int

30. www.eurunion.org

31. www.forbes.com

32. www.ft.com/indepth/globarl-finance.crisis

33. www.ifw-kiel.de (Kiel Institute for World economy)

34. www.mostlyeconomics.worldpress.com

35. www.seebiz.eu

36. www.webnet.oecd.org

Center for Economic Analyses

Publisher: Center for Economic Analyses - CEA

For the publisher: Marjan Nikolov

Title: CEA JOURNAL OF ECONOMICS

Cover & pre-press: GLOBAL Communications, Skopje

Skopje, December 2008

Major Sponsors:

Stopanska Banka AD Skopje and USAID BEA Project

STOPANSKA BANKA AD - SKOPJE
member of NBG group

USAID | MACEDONIA
FROM THE AMERICAN PEOPLE

This publication is supported by the Open Society Institute Think Tank Fund Budapest

Suporters:

Ministry of Finance
AD Ohridska Banka
Ministry of Foreign Affairs
University of SEE Tetovo
Municipality of Strumica