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**DETERMINANTS OF COUNTRY IMAGE – CROATIA’S IMAGE IN THE REPUBLIC OF
MACEDONIA**

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DETERMINANTS OF COUNTRY IMAGE – CROATIA’S IMAGE IN THE
REPUBLIC OF MACEDONIA

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Tatjana PETKOVSKA MIRCEVSKA, PhD²

ABSTRACT

The main purpose of this paper is to reveal the overall image of Croatia among Macedonian citizens. ANOVAs test was employed to measure whether the overall image of Croatia among Macedonian citizens is homogeneous and which group has the most favorable opinion about Croatia. The empirical data were collected by using a structured questionnaire and 216 respondents grade the importance for each of eighteen country image determinants on a ten-point Likert scale.

Country image as a multidimensional construct influence on associations connected with a country on consumers’ evaluation of products coming from it. Understanding of the determinants of the country image would be beneficial for academic and business parties.

KEYWORDS: country image, Croatia, dimensions

JEL CLASSIFICATION: M31

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1. INTRODUCTION

The importance of exploring the determinants of country image is increasing due to the continuous growth of industry internationalization and globalization. Identifying and measuring relevant determinants of country image will contribute for defining each component as favourable or unfavourable, whether they affect product quality perceptions and purchase decisions and how they can be used in developing effective marketing strategies. Countries evoke different product images in consumers' minds, so consumers can use country image in product evaluations when they are unable to detect the true quality of a country's products before purchase³. Significant amount of research has been devoted to examining the influence of country image structure on consumer evaluations of products⁴. Contrary, there is limited number of local researches in ex- Yugoslav countries that investigated the dimensions of country image⁵. The growing literature on country image has indicated that consumers develop stereotypical images of countries. However, despite the globalization and stereotypical images, countries are perceived differently in particular country. Exploring the country image of Croatia would be from high importance for Croatian producers and economic institution⁶. This article presents a study performed in the Republic of Macedonia undertaken to explore the different determinants of country image of Croatia among Macedonian citizens. We investigate the country image of Croatia as multidimensional construct comprise of eighteen dimensions: the country cares for environmental protection, has a high quality life, supports humanitarian and human rights issues, is an enjoyable place to visit, has a high level of education and research, is politically stable, has warm and friendly citizens, is regarded as a nation of culture, provides good investment opportunities, has products that are of world class quality, is highly regarded worldwide, allows citizens to have a strong influence on political decisions,

³ Martin, I. M., & Eroglu, S. (1993)

⁴ Laroche, M., Papadopoulos, N., Heslop, L. A., & Mourali, M., (2005); Samiee, S., (1994); Ozsomer, A., & Cavusgil, S. T., (1991); Papadopoulos, N., Heslop, L. A., & Beracs, J., (1990)

⁵ Ozretic-Dosen, D., Skare, V., & Krupka, Z., (2008); Ozretic-Dosen, D., Skare, V., & Krupka, Z., (2007); Ozretic-Dosen, D., & Devila, I., (2010); Ozretic-Dosen, D., & Previšić, J., (2001)

⁶ Ozretic-Dosen, D., & Previšić, J., (2001)

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works toward international cooperation, has companies recognized as sound and trustworthy business partners, is an open, forward looking country, has products with innovative features, has companies known for their ethical and responsible approach to business and has companies that are internationally competitive and known. We employee ANOVAs test to measure whether the overall image of Croatia among Macedonian citizens is homogeneous and if there statistically significant differences in grading the importance of each dimension of country image among different group of respondents.

The contribution of this study is based on revealing of relevant finding for the perceptions that Macedonian citizens have for Croatia. Findings from this study would be beneficial for all concerned parties: academic, private and public companies interested for the image of a certain country.

LITERATURE REVIEW

Many studies demonstrated that country image influences the evaluation of products⁷. The other group of authors ⁸ found that consumer perceptions of a give product's country of origin are based on cognition, affect and conations. Others,⁹ claimed that the total effects of country image on purchase attitude appear to be substantial. Their findings suggest that country of origin and beliefs simultaneously influence consumer attitude. Country image and product beliefs affected product evaluations simultaneously regardless of consumers' level of familiarity with a country's¹⁰.

Country of origin reflects a perception of consumers about the product produce in a given country¹¹. The image of a country consists of a vast number of components such as tradition, history, politics, areas that are very difficult to manage and

⁷ Samiee, S., (1994); Ozsomer, A., & Cavusgil, S. T., (1991)

⁸ Papadopoulos, N., Heslop, L.A., & Beracs, J., (1990)

⁹ Knight, G. A, & Calantone, R. J., (2000)

¹⁰ Laroche, M., Papadopoulos, N., Heslop, L. A., & Mourali, M., (2005)

¹¹ Han, C.M., (1989); Bilkey, W. J., & Nes, E., (1982), Papadopoulos, N., Heslop, L.A., & Beracs, J., (1990)

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consequently to be measured. Country of origin image is often a cue for evaluating products, and some authors suggest that favourable perceptions about the country result in the according of favourable attributions to brands from that country¹².

In a meta-analysis, was concluded that country image appears to influence consumer evaluation of product quality, risk, likelihood of purchase, and other mediating variables¹³. It was noted that the nature and strength of origin effects depend on such factors as the product category, the product stimulus employed in the research, respondent demographics, consumer prior knowledge and experience with the product.

The group of authors¹⁴ defined country image as the overall consumers' perception of products from a particular country, based on their prior perceptions of the country's production and marketing strengths and weaknesses. Other authors define country image as the total of all descriptive, inferential and informational beliefs about a particular country¹⁵. Country of image and country-of-origin effects examines how consumers perceive countries and products emanating from a particular country.

Many authors investigate the multidimensional construct of country image. In the first country image study, it was claimed that the image is created by determinants as representative products, national characteristics, economic and political background, history, and traditions and it has a strong influence on consumer behaviour¹⁶. In the following period, many determinants for defining and evaluating country image were employee in different studies and close examination of the country image research findings revealed consistency among certain determinants across the majority of the studies¹⁷. Therefore, it were found four consistent dimensions of country image in

12 Paswan, A. K., and Sharma, D., (2004)

13 Liefeld, J.P., (1993)

14 Roth, M. S., & Romeo, J. B., (1992)

15 Martin, I. M., & Eroglu, S. (1993)

16 Nagashima, A., (1970)

17 Nagashima, A., (1977); White, P. D., (1979); Narayana, C. L., (1981); Cattin, P., Jolibert, A., & Lohnes, C., (1982); Jaffe, E. D, & Nebenzahl, I. D, (1984); Johansson, J.K., and Nebenzahl, I. D., (1986); Han, C. M, and Terpstra, V., (1988)

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previous studies -innovativeness, design, prestige, and workmanship¹⁸. An advantage of identifying country image dimensions is to generate greater comparability and generalizability of research findings. They employee product-country matches in predicting a consumer's purchase intention and willingness to buy the foreign products. Beside the fact that positive image of a country influence consumers' evaluations of products and buying intentions from that country, some authors felt that a country's image is of paramount importance and that a country should be treated as a brand¹⁹.

METHODOLOGY

The aim of the study is to analyze the overall image of Croatia among Macedonian citizens based on relevant image dimensions and the importance of image dimensions.

The survey was based on the methodology employed in the survey of Ozretic-Dosen, Skare & Krupka (2008) consistent with the research of Papadopoulos, Marshal and Heslop (1988) and Papadopoulos, Heslop and Bamossy (1990). Ozretic-Dosen, Skare & Krupka (2008) employed matrix for analyzing strength and weakness of small and great importance according the ratings of the importance for each image determinant.

The empirical data of this study was collected in the period from November 2015 till April 2016, by using a structured questionnaire, consisted of two sections: demographic questions (gender, age, education, income etc.) and statements assessing country image dimensions. Respondents from three groups (citizens who visit or transit Croatia and citizens who had never been in Croatia) were asked to grade the importance for each of eighteen country image determinants on a ten -point Likert scale (from 1="not important at all" to 10 = "from high importance").

A non-probability sampling method was used, conventionally distributing the questionnaire to 320 respondents and 304 responses were received. After conducting

18 Roth, M.S, & Romeo, J.B., (1992)

19 O'Shaughnessy, J., & O'Shaughnessy, N.J, (2000)

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the data screening procedure, 216 valid responses were remained (67.5% response rate). 118 of the respondents visit the Croatia, 80 had never been in Croatia and 18 only transit the country.

On the basis of the survey of Ozretic-Dosen, Skare & Krupka (2008) two hypotheses were set:

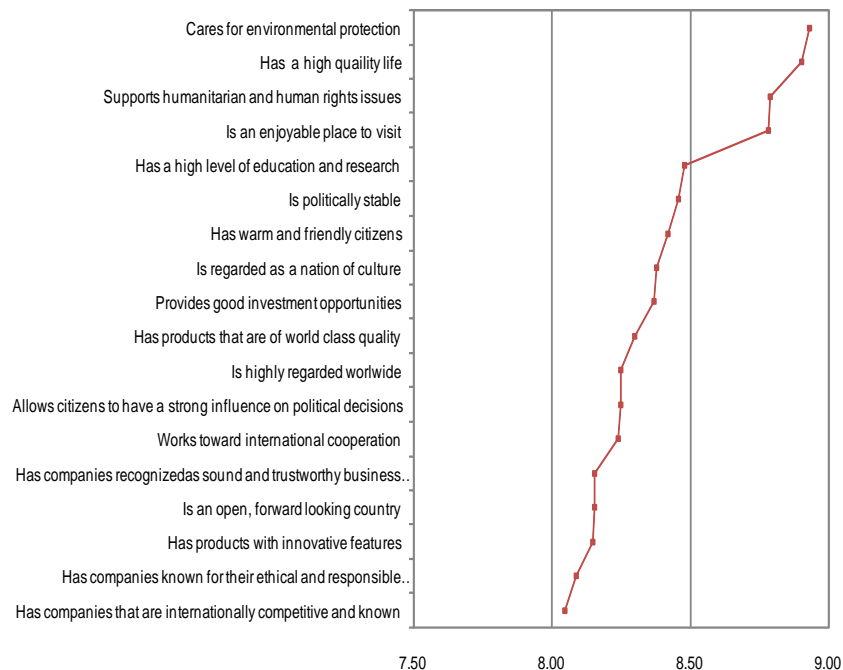
H1: The overall image of Croatia among Macedonian citizens is homogeneous.

H2: At least one of the groups (people who visited, who transited and who have not visited Croatia) has a more positive opinion about Croatia.

RESULTS

First, the entire respondents grade the individual dimension for evaluating country image. Therefore, cares for environmental protection (8.93) and high quality of life were ranked as the most important determinants. Contrary, the ethical dimension and responsibility of the country (8.09) and international competitiveness (8.05) have lowest grades (Figure 1).

Figure 1: Importance of image dimensions for assessing countries

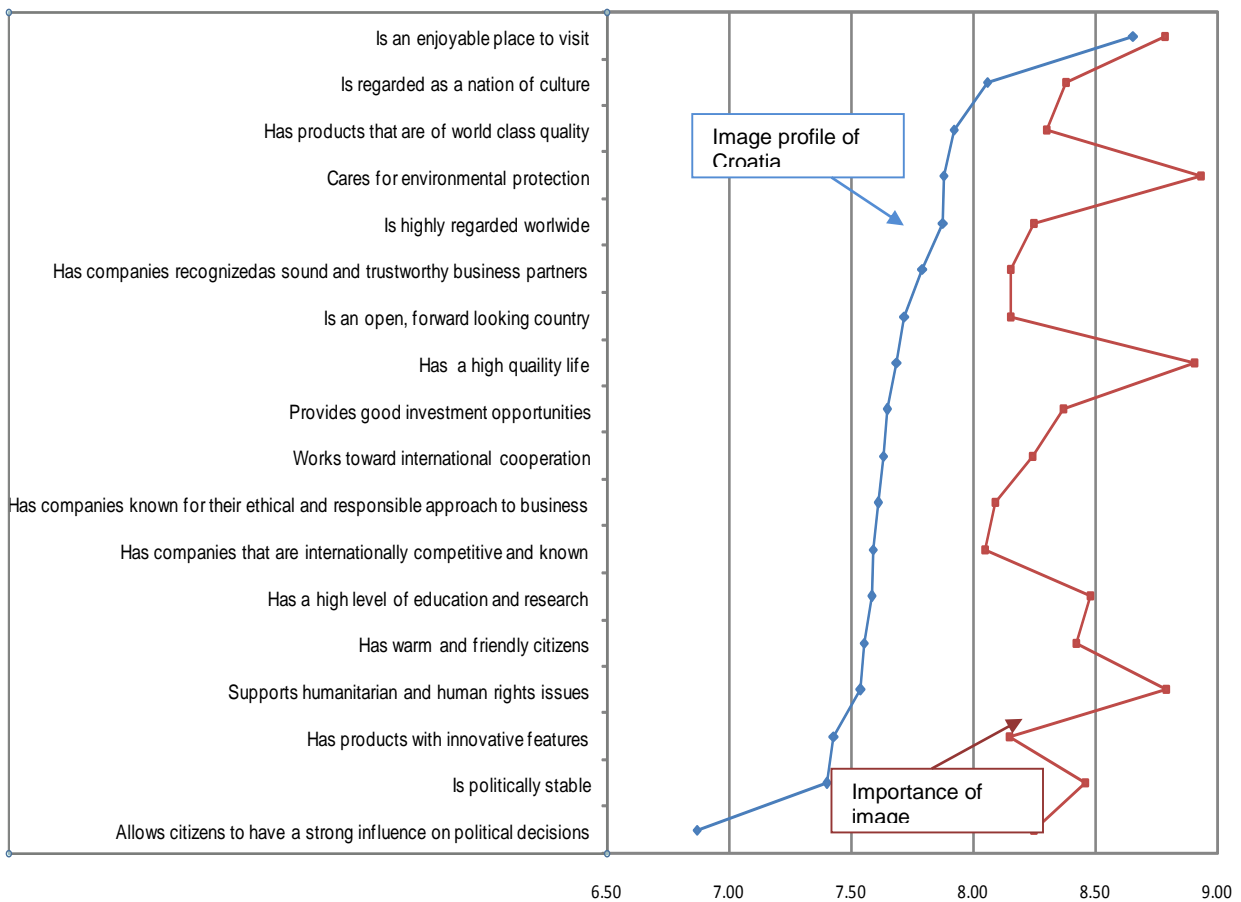


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Employing the same scale, respondents’ grade image profile of Croatia compared with the importance of image dimensions for assessing countries (Figure 2).

Respondents perceive Croatia as a country which is an enjoyable place to visit and care for environmental protection, dimensions which are rank as important in overall evaluation for assessing countries. Contrary, on the other dimensions from high importance in overall evaluation for assessing countries, respondents rank Croatia as a country which does not have a high quality life, does not support humanitarian and human rights issues and is not politically stable.

Figure 2: Comparison of the image profile of Croatia and the importance of image dimensions for assessing countries

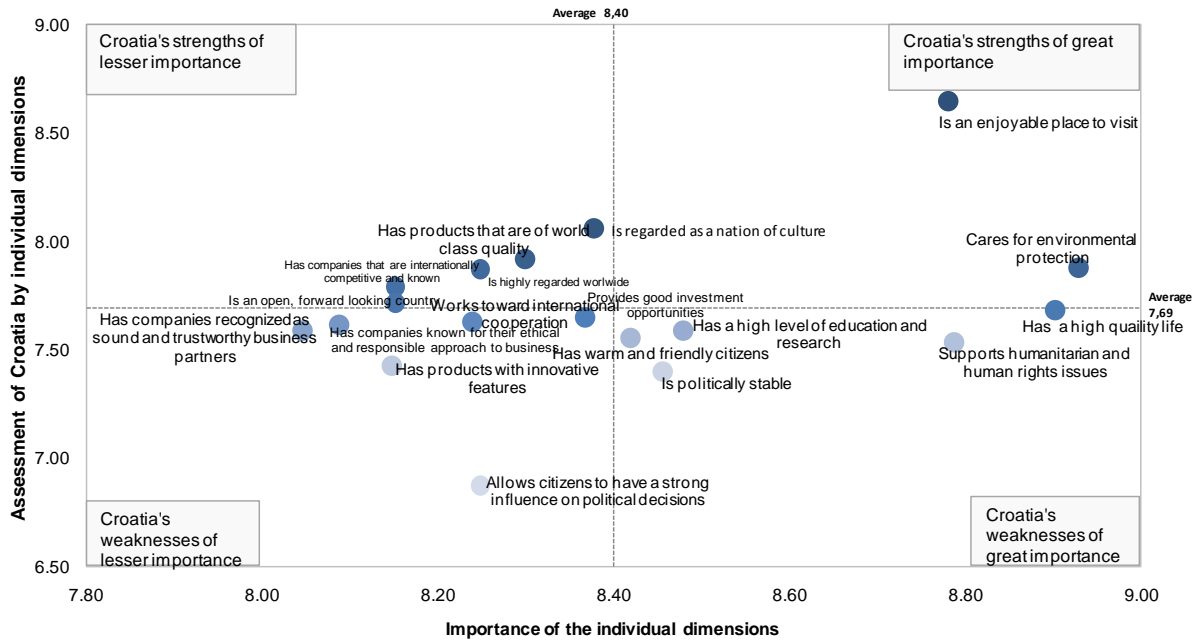


great importance respondents indicate not having high quality of life, high level of education and research and having friendly citizens. Respondents do not see Croatia as politically stable country and as country which support humanitarian and human

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rights issues. Other dimensions are divided in two remaining categories and they are Croatia's strengths and weaknesses of lesser importance.

Figure 3: Combined analysis of the assessments of Croatia by individual dimensions and the importance of the individual dimensions



Source: Authors calculation

Table 1: Image profile of Croatia for citizens who had visited Croatia, had been in transit through Croatia and who had not visited Croatia

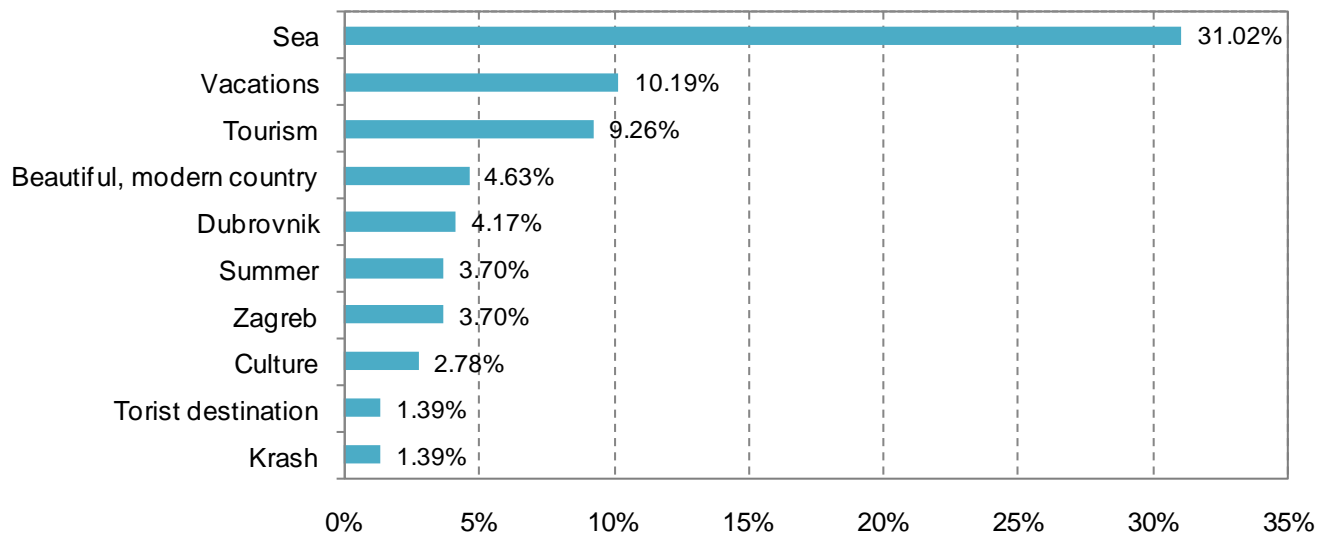
DIMENSIONS	HAD VISITED (n=118)	HAD BEEN IN TRANSIT (n=18)	HAD NOT VISITED (n=80)	Anova (p<0.05)
Is an enjoyable place to visit	8.771	8.500	8.488	0.519
Cares for environmental protection	8.076	7.778	7.588	0.202
Supports humanitarian and human rights issues	7.568	7.444	7.475	0.933
Is politically stable	7.458	7.611	7.238	0.664
Has a high level of education and research	7.669	7.611	7.425	0.659
Has a high quality life	7.864	7.389	7.450	0.311
Provides good investment opportunities	7.814	7.444	7.425	0.334
Has warm and friendly citizens	7.788	7.278	7.238	0.154
Is an open, forward looking country	7.966	7.111	7.450	0.067
Has companies recognized as sound and trustworthy business partners	7.788	7.278	7.338	0.170
Is regarded as a nation of culture	8.254	7.833	7.800	0.172
Works toward international cooperation	7.907	7.278	7.275	0.049
Has companies known for their ethical and responsible approach to business	7.915	7.389	7.188	0.020
Is highly regarded worldwide	8.195	7.722	7.400	0.015
Has companies that are internationally competitive and known	8.153	7.000	7.400	0.004
Has products that are of world class quality	8.237	7.944	7.425	0.021
Has products with innovative features	7.780	7.278	6.900	0.020
Allows citizens to have a strong influence on political decisions	6.992	6.000	6.850	0.254

N=216
Source: Authors' calculations

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The hypothesis H1, which stated that the overall image of Croatia among Macedonian citizens is homogeneous, is partially confirmed. Results of the respondents' assessments of Croatia by individual dimension were divided into three groups: citizens had visited Croatia, who had only been in transit through Croatia and who had not visited Croatia. We employed ANOVA and statistically significant differences ($p < 0.05$) were found for six dimensions of lesser importance: country has companies that are internationally competitive and known, is highly regarded worldwide, has companies known for their ethical and responsible approach to business, has products with innovative features, has products that are of world class quality and works toward international cooperation. For all remaining dimensions, statistically significant differences were not found. Results are shown in Table 1. The respondents that have visited Croatia grade each determinant higher compared to other groups respondents. They have a more positive and a more complete picture for Croatia, consequently H2 is confirmed.

Figure 4: Categorization of top 10 associations about Croatia among Macedonian citizens



Finally, respondent categorized the primary associations they have for Croatia. Most of the respondents associate Croatia with sea (31.02%), followed by associations related to vacation (10.19%) and tourism (9.26%).

CONCLUSION

Country image is a complex research issue, one with potentially important implication for investor, public and private institution. Country image plays an important role in consumers' market behaviour. All the involved parties can benefit from emphasizing and promoting dimensions of great importance for Croatia.

Respondents do not see Croatia as politically stable country and as country which support humanitarian and human rights issues. Also, as the weaknesses of great importance respondents indicate not having high quality of life, high level of education and research and having friendly citizens. All the five dimension of high importance should be considering as issues for improvement. Country image as a multidimensional construct is not stable, and might improve over time. Positive or negative country of origin image affected the perception of product manufactured in a certain country. Knowledge of the determinants of the country image construct, their nature, intensity, direction and of the possibilities of their effective management is necessary indeed for strategic marketing reflection and action. Results of a number of comprehensive research projects support assumptions on the importance of the impact that country image has on the decisions of consumers and businessmen with respect to the choice of products, services, business partners, markets, as well as tourist and foreign investment destinations (Ozretić Došen & Krupka, 2007). Therefore, it's particularly important to build a stable country with an economy, that has an image that encourages investing.

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THE EU MEMBERSHIP AND ITS EFFECTS ON OWNERSHIP OF BANKING SYSTEM: THE CASE OF THREE SOUTH EAST EUROPEAN COUNTRIES

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THE EU MEMBERSHIP AND ITS EFFECTS ON OWNERSHIP OF BANKING SYSTEM: THE CASE OF THREE SOUTH EAST EUROPEAN COUNTRIES

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ABSTRACT

The aim of this paper is to assess the impact of membership on a country in EU on the ownership of its banking system. The ownership of a banking system is important for a country. A growing number of studies provide empirical evidence that well operation of financial systems accelerates long-run economic growth by allocating funds to more productive investments than poorly developed financial systems. So, the foreign ownership of banking system, if the owners are from more developed economies, through know how can influence for greater financial intermediacy and for better allocation of resources, too. Also if the owners are global systemically important financial institution they can provide financial support and can make a bank competitive advantage with cheap credit lines. The down side is that all the decisions are taken on group level and the subsidiary can be affected of strategy for deleveraging or reduced support although the driver is the economic conditions of the mother company. In order to evaluate the impact of the EU membership, this paper will compare the ownership of the banking systems in Romania and Bulgaria before and after the EU accession. Also, the analysis will include the ownership of Macedonian banking system, and having in mind the changes in the other two sample countries, will be assessed the impact of EU membership on the ownership of the banking system.

KEYWORDS: Ownership, banking system, EU, membership

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1. INTRODUCTION

There is common consensus between the academic community about the importance of the banking system for economic development of a country. There is a sizable amount of theoretical literature on the relationship between financial development and economic growth. Developing a modern, market-oriented banking sector was a particular challenge for the transition economies of CESEE. They all inherited a monobank system, where banking activities were entirely subservient to central planning (IMF, 2012). The first reform step created a two-tier system with a central bank in charge of monetary and exchange rate policies and financial sector oversight and other parts of the monobank system transformed into state-owned commercial banks. The early phase of transition was marred by frequent banking crisis and difficulties to secure macroeconomic stability. There was little experience with modern banking practices. At least in the relatively small economies with aspirations to join the EU, a consensus emerged over time that privatization itself was not sufficient to improve bank performance but that involvement of a strategic investor was critical. As domestic strategic investors were in short supply, in practice this meant foreign control of a large share of CESEE banking systems. The timing of foreign bank entry differed across CESEE with Hungary registering a substantial foreign bank ownership already in the early 1990s while macroeconomic instability or political resistance delayed the process into the late 1990s in many other CESEE countries.

There are a lot of relevant studies that empirically confirm the positive effects of EU membership on new EU countries. Rapacki and Próchniak (2014) argue that EU enlargement significantly contributed to economic growth of the CEE-10 countries. This claim is supported by both, the convergence and economic growth determinants analyses. The econometric test of economic growth determinants shows that four variables related to the EU enlargement: FDI inflow, economic freedom, progress of structural reforms, and aid inflow, are positively and significantly correlated with GDP growth rates in the CEE countries.

The main question that this paper will answer is whether the EU accession which is accompanied by economic development has influenced on banking system ownership.

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The link between the EU accession and ownership on banking system will be analyzed through the prism of the banking systems of Bulgaria and Romania before and after the EU accession. Bulgaria and Romania accessed EU in 2007 so there is enough time to assess the effect of EU membership. The final goal is to assess whether the accession on Macedonia in EU will have impact on the ownership of the banking system. In order to assess the impact, the ownership of the banking system will be compared before and after the EU accession.

2. BANKING SYSTEM OF ROMANIA

The banking system of Romania in 2006 is comprised of 40 credit institutions (Central Bank of Romania, 2007). From them, 31 were banks with majority foreign capital. Their share in the total assets in the banking system was 62%. As can be seen in table 1, the foreign investors are mainly from developed EU countries. The share of foreign shareholders in that time was not as high as in Croatia and Bulgaria let's say where banks with majority foreign capital comprised above 80% of their banking systems.

Table 1 – Structure of foreign shareholding in the Romanian banking system

	% of total capital						
	Austria	Greece	Italy	France	Netherlands	Other	Total
Dec. 2000	3.2	8.5	0.4	6.8	3.1	18.4	40.4
Dec. 2001	21	6	1.1	3.4	8	13.7	53.2
Dec. 2002	24	8.2	2.7	5.7	3.5	11.7	55.8
Dec. 2003	21.5	11.1	4.6	5.9	4.5	10.6	58.2
Dec. 2004	24.6	10.1	8.4	5	5.9	16.6	70.6
Dec. 2005	21.8	12.4	5.8	5.6	8.2	15.1	68.9
March 2006	20.9	14.7	5.9	5.4	7.9	15.4	70.2

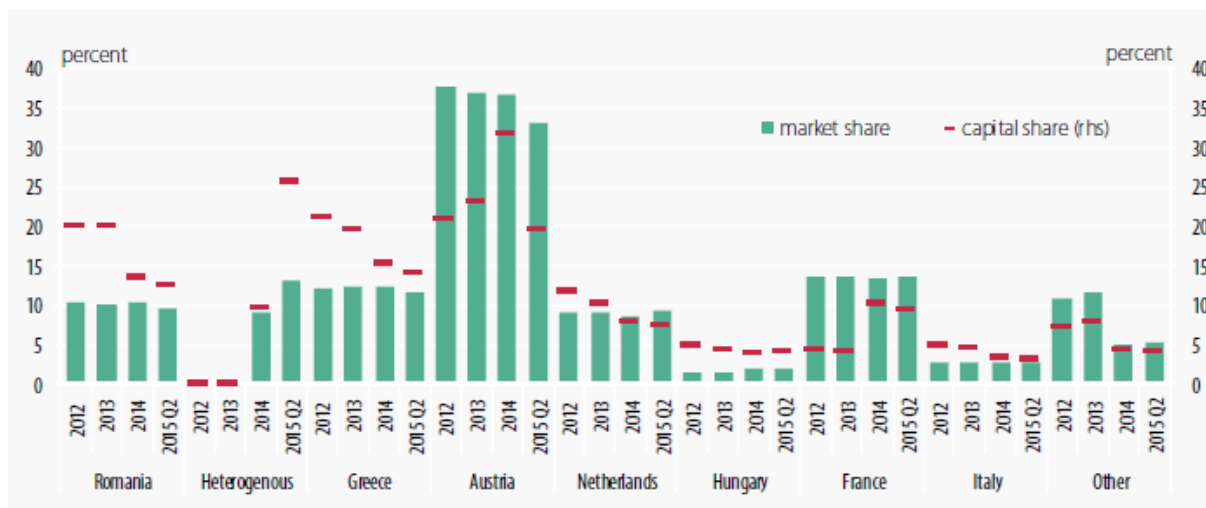
Source: Central Bank of Romania, 2007

In that time, the Central bank of Romania (2007) notes the positive effect from foreign shareholders that came from foreign financing, better credit risk management and improved corporate governance.

In 2015, compared to 2006, the number of credit institutions is unchanged. The number of banks with foreign ownership is increased to 34. The biggest change is in their market share. In the period of 9 years, after the accession of Romania in EU, their dominance in the assets of the banking system is increased for almost 30 pp and is 91% (Romanian Central Bank, 2016).

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Figure 1 – Credit institutions’ share capital as a percentage of total capital and market share by country of origin



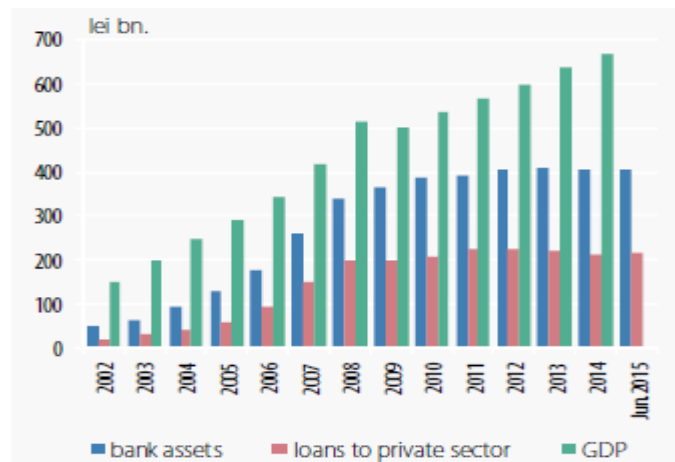
Source: Central Bank of Romania, 2016

As can be seen, from figure 1, the countries that are dominant owners of Romanian banking system remain unchanged. In this period of nine years what is changed is their market share on behalf mostly on domestic banks. The banks with Austrian owners have doubled their market share. Also, the banks with owners from Netherlands and France have increased their market share substantial. Only the banks with Greek ownership have preserved the same market share which is due on the difficulties in the Greek banking system.

The accession of Romania in EU further enhanced the dominant position of banks with owners from more developed EU countries. Positive effect on financial intermediation was felt in the period 2007-2009 (figure 2) that lead to increase of banking assets and loans to private sector. After 2009, the effects from EU debt crisis felt in Romania mostly through rise of NPL portfolio which resulted in credit granting contraction.

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Figure 2 – Bank assets and loans to private sector

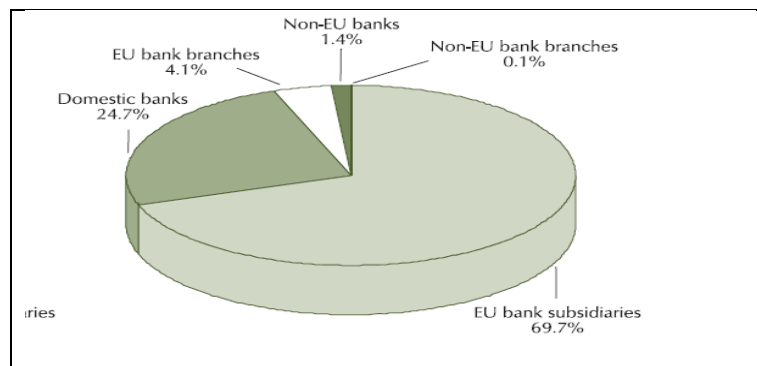


Source: Central Bank of Romania, 2016

3. BANKING SYSTEM OF BULGARIA

Bulgarian banking system in 2015, eight years after Bulgarian membership in EU is comprised of 28 banks.

Figure 3 - Market share of domestic and foreign banks in Bulgaria



Source: Central Bank of Bulgaria, 2015

As can be seen from Figure 3, 70% of the banking system is dominantly owned by EU bank subsidiaries. Compared to the previous sample country, although the share of foreign banks is dominant still the domestic owned banking share is bigger.

Historically, the trigger that led to transformation of Bulgarian banking system was the financial crisis 1996/97 after which the Bulgarian banking sector has gone through an impressive process of stabilization in recent years, which has involved the privatization of most banks, predominantly through foreign investors. Bad governance, weak regulatory oversight, unsound credit policies, and lack of privatization efforts contributed

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to the deterioration of the balance sheet of the banking system culminating in a severe banking crisis and a wave of bank failures in 1996–1997. ONB notes the positive effects of changes in ownership structure after 1997 on deepening of financial intermediation, although the share of banking assets in percent of GDP remains relatively modest by international and even Central and Eastern European (CEE) standards.

Table 2- Market share of domestic and foreign banks in Bulgaria

Banking Institutions							
	1997	1998	1999	2000	2001	2002	2003
Number of banks	34	34	34	35	35	34	35
Share of private banks in total assets (%)	32.8	39.4	53.4	80.2	80.1	83.5	98.0
Share of foreign banks in total assets (%)	18.0	32.3	44.7	73.3	75.0	72.0	86.0
Number of employees	22,266	21,616	20,997

Source: Central Bank of Bulgaria, 2004

As can be seen from Table 2 the share of foreign bank in total assets was dominant starting from 2000 or seven years before the accession of Bulgaria in EU. So figuratively speaking the banking system has entered EU way before Bulgaria itself and had positive influence through the know how of the EU owners and cheap sources of funds. After EU accession having in mind the ownership of the banking system, there were no changes so there is no empirical evidence of immediate impact on the membership status and banking system ownership. Still, Tochkov and Nenovsky (2009) argue that the accession to, and the membership, in the EU might have contributed to marked improvements in bank performance. They find connection between the signing of the Treaty of Accession in 2005 and the largest gains in technical efficiency over the sample period. The first year of EU membership was accompanied by improvement of cost and allocative efficiency.

According to Tochkov and Nenovsky (2009) there is empirical evidence that the changes in ownership structure of the banking system contributed for better efficiency of the banking system. As we mentioned earlier this is important for the support that the banking system is providing to the whole economy. The reason for the lower efficiency in the late 1990s and early 2000s they are looking in the fact that most banks were reluctant to lend as they were still haunted by the aftermath of the 1996 crisis. This changed in 2004 when foreign banks were attracted by higher rates of return and the prospect of Bulgaria’s EU accession, poured resources into the financial system through

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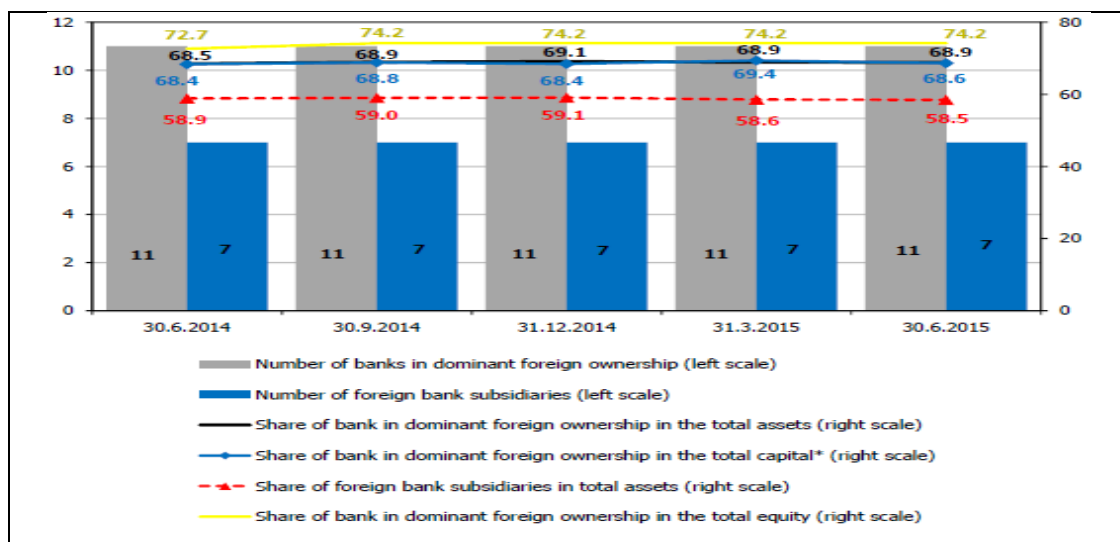
their Bulgarian subsidiaries creating a credit boom reflected in the jump in efficiency scores.

The foreign banks were significantly more cost efficient and more technically efficient than domestic banks which is consistent with the findings of previous studies on transition economies. The majority of foreign banks in Bulgaria are owned by large and established banks from Germany, France, Italy, and Austria giving them access to advanced technology and expertise, better risk management and corporate governance, and capital from their parent banks. Moreover, foreign banks have the advantage of counting foreign firms and the most creditworthy Bulgarian companies as their customers (Koford and Tscheogl, 2003).

4. BANKING SYSTEM OF MACEDONIA

As of 30 June 2015, the number of institutions that perform banking activities in the Republic of amounts fifteen banks and three savings houses (NBRM, 2015). Eleven banks are predominantly owned by foreign shareholders, and seven of them are subsidiaries of foreign banks.

Figure 4- Ownership structure of Macedonian banking system



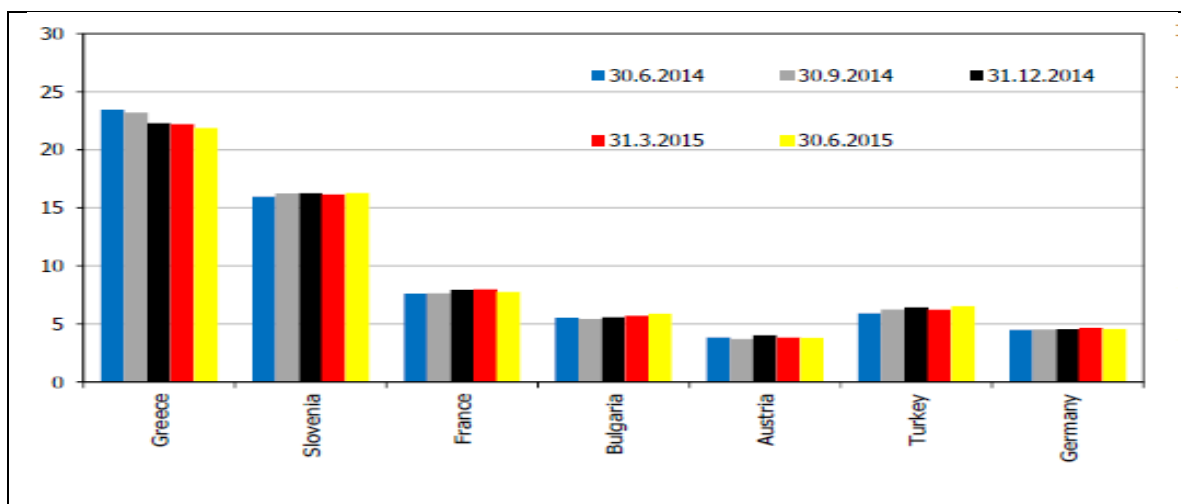
Source: NBRM, 2015

The origin on foreign owners by country puts Greece and Slovenia on the top two places with more than 22% and 15% share in total assets of the banking system (Figure

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5). Two banks are dominantly owned by Greek banks from which one is a large one. One large bank is owned by Slovenian bank.

Figure 5- Market share of banks by assets - origin of the dominant foreign shareholder



Source: NBRM, 2015

Giustiniani and Ross (2008) argue that foreign bank presence, compared to other Eastern European countries, is limited and mostly not from first-tier foreign banks. The foreign banks are from neighbouring countries – namely Bulgaria, Greece, Slovenia and Turkey – and in some cases, appear to service mainly their nationals’ business interests.

As a consequence, the transfer of know-how, innovative technology, good governance and other international best practices (e.g. risk management) from abroad remains slow.

The historical perspective shows same story as the other two sample countries. The process of privatization of the biggest Macedonian bank in 2000 has changed the banking landscape and the foreign investors had 45% share in the banking system. After 2000 their share has increased continuously. A lot of authors argue that the number of banks is too large having in mind the size of the market. Boshkoska (2013) argue that it is necessary to lower the number of banks existing in Macedonia through the processes of merging, overtaking of the smaller banks by the big ones, in order to strengthen the competition in the banking sector. The bank consolidation will increase market share, increase competitiveness, profitability and rationalize expenses and strengthen the bank capital. Expect from the process of consolidation that can have influence on the ownership

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of the smaller banks, changes in ownership can be expected in banks that are owned by Greek or Slovenian owners. The financial condition of the parent companies and the directions from EU commission can result in change of the ownership structure of the parent company or subsidiaries.

5. CONCLUSION

The pattern in all three sample banking system is clear. There is no visible evidence that EU membership can have effects on the ownership of the banking systems. In all three sample countries the banking system is dominantly owned by foreign owners after process of privatization and transformation that was taken by the states. So the EU banking groups are present in the sample countries way before the process of accession is even started. EU membership didn't have any impact on the ownership structure of the banking system in Bulgaria and Romania. Still, in Romania after EU membership, the foreign owners strengthened their position and increased the market share.

Regarding Macedonian banking system, foreign bank presence, compared to other Eastern European countries, is limited and mostly not from first-tier foreign banks. The changes in the ownership structure can be expected from two factors, consolidation of the banking system and the financial condition of the parent companies from Greece and Slovenia. The number of banks is too large having in mind the size of the market. It is necessary to lower the number of banks existing in Macedonia through the processes of merging, overtaking of the smaller banks by the big ones, in order to strengthen the competition and effectiveness in the banking sector.

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**ESTIMATING POVERTY AND INEQUALITY IN MACEDONIA USING LORENZ CURVE
FRAMEWORK**

UDC: 364.662:303.22(497.7)

**ESTIMATING POVERTY AND INEQUALITY IN MACEDONIA USING
LORENZ CURVE FRAMEWORK**

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Dushko JOSHESKI²

ABSTRACT

The primary aim of this short paper is to show how to construct poverty measures from grouped data, i.e., to show how to derive poverty measures from parameterized Lorenz curve. For this purpose, Gaurav Datt's approach has been applied. The derived poverty measures are estimated for the case of the Republic of Macedonia, using interactive software package "Povcal", created by the World Bank.

Our findings suggest two main conclusions: 1) that the high poverty level in Macedonia is accompanied with a moderate level of income inequality, and 2) that the transmission mechanism from the economic growth to poverty reduction in Macedonia is working properly.³

KEYWORDS: parameterized Lorenz curve, QC Lorenz curve, FGT index.

JEL CLASSIFICATION: C13, C15, I32, D31, D63

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1. INTRODUCTION

The grouped data are the most common form of information available to researchers, when it comes to the problem of poverty and income distribution. In general, there are two basic methods when constructing poverty measures from grouped data: the interpolation methods⁴, and the methods based on parameterized Lorenz curve. In this paper, the Gaurav Datt's approach, which is based on a parameterized Lorenz curve⁵, with a General Quadratic functional form, has been used.

In accordance with our knowledge, this is the first attempt in Macedonia using a parameterized Lorenz curve: 1) to construct poverty measures of a so-called P-alpha class of measures, and 2) to calculate poverty measures' elasticities with respect to the mean income and the Gini index.

The paper structure is as follows: in the first part, some relevant papers and studies related to our paper are presented. The second part explains the methodological background and sources of data. In the third part the obtained results are being sublimated, while the fourth part concludes.

2. LITERATURE REVIEW

In the literature not to many attempts are being made to test the theoretical validity and empirical performance of the alternative functional forms of the Lorenz curve⁶. First, Kakwani⁷ set the mathematical formulation for parameterization of the Beta Lorenz curve, and later Villasenor and Arnold⁸ did the same for the General Quadratic (GQ) Lorenz curve.

⁴ Kakwani, N., and Subbarao, K. (1993). Rural Poverty and its Alleviation in India. *Economic and Political Weekly*, Vol. 25.

⁵ Datt, G. (1998). Computational Tools for Poverty Measurement and Analysis. *FCND Discussion Paper No.50*.

⁶ Minoiu, C., and Reddy G., S. (2009). *Estimating Poverty and Inequality from Grouped Data: How well do Parametric Methods Perform?*, Journal of Income Distribution, pp.160-178.

⁷ Kakwani, N. (1980). On a class of poverty measures. *Econometrica* 48 (2), p.p. 437-446.

⁸ Villasenor, J. A., and Arnold, B.C. (1984). *The general quadratic Lorenz curve*. Technical report, Colegio de Postgraduados, Mexico City (mimeo).

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In his seminal paper, using Foster-Greer-Torbeke (FGT) class of poverty measures, Datt⁹ has showed how to construct poverty measures when grouped data are available. In the same paper, he has explained the means of constructing point estimates of the elasticities of poverty measures with respect to the mean income and the Gini index. To estimate the Lorenz curve, he has used the mathematical formulations (functional forms of the GQ and Beta Lorenz curve) proposed by Kakwani and Villasenor and Arnold.

Essama-Nssah¹⁰, following the procedure proposed by Datt, uses regression analysis to fit the data to a model such as the General Quadratic model. In fact, Essama-Nssah's simulation strategy is a modification of Datt's approach. For a parameterization of the Lorenz curve he computes the associated first and second order derivatives. Then, he combines these results with an estimate of the mean of the distribution to recover levels of the welfare indicator (using the first order derivative) along with an estimate of the density function (based on the second order derivative).

Minoiu and Reddy¹¹ assess the performance of functional forms proposed by Kakwani and Villasenor and Arnold to estimate the Lorenz curve from a grouped data. The methods are implemented using the computational tools such as Povcal and SimSIP, both developed by the World Bank. To identify biases associated with these methods, they use unit data from several household surveys and theoretical distributions. They are concluding that the poverty and inequality are better estimated when the true distribution is unimodal, rather than multimodal.

More comprehensive poverty and inequality studies, based on parameterized Lorenz curve, for different functional forms, can be found in: Bhalla¹²; Chen and

⁹ Datt, G. (1998). Computational Tools for Poverty Measurement and Analysis. *FCND Discussion Paper No.50*.

¹⁰ Essama-Nssah, B. (2005). *Inequality and Poverty Simulations within the Lorenz Curve Framework*. Poverty Reduction Group, The World Bank.

¹¹ Minoiu, C., and Reddy G., S. (2009). *Estimating Poverty and Inequality from Grouped Data: How well do Parametric Methods Perform?*, Journal of Income Distribution, pp.160-178.

¹² Bhalla, S. (2002) *Imagine There's No Country: Poverty, Inequality, and Growth in the Era of Globalization*, Institute for International Economics, Washington DC.

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Ravallion¹³; Figini and Santarelli¹⁴; Pritchett¹⁵; Son and Kakwani¹⁶; Kamin¹⁷; Edward and Sumner¹⁸; Kakwani and Podder¹⁹.

3. METHODOLOGY AND DATA

The used methodology is based on the following two functions²⁰:

1) Lorenz curve:

$$L = L(p; \pi) \quad (1)$$

where L is the share of the aggregate income that belongs to the poorest p percentages of the households, and π is a vector of the Lorenz curve (estimable) parameters.

2) Poverty measure:

$$P = P(\mu/z; \pi) \quad (2)$$

where P is a poverty measure given as a function of the coefficient of the mean income μ and the poverty line z , and the parameters of the Lorenz curve π .

The function L covers relative inequalities in the households and supports alternative parameterizations of the Lorenz curve, while the function P , which is homogenous of degree zero in mean income and poverty line²¹, covers the

¹³ Chen, S. and Ravallion, M. (2006) "China's (Uneven) Progress against Poverty", *Journal of Development Economics*, Vol. 82(1), pp. 1-42.

¹⁴ Figini, P. and Santarelli, E. (2006) "Openness, Economic Reforms, and Poverty: Globalization in the Developing Countries", *Journal of Developing Areas*, Vol. 39(2), pp. 129-151.

¹⁵ Pritchett, L. (2006) "Who Is Not Poor? Dreaming of a World Truly Free of Poverty", *The World Bank Research Observer*, Vol. 21(1), pp. 1-23.

¹⁶ Son, H.H. and Kakwani, N. (2006) "Global Estimates of Pro-Poor Growth", United Nations Development Programme International Poverty Centre Working Paper No. 31.

¹⁷ Kamin, David. (2013) "Reducing Poverty, Not Inequality: What Changes in the Tax System Can Achieve". *New York University Law and Economics Working Papers*. Paper 333.

¹⁸ Edward, Peter and Andy Sumner (2013), *The Future of Global Poverty in a Multi-Speed World: New Estimates of Scale and Location, 2010–2030*, CGD Working Paper 327, June.

¹⁹ Kakwani, N., and Podder, N. (1976). Efficient Estimation of The Lorenz Curve and Associated Inequality Measures form Grouped Observations. *Econometrica*, Vol. 44(1), p.p. 137-148, and Kakwani, N., and Podder, N. (1973). On the Estimation of Lorenz Curves from Grouped Observations, *International Economic Review*, Vol.14, p.p.278-292.

²⁰ Datt, G. (1998). Computational Tools for Poverty Measurement and Analysis. *FCND Discussion Paper No.50*.

²¹ If the poverty line and mean income change in same proportion, poverty will remain unchanged.

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assessment of the absolute living standard of the poor households, and supports different poverty measures²².

Regarding the poverty measures, we use the FGT index:

$$P_{\alpha} = \int_0^z \left[\frac{z-x}{z} \right]^{\alpha} f(x) dx \quad \alpha \geq 0 \quad (3)$$

where x is the household income; $f(x)$ is its density (roughly estimated proportion of households with income x); z is poverty line, and α is non-negative parameter²³. We prefer the FGT index since it belongs to the class of additively separable indices²⁴. It incorporates: head-count index (H); poverty gap index (PG); and poverty severity index (PS), where: H corresponds to $\alpha = 0$; PG to $\alpha = 1$, while PS corresponds to $\alpha = 2$ (see eq.3).

Given the best performances, the estimation of the Lorenz curve is usually based on the following two functional forms: GQ Lorenz curve²⁵ and Beta Lorenz curve²⁶. In this paper our focus is aimed at the GQ Lorenz curve, which specification, as well as the equations for estimation of the poverty measures (H, PG, PS), are given in Annex 1, Table A1.1.

²² Datt, G. (1998). Computational Tools for Poverty Measurement and Analysis. *FCND Discussion Paper No.50*.

²³ Higher value of the parameter α means higher sensitivity of the measure with respect to the inequality of the poor households.

²⁴ FGT belongs to the class of additively separable poverty indices, which means that deprivation that one household feels depends only on a fixed poverty line and its level of welfare, but not on the welfare of other households. So, if z is the poverty line, n is the number of households, x_i is the level of welfare of the household i , and $\psi(z, x_i)$ is the indicator of deprivation at the household's level, then this class poverty measures give the average deprivation of the total number of households:

$$P(z, x) = \frac{1}{n} \sum_{i=1}^n \psi(z, x_i).$$

When the households are divided into groups, this class of measures allows one to compute the overall poverty as a weighted average of poverty in each group. The weights here are equal to households' shares. Thus, such indices are also additively decomposable (see: Essama-Nssah, B., 2005)

²⁵ Villasenor, J. A., and Arnold, B.C. (1984). *The general quadratic Lorenz curve*. Technical report, Colegio de Postgraduados, Mexico City (mimeo).

²⁶ Kakwani, N. (1980). On a class of poverty measures. *Econometrica* 48 (2), p.p. 437–446.

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In order to estimate the poverty measures, in the first step, we estimate the parameters of the GQ Lorenz curve, by using the following regression:

$$L(1-L) = a(p^2 - L) + bL(p-1) + c(p-L) \quad (4)$$

The regression (4) does not contain an intercept. The parameters are estimated with the OLS method, using all except the last observation for (p, L) . The last observation that takes values $(1, 1)$ is excluded since the functional form for the Lorenz curve already is being established to pass through the points $(1, 1)$. Then, in the second step: 1) we compute the mean income μ , 2) we set the poverty line z , and 3) we check out whether the parameterization enables theoretical validity of the Lorenz curve (for the conditions of theoretical validity of the Lorenz curve, see: Annex 1, Table A1.2). Finally, in the third step, we construct point estimates of the elasticities of poverty measures with respect to the mean income and the Gini index (the formulas are given in Annex 1, Table A1.3).

The grouped data, at a monthly frequency, have been obtained from the study "Material deprivation poverty and social exclusion in Republic of Macedonia"²⁷ (see: Annex 2, Table A2.1).

4. RESULTS

The estimated parameters a , b and c of the general quadratic Lorenz curve are presented in Annex 2, Table A2.2. Our Lorenz curve satisfies previously outlined theoretical conditions regarding its validity.

The Gini index equals 37.84, which implies moderate to a high level of inequality in income distribution among the households (see: Annex 2, Table A2.3 and Figure A2.1).

The mean income μ is equal to 19073,70 denars (or about 347,00 US\$), while the poverty line z is set to a 60% of the mean income, which is 11444,00 denars (or about 208,00 US\$), (see: Annex 2, Table A2.3).

²⁷ Mitev, M, G., (2012). *Material Deprivation, Poverty and Social Exclusion in Macedonia*. Friedrich Ebert Stiftung.

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The estimated head-count index (H) proves that 33.38% of the households are below the poverty line (see: Annex 2, Table A2.3).

The estimated poverty gap index (PG) counts 11.40% (see: Annex 2, Table A2.3). It shows that, on average, it takes 1304,16 denars (or about 25US\$) per month, for a poor household to get out of the poverty zone. It also means that it takes approximately 217.664.301,00 denars (or about 3.957.532,00 US\$) per month, for all poor households in Macedonia to pass the poverty line. Finally, the poverty severity index counts 8.49%.²⁸

The elasticities of poverty measures with respect to households' mean income indicate that the increase of the mean income for 1% leads to a decrease of the head-count index for about 1.23%, and a decrease of the poverty gap index for 1.32% - which implies a high level of responsiveness of the poverty indices (see: Annex 2, Table A2.4). The elasticities of poverty measures with respect to Gini index show that the increase of the Gini index for 1% results in an increase of the head-count index for about 0.82%, and an increase of the poverty gap index for 2.54% - which, as in the previous case, implies a high level of responsiveness of the poverty indices (see: Annex 2, Table A2.4).

5. CONCLUSION

The estimation of the Lorenz curve parameters (which functional form is assumed as a general quadratic) results with an inequality index, that indicates moderate to a high level of income inequality among households in Macedonia.

The poverty measures estimated on the basis of the household's mean income (19.073,70 denars, or about 347,00 US\$) and the poverty line (set to a 60% of the household's mean income i.e. 11.444,00 denars, or about 208,00 US\$) are as follows: the head-count index equals 33.38%, the poverty gap index is found to be 11.40%, while the poverty severity index is 8.49%.

²⁸ This index is useful for intertemporal comparison of the severity of poverty in certain country, or for country ranking.

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From the aforementioned, a somewhat controversial conclusion for the relationship between the Macedonian poverty rate and inequality index, should be withdrawn. Namely, the high level of poverty, accompanied with the moderate level of inequality and low households' mean income, suggests that the only "thing" that should be treated as a relatively equally distributed among the households in Macedonia, actually is the poverty.

The elasticities of poverty measures show a high level of responsiveness of the poverty indices in respect to the mean income of households. The same conclusion is valid for the elasticities of poverty measures in respect to the Gini index. We believe that these findings might be of a particular interest to the creators of economic and social policy in the Republic of Macedonia, since they lead to the conclusion that the transmission mechanism, from the economic growth towards the poverty reduction works properly. Furthermore, they confirm that, in the case of the Republic of Macedonia, the so-called, ruthless growth, does not exist.

A further analysis of poverty in the Republic of Macedonia requires decomposition of the poverty rate changes into a growth and redistribution component²⁹.

²⁹ Datt, G., and Ravallion, M. (1992). Growth and redistribution components of changes in poverty measures: A decomposition with applications to Brazil and India in the 1980s. *Journal of Development Economics* 38 (2), p.p. 275–295, and Kolenikov, S., and Shorrocks, A. (2005). A decomposition analysis of regional poverty in Russia. *Review of Development Economics*.

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ANNEX 1.

Table A1.1: Poverty measures derived from the parameterized GQ Lorenz curve

	GQ Lorenz curve
Lorenz curve equation	$L(1-L) = a(p^2 - L) + bL(p-1) + c(p-L)$ or
$L(p)$	$L(p) = -\frac{1}{2} [bp + e + (mp^2 + np + e^2)^{1/2}]$
(H)	$H = -\frac{1}{2m} \left[n + r(b + \frac{2z}{\mu} \{ (b + 2z/\mu)^2 - m \}^{1/2}) \right]$
(PG)	$PG = H - (\mu/z)L(H)$
(PS)	$PS = 2(PG) - H$
	$-\left(\frac{\mu}{z}\right)^2 \left[aH + bL(H) - \left(\frac{r}{16}\right) \ln \left(\frac{1-H/s_1}{1-H/s_2} \right) \right]$
Note:	$e = -(a+b+c+1)$ $m = b^2 - 4a$ $n = 2be - 4c$ $r = (n^2 - 4me^2)^{1/2}$ $s_1 = (r-n)/(2m)$ $s_2 = -(r+n)/(2m)$

Source: Datt, G.(1998).

A theoretically valid Lorenz curve satisfies following four conditions:

- 1) $L(0; \pi) = 0$; 2) $L(1; \pi) = 1$; 3) $L'(0^+; \pi) \geq 0$; 4) $L''(p; \pi) \geq 0$ za $p \in (0,1)$

The first two conditions imply that 0 and 100 percent of the households account for 0 and 100 percent of the total income, respectively. The third and fourth conditions mean that Lorenz curve is monotonically increasing and convex.

The equations for the first and second derivative of the GQ Lorenz curve, as well as the conditions for the GQ Lorenz curve validity, are presented below:

$$L'(p) = -\frac{b}{2} - \frac{(2mp+n)(mp^2+np+e^2)^{-1/2}}{4}; \quad L''(p) = \frac{r^2(mp^2+np+e^2)^{-3/2}}{8}$$

Table A1.2: Conditions for theoretical validity of the Lorenz curve

Condition	GQ Lorenz curve
first	$e < 0$
second	$a + c \geq 1$
third	$c \geq 0$
fourth	(1) $m < 0$ or

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$$(2) \quad 0 < m < (n^2 / (4e^2)), \quad n \geq 0 \text{ OR}$$

$$(3) \quad 0 < m < -(n/2), \quad m < (n^2 / (4e^2))$$

Source: Datt, G.(1998).

The formulas for the elasticities of poverty measures with respect to the mean income and the Gini index are given in Table A1.3:

Table A1.3: Elasticities of poverty measures with respect to the mean income and the Gini index

Elasticity of	with respect to	
	Mean income	Gini index
H	$-z(\mu HL''(H))$	$(1 - z/\mu)/(HL''(H))$
PG	$1 - H/PG$	$1 + (\mu/z - 1)H/PG$
SPG	$2(1 - PG/PS)$	$2(1 + (\mu/z - 1)PG/PS)$

Source: Datt, G.(1998).

ANNEX 2.

Table A2.1: Distribution of monthly incomes of households in Macedonia

Monthly income per household in denars (2012)	P	L
0-3000	0.0730	0.00918
3001-6000	0.1320	0.02310
6001-9000	0.2470	0.06832
9001-12000	0.3610	0.13108
12001-15000	0.4730	0.21035
15001-18000	0.5430	0.27090
18001-21000	0.6400	0.37007
21001-24000	0.7110	0.45382
24001-27000	0.7580	0.51666
27001-30000	0.8520	0.65711
30001-45000	0.9340	0.81833
45001 and above	1.0000	1.00000

Note: p = cumulative proportion (or percentage) from total number of households;
 L = cumulative proportion (or percentage) of monthly income

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Figure A2.1: GQ Lorenz curve – Macedonia, 2012

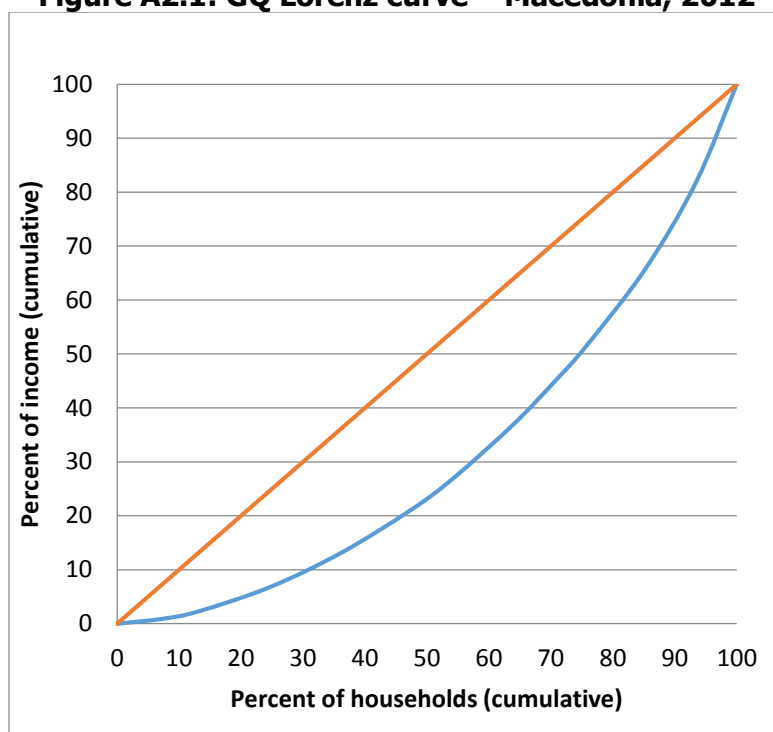


Table A2.2: Regression results – GQ Lorenz curve

Dependent Variable: $L*(1-L)$
 Method: Least Squares
 Sample: 1 12
 Included observations: 12
 $L*(1-L)=a*(P^2-L)+b*(L*(P-1))+c*(P-L)$

	Coefficient	Std. Error	t-Statistic	Prob.
a	1.430599	0.025493	56.11786	0.0000
b	-1.194924	0.038519	-31.02190	0.0000
c	0.062716	0.014898	4.209749	0.0023

R-squared	0.999814	Mean dependent var	0.139793
Adjusted R-squared	0.999772	S.D. dependent var	0.095691
S.E. of regression	0.001443	Akaike info criterion	-10.03128
Sum squared resid	1.88E-05	Schwarz criterion	-9.910053
Log likelihood	63.18768	Hannan-Quinn criter.	-10.07616
Durbin-Watson stat	1.754458		

Table A2.3: Poverty line, mean income, poverty measures and Gini index

	denars
Poverty line	11444,00

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Mean income	19073,70
	%
Head-count index (H)	33.38
Poverty gap index (PG)	11.40
Poverty severity index (PS)	8.49
Gini index	37.84

**Table A2.4: Elasticities of poverty measures with respect to
the mean income and the Gini index**

Poverty measures	Mean income	Gini index
Head-count index (<i>H</i>)	-1.23009	0.82010
Poverty gap index (<i>PG</i>)	-1.31852	2.54575
Poverty severity index (<i>PS</i>)	-1.39075	4.26061

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UDC: 334.72.012.63/.64:339.137.2]-027.511(497.7)

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BUSINESSES IN REPUBLIC OF MACEDONIA**

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ABSTRACT

Globalization affects all economic actors in all industries and parts of the world. Hence, business people all around the world are equally interested in how to exploit the benefits and how to avoid the threats it brings. However, by doing so, they often fail to foresee the real risks that the globalization brings to their business and business models, or to take advantage of the opportunities. The low visionary capacity of their management, the low level of innovation and the insufficient funding, are the most frequently stated reasons for that failure in the case of small and medium businesses. However, it seems that the overarching reason for this erroneous perception of the real nature of the phenomenon of globalization, in the case of the small business leaders stems from their tendency to see only opportunities and chances for growth and prosperity of their companies. Moreover, managers and national economies that tend to see the threats also tend to be characterized as too pessimistic. We survey the perception of the managers and owners of small and medium enterprises in the Republic of Macedonia on the impact of the globalization on their respective businesses and on the national economy, as a whole. The results show that our entrepreneurs tend to perceive globalization more as an opportunity than as a threat, with some specifics in relation to the industry in which they operate and their educational and professional background. Finally, following the triple helix model we offer several measures to the state, education institutions and to the business community, aiming

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to help the leadership of the small and medium sized companies in the country to develop the necessary skills and suitable strategies for growth of their competitiveness appropriate to the realities of the globalization today.

KEYWORDS: Globalization, Small and Medium Enterprises, Internationalization, Competitiveness

JEL: L25, L26, M26

INTRODUCTION

Much has been written about the globalization. Although it is usually perceived as a modern phenomenon, we can trace the elements of the globalization even in the campaigns of Alexander the Great, in the state structure of Rome, Byzantium, Ottoman Empery, up to the concept of the British Commonwealth, or the European Union, today. However, Herman Kahn was first who defined globalization in the context of the modern civilization. This rather controversial American (quasi) futurist, in 1950s expected that "the sustained economic growth will act in the direction of voluntary full acceptance of the western economic system and values by all other nations and cultures". Kahn's predictions fortunately did not come through, at least not in a form he wished. While, the key factors of globalization, the rapid development of international trade and technology lead to reduction of the costs of the transport of goods and people, faster and easier communication, they, same time, by fostering the economic and political integrations, allow for increased economic and cultural hegemony and reduced cultural diversity.⁴

Competitiveness is one of the most popular concepts in contemporary macroeconomics. Having a competitive advantage means higher profits, growth and better standard of living. It is prerequisite for faster integration of the small national

⁴ See: Ch. Marrewijk (2002) International Trade and the World Economy, Oxford University Press and N. Brune, N.(2004). Explaining Financial Liberalization around the World, Ph. D. Dissertation, Yale University

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economies into the global market.⁵ Moreover, one of the major prerequisite for successful introduction of a national economy into the global markets is the sufficient competitiveness of its companies.

In this paper we explore the perception of small and medium sized businesses from Republic of Macedonia of globalization and the need for constant improvement of their competitiveness if they want to harvest the opportunities and withstand the drawbacks of the modern globalization.

GLOBALIZATION AND SMALL AND MEDIUM ENTERPRISE

Many authors consider that economic globalization the main pillar of the entire social process over which all other components of the phenomenon are built. Although, the globalization has many complex processes that are very dynamic, there is one that involves strengthening and expanding the relations between the national economies and that the economic dimension is the key factor to support globalization in all other spheres - believes Pogge.⁶ Therefore, the fear of the developing countries that the globalization can endanger their development and that the world can end up in some sort of neo-colonialism. This since the developing countries are not able to compete with the developed North on an equal basis. They lag in organizational, technical, financial and social perspective of the contemporary business. Consequently, there is a danger their companies to be marginalized for the favour of the big companies and large multinationals. Although, fostering the technological change creates many opportunities, to take advantage of these opportunities, these countries should be able to cope with the competition from developed economies.⁷ In fact, the small and medium sized companies are under pressure all over the world. Since they make up 99 percent of all businesses in the European Union and in the US, the problem is more

⁵ T. Petkovska, & B. Jovanović, (2015) 'Export and Foreign Trade Competitiveness in the Republic Of Macedonia', *Economic Development* 17, 3, pp. 11-28

⁶ T. Pogge (2007) *Why Inequality Matters*, in David Held and Ayse Kaya (eds), *Global Inequality*, Cambridge Policy Press

⁷ I, Alvarez, R. Marin and A. Fonfría (2009) *The Role of Networking in the Competitiveness of Firms. Technological Forecasting & Social Change*, 76(3): 410-421.

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than critical in many other countries of the world. Small and medium sized businesses are the largest employers. In the EU, they employ two thirds of the workforce.⁸ They also account for the biggest chunk of the reported innovations, emerged new business concepts, rollouts of new products. They, as opposite to the big companies, are able to withstand worst recession. However, with the opening of the global markets, the small and medium sized companies are in a continuous pursue for customers all around the world, facing diverse and rapidly changing customer needs, shortened delivery times and reduced product lifecycle. The pace of this pursue improves their agility and innovation. They have to be more cost efficient, technologically advanced and flexible and, most importantly, able to acquire oriented approach to the market in terms of close customer focus.⁹

However, contrary to their number, the small and medium sized companies show lower profitability and face more difficulties when obtaining finances, in comparison with the large businesses. Their contribution to the Gross Domestic Product is significantly lower than that of the large enterprises. Moreover, they traditionally lack advanced strategic management and their future, very often, depends on the vision and attitudes of the founder towards the change in the business environment. Many small and medium sized companies are not adequately prepared to face the reality of the global challenge.¹⁰ They can rarely afford the costs of high-quality human resources, information and or relevant managerial knowledge needed to cope with these tasks.¹¹ In relation with the globalization, they often do not have sufficient awareness of their real position, their strengths and weaknesses. They also fail to assess the threats that the globalization brings. The lack of the wider managerial vision and the excessive focus to the operational side of the business are the two main factors for that. If they want to be successful and to exploit the advantages of the globalization,

⁸ European Commission (2014) Annual Report on European SMEs

⁹ A. Wolff, and L. Pett (2000) Internationalization of small firms: An examination of export competitive patterns, *Journal of Small Business Management*, 38, 2, 34 – 48.

¹⁰ G. Bekaert (2000) Emerging Equity Markets and Market Integration, *NBER Reporter*, pp. 8-11, Winter.

¹¹ A. Frankel (2000) Globalization of the Economy, *NBER Working Paper No. 7858*, August.

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they must move away from the current position, determining whether and how it (mis)matches with the trends brought by the globalization. They must examine the market worldwide and introduce advanced concepts.¹² The financial constraints they suffer bring lack of modern technology and limit their research and development.¹³ In some countries, they face lack of awareness among the relevant government institutions and limited level of activities aimed at development of small and medium enterprises.¹⁴

INTERNATIONALIZATION OF OPERATIONS AND COMPETITIVENESS

According to some researchers, there is a direct link between the efficiency of the small and medium sized companies and their better competitiveness and the internationalization of their operations.¹⁵ The global presence brings four major benefits: (1) possibility of achieving economies of scale, (2) exploitation of lower input costs, (3) dispersion of risk and (4) large enough markets to achieve the needed and desired growth.¹⁶ In the case of the USA businesses, 24% of small companies are already involved in the global trade and 64% of those that have operations abroad, scored positive results, as early as in their second year of international operations.¹⁷ However, for the small and medium sized companies the very decision to enter new market(s) is challenging and risky move.¹⁸ Research indicate on several issues that the

¹² R. Blackburn and T. Wainwright (2010). *The Year Ahead: A View from Britain's Small Businesses*. Project Report, London, UK: Barclays Bank PLC

¹³ D. Fletcher and S. Vyakarnam (1999). *International enactment of entrepreneurial values: Mapping internationalisation processes in small firms*.

¹⁴ G. Gankema, R. Snuif and S.Zwart (2000). *The internationalization process of small and medium-sized enterprises: An evaluation of stage theory*. *Journal of Small Business Management*, 38, 4, 15 – 28.

¹⁵ L. Szerb and S. Terjesen (2010). *Measuring the Competitiveness of Small Businesses*

¹⁶ C. Boudreau et al. (1998) "Going Global: Using Information Technology to Advance the Competitiveness of the Virtual Transnational Organization", *Academy of Management Executive*, 12, 4, pp. 120-128.

¹⁷ UPS Survey (2014) *Perceptions of the World Trade*

¹⁸ See: O. Keohane and N. Joseph (2000). *Globalization. Whats New, Whats Not and So What?* *Foreign Policy*, No. 118, 104-119 or P. Servais and M. Knudsen (2004) "SME's International Engagements - Imports, Exports and Intra-industry trade". , in Larimo, J. and Rupunen, S. (eds.). *Recent European Research on SME Export Behavior and Internationalization*, University of Vaasa Reports 111, pp. 115-131

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small and medium sized companies face when enter a foreign market. Firstly, they suffer from lack of knowledge how to conduct their business abroad.¹⁹ Therefore, they make excessive transaction costs to find reliable local agents, to negotiate favourable terms, to monitor the execution of the contracts.²⁰ Experts also point out on another important barrier to the globalization of SMEs, i.e. their lack of legitimacy and influence in the new environment.²¹ This lack of complementary resources needed for understanding the new environment and its institutions, generates difficulties and costs.²² Perhaps subconsciously, but it seems that small and medium enterprises underestimate both external and internal challenges.²³ The time constraints, the incompetence, the low potential for upgrading the technology and the lack of financial strength, often prevent small and medium sized companies to take advantage of new opportunities.²⁴ Therefore, a number of small enterprises that are prosperous at the local level do not manage to score same results on the foreign markets.²⁵ However, the number of small and medium-sized enterprises able to use new technologies to increase their productivity grows.²⁶ Some researchers indicate that the various strategic partnerships as more traditional forms of inter-organizational cooperation can also be

¹⁹ A. Kuczera (2002). The Internationalization of Small and Medium-Sized Enterprises (SMEs) and the Impact of the Internet

²⁰ P. Julien and A. Joyal (1994). SMEs and international competition: Free trade agreement or globalization? *Journal of Small Business Management*, 32, 3, 52 – 65.

²¹ K. Mitchell, B. Smith, A. Morse, W. Seawright, M. Peredo and B. McKenzie (2002) Are entrepreneurial cognitions universal? Assessing entrepreneurial cognitions across cultures. *Entrepreneurship: Theory & Practice*, 26 (4), pp. 24 - 33

²² L. Reason and O. Nicolescu (2002). Entrepreneurship in difficult circumstances: Internationalization and small and medium sized enterprises in Eastern Europe, *Proceedings of the 47th World Conference of the International Council for Small Business*

²³ M. Ruokonen, N. Nummela, K. Puumalainen and S. Saarenketo (2006). Network management - the key to the successful rapid internationalization of small software firm?, in *International Journal of Entrepreneurship and Innovation Management*, 6 (6), pp. 554–572.

²⁴ J. Sapienza, E. Autio, G. George and A. Zahara (2006). A capabilities perspective on the effects of early internationalization on firm survival and growth, in *Academy of Management Review*, 31 (4), pp. 914-933

²⁵ D. Sharma and A. Blomstermo (2003) The internationalization process of born global: a network review, in *International Business Review*, 12 (6), pp. 739-753.

²⁶ M. Simpson and J. Docherty (2004) E-commerce Adoption Support and Advice for UK SMEs. *Journal of Small Business and Enterprise Development*, 11(3): 315-328.

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used for enhancing the competitiveness of the companies and the national economies.²⁷

GLOBALIZATION AND COMPETITIVENESS – ROLE OF STATE

Porter was the first who defined competitiveness of a given country simply as a sum of the competitiveness of its respective companies. World Economic Forum launched The Global Competitiveness Report and regular country ranking. The competitiveness started to be considered as the key factor for exploitation of the opportunities that globalization brings and for safeguarding from its detrimental side effects. The policy makers accepted this standing and started to concentrate on their measures for improvement of the competitiveness. Firstly, they started to invest in public infrastructure as tangible support to the businesses. For example, the engineering and technological infrastructure was the most significant impact of the EU Structural Funds support to the new member states.²⁸ Secondly, the states started to foster bilateral and multilateral free trade agreements. According to the World Trade Organization, the trade agreements have become increasingly prevalent since early 1990s, and currently there are 267 in force, worldwide.²⁹ Pilinkiene surveyed the effects of such trade openness on the competitiveness of some Central and Eastern European countries, between 2000 and 2014, and found interdependence between the trade openness, the economic growth and the competitiveness. Moreover, the improved competitiveness had long-lasting effect on the growth, measured as GDP per capita.³⁰ However, some researchers noticed that in order this to hold, the free trade and openness should be between countries and regions with similar, if not same, stage of

²⁷ A. Adamik (2016) 'The mechanism of building competitiveness through strategic partnering', *Management* (1429-9321), 20, 1, pp. 292-309

²⁸ I. Gasparėnienė, and R. Remeikienė (2016), 'EVALUATION OF THE IMPACT OF THE EU STRUCTURAL SUPPORT ON THE COMPETITIVENESS OF LITHUANIAN ECONOMICS', *Business, Management & Education / Verslas, Vadyba Ir Studijos*, 14, 1, pp. 74-88.

²⁹ WTO (2016) Regional trade agreements database, <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>

³⁰ V. Pilinkiene (2016). 'Trade Openness, Economic Growth and Competitiveness. The Case of the Central and Eastern European Countries', *Engineering Economics*, 27, 2, pp. 185-194,

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development. Thus, analyzing the effects of the free trade agreement between Thailand and Australia, Siddique at al., found that, on the side of Thailand, the less developed partner, the growth in exports was mainly achieved by the bigger presence of foreign companies looking for the opportunity to take advantage of the free trade with Australia, while located in much cheaper Thailand.³¹

Apart from the infrastructure and the free trade agreements, experts indicate on the industry clusters and business networks as tools for practical overcoming of some of the apparent weaknesses of the small businesses. With networking, the small and medium enterprises can penetrate globally without investing directly in the foreign operations.³² However, Biuksane (2016) stresses that the factors that influence the competitiveness of the Latvian clusters are not entirely economical, but are in domain of the much wider social, political and environmental background. According to her, it is advisable to the institutions involved in the policy-making to take into account entire spectrum of factors influencing the competitiveness and their changes, when making and improving the general policy of a sector.³³ Although the various socio-cultural factors like the shared values, norms and attitudes are not always acknowledged as sources of international competitiveness, they positively affect the various aspects of international competitiveness such as the entrepreneurship attitude, innovation, productivity and international cooperation. Moreover, these factors are far more sustainable and much less affected by everyday changes and provide an opportunity to develop competitiveness strategies based on the unique advantages of a given society. On the other hand, the collectivism and the rigid social hierarchy tend to reduce the national competitiveness.³⁴ In this terms, recognizing the need for new profiles of graduates able to cope with the challenges of the globalization, states also started to

³¹ M. Siddique, R. Sen, & S. Srivastava, (2016). 'Australia-Thailand Trade: An Analysis of Competitiveness and Effects of the Bilateral FTA', *Journal Of Developing Areas*, 50, pp. 103-118

³² K. Morgan (1996). "Boosting Innovation -The Cluster Approach", OECD

³³ I. Biukšāne (2016), 'Model of the Factors Influencing Competitiveness of the Latvian Fisheries Sector Cluster', *Economics & Business*, 28, pp. 76-82,

³⁴ M. Apsalone & E. Šumilo, (2015). 'Socio-Cultural Factors and International Competitiveness', *Business, Management & Education / Verslas, Vadyba ir Studijos*, 13, 2, pp. 276-291

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reform their educational systems. The educational system for the new Millennium they try to build would reflect the industry needs and the knowledge-based economy and requires more intensified convergence of the science towards the market needs and, vice versa, the market "interference" in the world of science with systematic knowledge commercialization and innovation. Such organized interaction between the state institutions, the education system (universities) and the industry is the basis for development of an effective national innovation system in the function of a sustainable national competitiveness.³⁵

OUR SURVEY

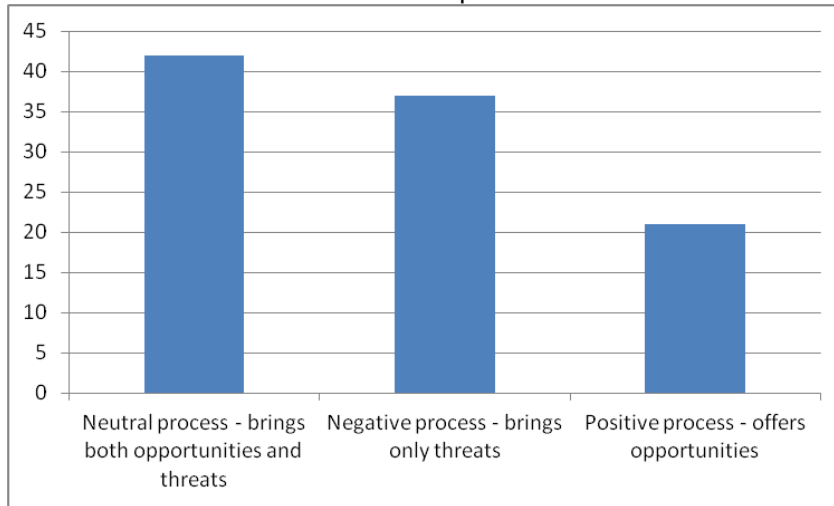
In order to examine their perceptions of globalization and its impact in more details, we developed electronic questionnaire and disbursed it to 160 small and medium sized companies in various industries and regions of Republic of Macedonia. The survey was performed during the summer 2015 and collected answers from 100 small and medium enterprises. The sample included 46% small (up to 50 employees) and 54% medium-sized (up to 250 employees) companies. In terms of their stage of internationalization of operations, majority or 72% reported that they operate solely on the national market. Regarding the type of their business, 54% were providers of some business service (distribution, transport and forwarding) and 46% were producers. The companies, in 70%, were older than 5 years, 25% were older than two years while 5% were younger companies with not more than two years of business record. With a regard to the age of their management and leadership, between 41 and 50 years of age were 40%, between 31 and 40 years of age were 30% of the managers, older than 50 years were 16% and younger of 30 were 14%. From the analysis of the collected answers, it can be concluded that for the most of the surveyed companies and their management teams (42%) the globalization brings both opportunities and

³⁵ N. Penezić, & J. Ješić (2016) 'Trostruki Helix (Univerzitet-Privreda-Država) Model Nacionalne Konkurentnosti u Regionalnoj I Globalnoj Ekonomiji - Iskustva Srbije', Business Consultant / Poslovni Konsultant, 8, 52, pp. 38-52

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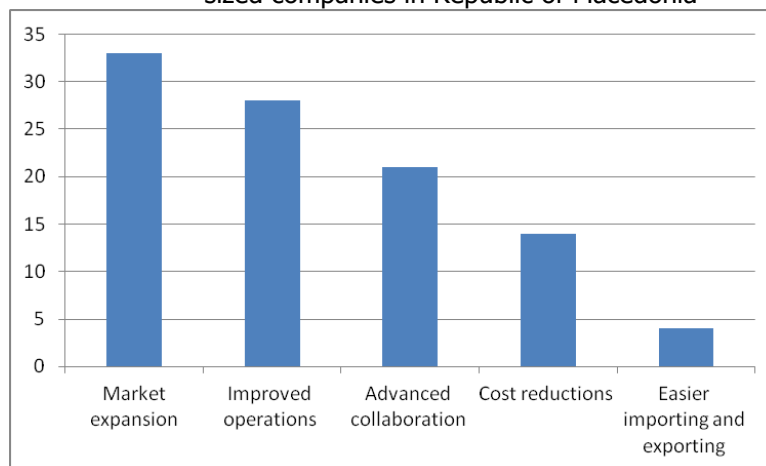
threats, 21% globalization is positive process that offers opportunities and that for 37%, it is a negative process that brings only threats.

Chart 1. Perception of globalization by small and medium sized companies and their leaders from Republic of Macedonia



The lists of the opportunities that globalization brings is topped by the market expansion (33%), followed with improved operations (28%), advanced collaboration with customers and suppliers (21%), cost reductions (14%) and easier importing and exporting of the goods (4%).

Chart 2. Perception of opportunities that globalization brings for small and medium sized companies in Republic of Macedonia

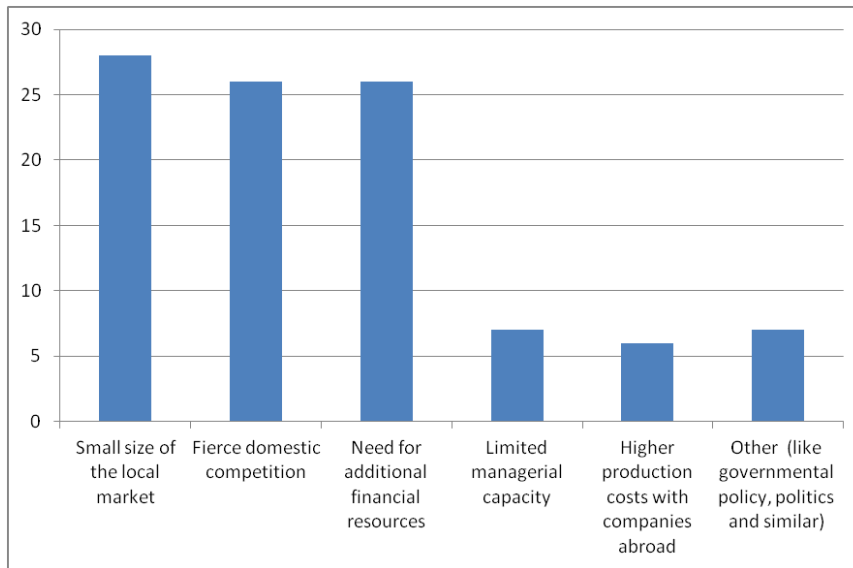


Asked about the threats brought by the globalization, answers are split between 28% of the surveyed managers, who put forward the small size of the local market, 26% who indicated on the fierce domestic competition and other 26% who think that

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it is the need for additional financial resources. For 7% of the surveyed managers, the major threat is the limited managerial capacity, and for 6% it is the higher production cost with companies abroad.

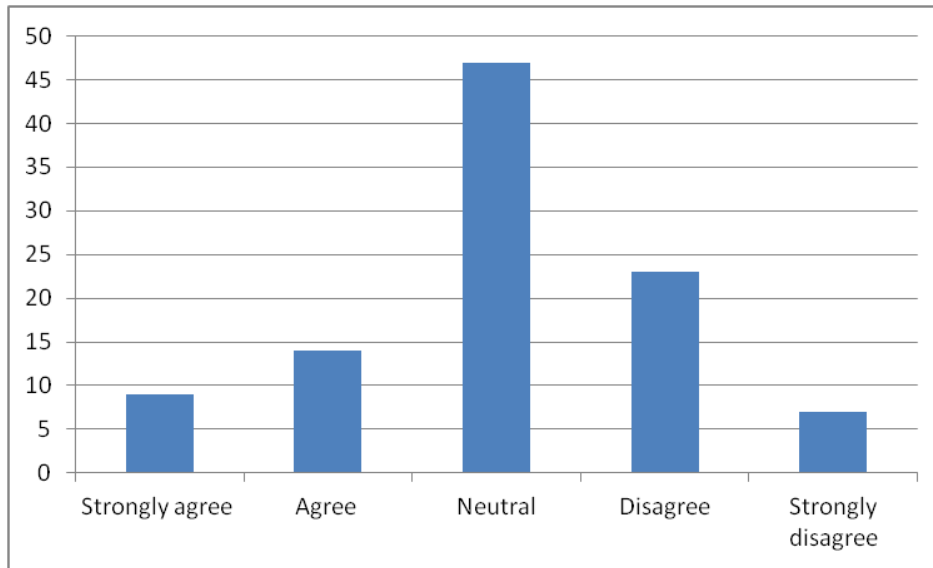
Chart 3. Perception of major threats that globalizations brings for small and medium sized companies in Republic of Macedonia



Managers and owners of small businesses in Republic of Macedonia who strongly agree that the globalization significantly and positively affects and encourages the innovation, are 9%. Managers who agree with the statement are 14%. Managers who think that the impact of the globalization is neutral resulting with positive and negative impact equally, are 47%. Managers who disagree with the statement are 23% and those who strongly disagree are 7%.

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Chart 4. Perception of the link between innovation and globalization of business leaders of small and medium sized companies in Republic of Macedonia



CONCLUSIONS AND RECOMMENDATIONS

The small and medium enterprises have to understand properly the globalization in order to be able to use the benefits it brings. Moreover, the globalization imposes many challenges to their operations and even to their long-term business survival. It opens the world markets, but only to those who timely prepare for the internationalization of their business, and that task is far from being easy for the small and medium sized businesses that often lack the needed managerial skills, lack proper funding and have little knowledge of other cultures and business habits and etiquette. Consequently, many small and medium enterprises often fail to recognize the threats or to exploit the opportunities that globalization brings.

Small and medium sized enterprises from Macedonia and their managers see more neutral and positive (in total 63%) than negative, the impact of the globalization on their businesses. However, they are realistic when stress that the extremely small local market is our disadvantage. The strong local market traditionally is seen as place where the extra costs of the expensive international operations can be offset with the higher mark ups to the domestic customers. The fierce domestic competition is also

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very real treat. In order to take advantages of the globalization, our companies will have to stop compete based on the low prices and to start putting forward the innovative processes and introduce modern equipment resulting in their higher competitiveness on the demanding global markets.

In addition to the small sample size, our research is limited with the general gratification with the high position of the Republic of Macedonia on the Doing Business ranking and on the other hand, with the influence of the ongoing problems of the respondents with their everyday chores. Both factors certainly biased their expressed opinions thought in different sides. However, we believe that survey indicates on the general positive perception of the globalization and its findings are consistent with the results of many similar surveys on the general perception about the benefits for Macedonia from its prospective membership in EU, CEFTA or in the Euro-Atlantic Alliance.

Same time, the results are not quite consistent with the current rank of the economy of the Republic of Macedonia by the Global Competitiveness Index, as efficiency based economy that competes on low operational costs, rather than on innovativeness and investment in research and development. The change in these terms will certainly open new ways for more direct involvement of our enterprises into the global supply chains and capital flows. Many of our small and medium enterprises currently operate with companies abroad through various intermediaries and thus lack timely and objective information about the global markets. Larger investment into the managerial training with an emphasis on the modern skills such as information technology and readiness for experiment, can help the small and medium sized businesses from the Republic of Macedonia in their strive for better competitiveness on the international markets. Adequate managerial training programs would raise the awareness about the weaknesses and about the fact how much the small and medium sized companies from Macedonia harm themselves by competing almost exclusively through low prices. With their unorganized approach to the supply and sales markets, with their reluctance to invest in new, cost effective and modern equipment, in staff

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development and in expert knowledge, they maybe wrongly blame the globalization for their troubles.

The policy makers in the country should stop providing blanket support to the small and medium sized business and start channelling the financial and non-financial incentives to the companies and leadership that show innovativeness, not only in terms of new products or processes, but also in terms of new managerial practices and marketing attitude of the small businesses.

Finally, in order to start narrowing the gap in the competitiveness, the country should start investing the planned portion of its gross domestic product (app. 3%) to research and development. The educational institutions should introduce the impact of globalization in practically all curricula and foster the creativity of students as the only way the new generations will fight the challenges of globalization.

Our small and medium sized businesses and their managers should become aware about the actual gap that they have in comparison with the most innovative and competitive nations. Their optimism in relation with the globalization thus would certainly diminish, but it would open many new innovative programs for taking advantage of opportunities and for escaping the dangers of the globalization resulting in the desired sustainable improvement of the country's competitiveness rank.

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