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Content

It Outsourcing Partnerships: Empirical Research on Key Success Factors

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Extended Abstract

IT outsourcing is among the prevalent practices in the global business today. It becomes an overall managerial strategy in the search for global competitiveness nowadays. It is found that business organizations decide to transfer IT services to other firms (identified as "vendors") not only because of cost-related advantages – outsourcing of knowledge-intensive work takes place also in organizational areas of core competency like applied research & development. The rationale behind outsourcing of knowledge intensive services is to form alliances through which to take advantage of (or to add value by) the mature practices of outsourcing partners and to benefit from the complementary skills of outsourcing vendors (Smuts et al., 2010).

According to many authors outsourcing is a reasonable consequence of the globalization and the partnership between the participating actors is of key importance for the overall efficiency and competitiveness of business activities (Bergkvist & Fredriksson, 2008). If the internal IT operations are not a core competence of an organization, outsourcing some of the IT functions is considered as a way of coping with the constant technological evolution and the pressure for constant increase of the internal IT competence.

Outsourcing has progressed in a strategic way where collaboration and partnership between the client and vendor are targeted to the achievement of mutual goals – which is especially valid for IT outsourcing. From this point of view, a long-term relationship based on trust and cooperation is required in order to gain a sustainable competitive advantage. Many authors have identified that the excellence of outsourcing partnership is crucial to ensure long-term success, however, in many cases the partnering organizations lack the capability to achieve such an excellence (see a review by Ishizaka & Blakiston, 2012).

The objective of the paper is to explore some main key factors affecting the success of IT outsourcing partnership. An approach for empirical study of these effects is suggested using survey data about outsourcing partnerships between vendor organizations and their clients (outsourcers). The survey considers issues related to the key factors of the development of a successful strategic partnership in IT outsourcing. One of the main hypotheses of the study is the existence of an interrelation between the efficiency of business activity of vendor organizations –originating from the economic gains achieved– and the strategic orientation of the outsourcing partnership.

Previous research on the topic is based mainly on utilization of large questionnaires providing information about motivation and effects of outsourcing practices. In general, their results are reported in a quantitative format (see a review by Ishizaka & Blakiston, 2012). The present study is based on the case study approach performed by in-depth interviews conducted in the period 2008-

2011. The survey collected information from key experts and managers that are aware of the practices at 57 IT outsourcing partnerships. The subject of the study is the analysis of the key success factors influencing the formation and development of strategic outsourcing partnerships between Bulgarian vendor organizations and their clients (foreign companies). The analysis is structured in the framework of a specifically developed model of key success factors which reflects the achievements of research in IT services outsourcing in the last decade (Beulen et al., 2011; Barthélemy, 2003; DeLone & McLean, 2003; Kern & Willcocks, 2001).

It is assumed that the system of key competences of the vendor appears to be "complementary" in respect of the competences of the client organization. This can be explained by the fact that the vendor organization makes efforts to build own technologic infrastructure, know-how, and capacity by which to substantially increase the efficiency of realization of a set of similar high technology services. A strategic partnership presumes sharing of the value added between the vendor and the client generated through the attainment of the comparative advantages. This is realized by a complex of both formal and informal relations between units of the organizational structures of partner organizations. It is important for applied research to determine the key factors that have a major impact on the positive outcomes for both outsourcing partners not only in the short-run but in a strategic perspective.

The main orientation of the research in the area of outsourcing of high technology services are several aspects of vendor-client interrelations. Various studies find a relative parity between the importance of the informal aspects of these relations (e.g. personal trust) and the formal aspects formulated in the outsourcing contract (Poppo, 2002). In order to achieve strategic partnerships, however, it is necessary that both aspects of these relations are emphasized (Kern & Willcocks, 2001). According to the study of Kern & Willcocks (2001) the strategic vision and the technical capacity shape not only the formal structuring of contract relations but also the development of inter-personal relations. As factors influencing the success of the outsourcing partnerships can be highlighted: the high degree of synchronization between the client and the vendor; team working; balance of control function; clear responsibilities of the partners; the degree of flexibility and intensity of the transferred processes (Goles, 2001). The latter author derived several important factors characterizing the vendor organization: technical competencies; knowledge of the subject area and the specifics of client's operations; competences for coordination and management of partner relations.

Although IT outsourcing practices are broadly studied from various points of view, relatively little attention in research literature is paid on the factors affecting the strategic relationships and the value adding processes within the outsourcing partnership. For example, Kinnula & Juntunen (2005) consider the outsourcing partnerships where the relationship success factors were evaluated from the point of view of both parties. Two categories of resulting factors are identified: (i) concerning the formation phase of a relationship, and (ii) concerning a mature relationship. Albeit the interest regarding the key success factors is growing there is still a scarcity of empirical evidence for the specifics and the degree of their impact on the success of IT outsourcing partnership.

In the present study the **model of key factors** /MKF/ provides an abridged presentation of the interrelations between the key characteristics of IT outsourcing partnerships which determine its success or failure. In the same time, MKF has also practical implications since it helps the applied researches and IT managers to better understand the nature of IT outsourcing partnership and to identify which factors are most influential in respect of its overall success. MKF assumes a clarification of the interrelations between a complex of factors and a response variable that captures the level of success of the outsourcing partnership. The model incorporates the following key factors:

1) Top management commitment
No partnership can be successful without a clear engagement of the top management of both partners in the outsourcing partnership goals. Client organizations (outsourcers) should assume that the dedicated management requires a strategic understanding of outsourcing partnership goals as well as capabilities for sophisticated negotiation and mediation (ITBE, 2010). Executive leadership and its commitment are recognized as an important factor for a successful IT outsourcing arrangement (Donald et al., 1991; Iakovou & Nakatsu, 2008). In outsourcing setting the managers need to consider strategies for ensuring the discipline of outsourcing relationship by developing such a governance structure that go far beyond the typical operations and processes.
H1. The degree of success of outsourcing partnership is positively related to the degree of commitment of top management.

2) Common aims and objectives
This feature is considered as important factor of the outsourcing partnership as it presumes "goal symmetry" between the outsourcer and vendor organization. Both parties should be responsible for adding value to the relationship by stimulating them to better focus on organizational and cost efficiency (Kishore et al., 2003). Having such a strategic arrangement, partners are able to transfer not only peripheral but also core business processes. With clearly identified common organizational goals both parties should benefit from external input which is expected to provide a long-term impact on the success of the relationship.
H2. The degree of success of outsourcing partnership is positively related to the establishment of common aims and objectives.

3) Bidirectional transfer of knowledge /BTK/.
BTK emerges when optimal (as a quantity and quality) information necessary for the realization of the service is provided through the channels of effective communication between the partners. The knowledge could have two forms: implicit /informal, tacit/ and explicit /formal/ (Nonaka & Takeuchi, 1995). Special attention should be put on the way which organizations "learn" from their partners as this appears to be one of the means for development of key competences. The following research hypothesis is raised in respect of this factor:
H3. The degree of success of outsourcing partnership is positively related to the degree of effectiveness of BTK.

4) Achievement of the contracted mutual goals as results of outsourcing partnership
Another key factor in the model is the degree of achievement of results set as contract goals in the outsourcing agreement. This degree should reflect the divergence between actual benefits and relative costs that client organization would have to spend without the realization of the particular partnership (Anderson & Narus, 1990). A research hypothesis regarding this factor is also raised:
H4. The degree of success of outsourcing partnership is positively related to the degree of achievement of contracted goals.

5) Mutual trust
The third key factor reflects the intensity of the informal relations between partner organizations having in great extent a psychological dimension. The degree of trust between the partners compensates any eventual drawbacks of the formal contracting and the lack of strong defense clauses in outsourcing agreement (Lee & Kim, 1999). This factor reflects the flexibility of the cooperation and the orientation to mutual correctness based on the understanding that the interests of the partner organization should be respected (as far as "the success of the partner works for our own success"). The following research hypothesis is raised in respect of this factor:
H5. The degree of success of outsourcing partnership is positively related to the degree of mutual trust between the partners.

6) Security assurance of outsourcing partnership
The existence of security assurance is an important factor of the success and sustainability of outsourcing partnership that is likely to provide strategic nature of the partnership. Unlike the mutual trust (that is of informal nature) the availability of security assurance has entirely formal character as far as it is incorporated in the outsourcing agreement. These warranties should be provided by special clauses in the contract. As a base precondition for the provision of reliable assurance is a targeted negotiation process before the finalization of the contract (i.e. the decision to form the outsourcing partnership). The following research hypothesis regarding this factor is raised:
H6. The degree of success of outsourcing partnership is positively related to the degree of security provided in the agreement.

7) Interdependence between client and vendor organization
This factor reflects the degree of dependency of the activities of client organization from the operations of the vendor organization supplying a high technology service as a subject of the outsourcing agreement. This interdependence has a clear bidirectional nature – often in practice the vendor organization is strongly dependent on the realization of contracted service. It is particularly valid in cases when the vendor is serving one key client or diversification of the vendor services/client was not achieved.
H7. The degree of success of outsourcing partnership is positively related to the degree of interdependence between the operation of the client and the vendor organization.

8) Shared values within the outsourcing partnership
The sustainability and the strategic nature of outsourcing partnerships are expected to reflect the sharing of common values, principles, and cooperation ideas as elements of the organizational cultures of partner organizations. As a result of the formation of the outsourcing partnership transformations of organizational cultures have often taken place in both client and vendor organizations. Along with the direct net benefit of the agreement having immediate effect on the economic status of the partner organizations, the sharing of common values and the exchange of organizational and managerial know-how has a significant (although indirect) long-term effect on the operation of the organizations. The research hypothesis regarding this potential factor states that:
H8. The degree of success of outsourcing partnership is positively related to the degree of sharing of common values between the partner organizations.

9) Human resources competence
IT outsourcing allows the client organizations to refocus on their core business activities as they obtain the necessary IT competence from the vendor. This way, the strategic effect emerges from the focus on the core operations assuming the availability of a reliable IT service. The enhanced IT staff expertise of the vendor appears to be a critical factor of the partnership success. Client companies rely on the outsourcing for long-term intellectual value which is found to be more beneficial than outsourcing for cost-cutting in the short run (Manning, 2008).
H9. The degree of success of outsourcing partnership is positively related to the competence of human resources in vendor organization.

10) Effective communication
Last but not least, effective communication between outsourcing partners is assumed to be of crucial importance for the successful relationship. This factor is emphasized widely in the literature as a core determinant of the outsourcing partnerships' success since it amplifies the level of understanding and the adequate information exchange (Kannan, 2007; Berger & Lewis, 2011). It is typically considered that communications concern mainly the client organization that should provide facilitating information to the vendor. However, the opposite is also of importance since the client decreases its degree of control over the outsourced services and functions. This way, an ineffective communication from the vendor can obstruct the outsourcing relationship.

H10. The degree of success of outsourcing partnership is positively related to the level of effectiveness of the communication between the partners.

The degree of success of outsourcing partnership is the main dependent (response) variable in the MKF. It is however commonly considered as quite difficult for operationalization and empirical measurement as far as it is of multidimensional nature. For example, Lee & Kim (2003) define the success of partnership as the degree of satisfaction of the needs of client organization from the services provided by the vendor organization. Other points of view are also applicable, e.g. that which characterizes the outsourcing partnership success by the degree of achievement of overall (pan-organizational) comparative advantage through outsourcing of all or part of ICT functions of the client organization.

The operationalization of the concept indicators is performed through a multivariate (multi-item) method where for each factor 1 to 4 questions are involved. For the standardization of primary data a unified 7-rank Likert scale for the answers is adopted which allows the summarization of the answers on the items to extract one empirical measure (variable) for each concept indicator. Rank 7 codes the opinion expressed at the maximum of the scale (e.g. maximum degree of agreement with the respective statement) and with rank 1 respectively at the minimum of the scale.

The success of an outsourcing partnership is evaluated by the degree of matching between goals planned and results actually achieved. This evaluation is required in respect of four key dimensions: the realization of expected financial benefits; complying with the deadlines; successful execution of the tasks; provision of the required service quality. Caution should be put here since the evaluation of the results achieved may diverge from the points of view of the vendor and client organizations. In our case the evaluation results obtained by the survey reflect the position of the vendor organizations.

MKF is depicted on fig.1 where the preliminary results for the correlations between the variables are presented. They are obtained as Pearson correlation coefficients measured for the summarized (composite) success variable and the composite variable for each factor. Considering the hypotheses raised about the potential interrelation between each factor in the model and the level of success of outsourcing partnership, the following results were obtained.

H1. The hypothesis for the presence of a positive relation with the commitment of top management is confirmed by the observation of a strong positive correlation (0.82).

H2. The hypothesis for the existence of a positive relation with the establishment of common aims and objectives is confirmed by the observation of a moderate positive correlation (0.68).

H3. The hypothesis for the presence of a positive relation with the effectiveness of the bidirectional transfer of knowledge is confirmed by the observation of a moderate positive correlation (0.64).

H4. The hypothesis for any positive interaction with the degree of achievement of contracted goals is also confirmed, however, at the higher estimated correlation (over 0.88) which provides evidence for the strongest effect of this factor on the level of partnership success.

H5. As assumed, the degree of success of outsourcing partnership is also positively related to the degree of mutual trust, albeit confirmed by a moderate correlation (0.54), possibly due to the simultaneous influence and moderating effect of other variables. These effects should be further analyzed by specific multivariate method.

H6. The hypothesis about the relation with formal security assurance is not confirmed – the correlation is not significant and its negative sign (–0.16) could be ignored. At that stage we can conclude that the formal warranties included in the outsourcing agreement do not

directly contribute to the level of success of the partnership. The results show that other factors (e.g. informal relations and trust) have strongest impact on the response variable.

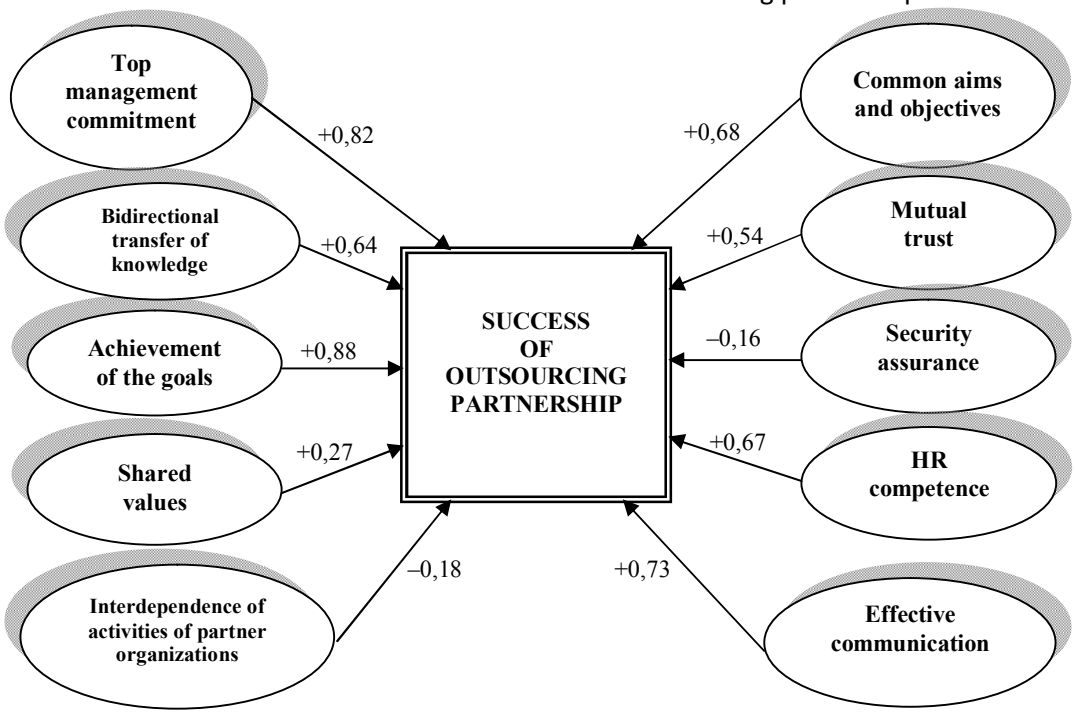
H7. The same result is obtained regarding the interrelation between the degree of success of outsourcing partnership and the interdependence of the operation of vendor and client organizations (weak negative correlation: –0.18). Here the analysis is to be further clarified in order to offset any multicollinearity and moderating effects.

H8. With the evidence of the low correlation (0.27) it can be concluded that the degree of success of outsourcing partnership is not substantially related to the degree of sharing of common values between partner organizations.

H9. The hypothesis about the effect of the competence of human resources is confirmed in light of the moderate correlation (0.67) – the degree of success of outsourcing partnership is positively related to the level of HR competence and expertise.

H10. In light of one of the highest correlation estimated (0.73) the hypothesis regarding the degree of effective communication between partner organizations is also confirmed.

Figure 1: Estimated correlation coefficients in the MKF of outsourcing partnership success



This survey can be treated as step in the probation of a methodology through which a justified evaluation of the characteristics of IT outsourcing partnerships can be obtained. Along with the evaluation of the status of these partnerships, the development and application of this methodology could support the identification of the perspectives for advancement of the outsourcing of high technology services as well as to provide a basis for comparison of local practices with the world experience in this area. This paper contributes to the existing research in IT outsourcing to CEE region by identifying and exploring key success factors of outsourcing relationships in respect of their strategic orientation and overall attainment.

Keywords

IT outsourcing, outsourcing partnership, key success factors.

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A Comparative Analysis of Lithuania Regions: Changes in the Labor Market and Macroeconomic Trends

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Abstract

There are considerable social and economical differences between regions in Lithuania. Regional statistics allows measuring and following these differences. As it turned out, regional differences in the labor market are formed due to demographic, economical, social, geographic and political factors. The most noticeable differences of labor market in the regions are caused by the population, birth-rate, mortality, migration. All these factors influence the regional unemployment and employment levels. Population living in the regions depends not only on the region's geographical location, legal and political environment, the development level of the transport network, but also on economical indicators such as GDP and its generation, export volumes, direct foreign investments, wage levels and so on.

The research shows that labor market indicators are closely linked with the country's overall macro economical situation. Interdependency analysis of these indicators is important and meaningful aiming to determine regional differences and foreseeing their further development prospects.

The objective of the paper: to do Lithuania regions' labor markets comparative analysis in the year 2005 – 2010 in the context of the macro economical trends.

Applied research methods: comparative analysis of scientific literature, synthesis, organization, visualization, assessment of changes and quantitative statistical methods (statistical ranking (classification), linear regression analysis. The research included data from Lithuania Statistics Department and its publications as well as Lithuania's and territorial labor markets annual information. Trying more accurately to assess changes in the labor market in the context of economical fluctuation, six years period have been taken for this analysis.

Findings presented in the paper: significant Lithuanian regional economical differences have been defined: some regions, such as Taurage, Marijampole and Alytus, in the analysis period, managed to keep their VAT more than twice less (in terms for one regional citizen) than economically productive Vilnius region. Meanwhile, labor market indicators in these regions were less beneficial and responded more sensitively to negative changes of economical situation.

In the period of economical downturn unemployment rates in Lithuanian regions converge, but after the crisis economically stronger regions recover faster while in the weaker regions unemployment rate is decreasing slowly.

Only significantly stronger economical regions such as Vilnius and Klaipeda, with more favorable labor market (the lowest unemployment level, the highest employment rate and wages, the largest

working-age population and the greatest opportunities for employment) create a higher added value. This indicates that favorable labor market indexes do not guarantee better economical situation in the region. Increased productivity can be reached with worse labor market performances.

Keywords

The country (regions), labor market, macro economical indicators, regional differences

1. Indicators Characterizing Labor Market

Situation in Lithuania labor market varied substantially during the last decade. Rapidly growing economy has been changed by a recession, which was followed by increase of an unemployment rate and by the number of unemployed people. National economy trying to recover from crisis has encountered with the painful problem for whole Lithuania– the shortage of skilled labor. Economic and financial crisis encouraged the collection of information about labor market. According to the New Millennium Development Goals Employment Indicators (2009, p.10), it's vital for the most countries because informative, fairly treated information about the labor market may help to improve national development plans and to choose the right priorities. Selecting the specific labor market indicators' group, you can learn a lot about the country's development, economic situation and the like. The Global Employment Trends (2010, p.9) states, if you, properly, want to register what changes did the crisis cause in the labor market, it is necessary to examine the trends and few other indicators such as unemployment, employment, poverty, GDP and inflation.

According to A. Pocius, L. Zabulytė (2005), the most important indicator of different calculations for unemployment rate – the number of unemployed people. Although this absolute rate does not enable to compare unemployment intensity scales in accordance with certain areas of the country. Population activity in the labor market makes influence on unemployment indicators. It is expressed by the work force, i.e. a part of economically active population together with the number of analyzed people. Since not all people are economically active, working-age population far exceeds the available labor force. These figures are commonly used to compare indicators of the labor market:

- The labor force – are all employed and unemployed population.
- Employed – analyzed age people (15 years old and older) who, during the research week, worked any job not shorter than 1 hour, for which they were paid or they had benefit. They are persons belonging to the category of employed: manual workers, owners, farmers, employees, family members working in a family company and self-employed.
- Unemployed people – according to the International Labor Organization, they are people aged from 15 to 75, who were unemployed during the analysis week, but when they got the job, they were ready to start working within two weeks. Four weeks, in many ways they were, actively, seeking for paid job. Jobless people applied for employment agency, employers' friends, the media. They looked for premise, equipment for their business, tried to get a business license.
- Working in a family business – are persons who work independently in their own enterprise (registered or not) with two or more partners and do not have permanent employees. Their activity is based on an individual or family work. This category includes farmers and other small agriculturalists, florists, traders, craftsmen, musicians, artists, painters and others.

However, these absolute labor market indicators do not allow the comparison of regions which are of different size, and thus may only reflect the general situation or its changes in the labor market. Therefore relative indicators, such as unemployment level, labor force activity, employment and so on, are used more often. Relative labor market indicators better reflect current situation. They eliminate disparities between regions and show real market situation.

- Unemployment rate – the rate that describes which part of workforce is left unoccupied. It expresses population's activity, because people who are looking for a job are included in the structure of economically active manpower. Unemployment rate is calculated as the proportion of registered unemployed and active population, which is total labor force.

Labor force consists of total number of employees. Unemployment rate shows, how many jobless people, in percentage expression, are, with regard to workforce. In general, the unemployment rate is lower, the higher is economic activity. Calculation of unemployment rate may vary depending on:

- People, representing workforce, working age range;

- Job search time;
- Job search criteria;
- Statistical data about people, temporarily dismissed from work and again returning to the same work, numerical calculation procedure.

When we are talking about unemployment and its scale, it is necessary to mention the level of labor force participation rate – it is 15-64 years active population proportion. It is expressed as a proportion of workforce together with relative age population. And it can be calculated as follows:
Very important is labor force participation rate – the employment rate, which is calculated as a proportion among employed, working – age population and older workers.
M.A. Botezatu and E.Botezatu (2009) identify the following indicators of the labor market:

- Active population – are all persons who work during the period of analysis or are looking for a job;
- Employed population consist of persons aged from 15 years and older, who have a job, and during the period of analysis, worked for at least 1 hour or more than 15 hours in non-agricultural activities. This figure includes all population groups (employed people, employers, people having their own business and others), who work legally and illegally in the public and private sector.

Guide to the new Millennium Development Goals Employment Indicators (2009, p.12) states, that International Labor Market Organization in order to reveal current labor markets characteristics and features, introduces indicators that are directly associated with analyzed labor market problems. The new labor market indicators would be:

- The pace of change in labor productivity (GDP per employee);
- Employed and work force proportion;
- Working people poverty limit;
- Working in a family business and employed relationship.

As stated in mentioned publication, the pace of change index in labor productivity shows changes in GDP for each employee. It also indicates that the link between productivity growth and poverty reduction is the tightest, when development of productivity and labor market are going smoothly. In addition, increase in productivity positively affects social and economic environment, stimulating the reduction of poverty due to investment, changes in economy sectors, international trade and technological progress and improving social security.

An indicator level of working resources shows national economy's opportunities to provide people with work. It also can be linked with economic growth or poverty threat. Employed and labor force proportion can be evaluated by sex or age, in order to reveal different groups possibilities in the labor market. This indicator's disadvantage is that it is quantitative, not showing the quality of work.
Guide to the new Millennium Development Goals Employment Indicators (2009, pp.20-21) points, when this indicator's proportion is between 50 and 75 percent, it means that bigger part of people who can work, really work. A lower proportion shows, that a big part of people for one or other reasons do not take part in labor market. In many European countries, this proportion is lower among women than men. In addition, in most countries working age is calculated from 15 years and more, but this rate may vary and may be diverse in different countries. Increase of indicator means that larger part of population became employed. This positively effects poverty reduction, if busy working places are well paid, productive and safe. High values of this indicator can also display poor situation in the labor market. For example, index value exceeding 80 percent is typical for some developing economics and usually shows the abundance of low – quality jobs.

Wanting to calculate working force poverty indicator it is necessary to determine poverty limit. Different countries use different methods to determine poverty line. In many countries information

is obtained from economic survey, based on personal consumption expenditure or personal income. Private consumption data is generally preferred as they are reliable and provide more accurate study of the household standard of living. The lower the figure the person or household is poorer. This level is determined on the basis of essential net interest seeking to get certain quantity of goods.

According to the Department of Statistics under the Government data (www.gov.stat.lt), in the European Union, relative poverty indicators are calculated under same methodology and they are agreed to call – the risk of poverty indicators. Line of poverty risk is set by counting 60 percent reciprocal monetary disposable median income. Different composition calculations to increase household comparability are used, so called, modified Economical Cooperation and Development (OECD) equivalent scale.

Since the year 2005, income and living conditions survey data is used to calculate poverty risk indicators. Mentioned indicators are calculated on the basis of previous years' income.
Here are the key indicators which refer to poverty analysis:

- Poverty risk limit – relative income proportion, when households receiving lower disposable income are classified as poor.
- Poverty risk rate – people, whose reciprocal monetary disposable income are below poverty line.
- Poverty risk depth – difference expressed in percentage between poverty line and those who live below poverty line, disposable median income.

Working in a family business and employed relationship. According to Guide to the new Millennium Development Goals Employment Indicators (2009, pp. 26-27) this is a newly defined group of persons which includes people working in family business. This indicator is sensitive to economic cycles, as family business is such activity which does not guarantee benefits or social security for workers.

2. Labor Market Changes in the Context of Macroeconomic Situation

Solving macro economical, effective country's functioning issues, unemployment problem occurs. This problem raises a number of concerns in Lithuania: high unemployment rate reduces investment, stops development; more and more people find themselves close to poverty line. Therefore, it can be said that economic situation directly affects labor market.

According to D.Griškevičienė (2006) the extent of unemployment is a changeable proportion, whereas the growth of it is always in progress, and on the other hand, a part of unemployed find a suitable job and supplement the ranks of employed. Unemployment rate is increasing during economic and financial crisis, closure of businesses and when people are trying to find a new job due to unsatisfactory conditions, low wages. The number of unemployed increases because of training graduates who are seeking a job for the first time, of those who left the job due to excessive demands or disposition. Sometimes, and qualified people lose their jobs, often due to unusual or unpopular professions.

S. Millard and others (1997) believe that employment fluctuations are related to business cycles. Both, in the USA and Great Britain the number of worked hour's cyclical fluctuation is identical to production volume changes. Growth of labor market indicators is different in market development and downturn times, and their negative effects during the downturn last longer. As noted in the Labor markets, employment varies cyclically, as it expands during periods when economic activity increases and decreases during the economic downturn. According to B. Martinkus and D. Beržinskienė (2005) each country employment's level is determined by the size of effective general demand as a result of consumer and investment demand. Failure or decline of general demand

suggests reduction of economic activity. Negative change of economic processes signifies the period of economic downturn. Economic downturn leads to increase of unemployed and unemployment. On the other hand, increase of general demand encourages economic recovery, creating conditions for employment growth and decline of unemployment rate. This is explained by the fact that during recession goods and services' output decrease and hence the demand for labor. When economic activity increases, the reverse process takes place. The longer and more intensive period of economic upturn the unemployment rate declines further. A. Simanavičienė and L. Užkuraitienė (2009) mention that the decline is accompanied by such major events as: growing scale of unemployment, increase of state budget deficit as a result of insufficient tax revenues and higher welfare benefits to persons who have lost their jobs, lower companies' profitability is reflected in falling stock price, declining inflation rate, investment slowdown. In D. Laskienės (2009) opinion, economic downturn leads to unemployment increase and during rapid economic growth low unemployment is typical. This relationship is mutual. Declining unemployment rate shows that one of the productions factors' – labor, is used more, which leads to production of goods and services in the country.

Shortage of skills is major reduction reason of work force demand during the growth period. This results in high employment and economic growth which requires substantial changes in knowledge, technology, manpower, geographical situation and demographic factors. According to Labor markets (p.43) shortage of workforce with the right skills may have a significant impact on the economy, it may constrain economic growth.

Economic prosperity of population is closely related to country's economic growth. In international practice it is usual to assess economic growth by the rate of GDP. GDP growth and labor market changes' bond is mutual: on one hand employment is a result of economic growth and on the other – employment is a factor of GDP changes. As A. Pocius and L. Okunevičiūtė – Neverauskienė (2005) say, social and economic impact of this growth factor is always seen as very important, because employment rate allows to decide about country's welfare and labor market policy reliability. D.Laskienė (2009) believes that work is not only an economic growth factor, but also people's income, their social status and self – satisfaction base. Therefore unemployment rate is one of the main indicators of the economic situation.

As noted in the Labor market (2009, p.1), economic crisis began at the end of year 2007, the first steps of it were noticed in financial and real estate sectors of the USA, unfortunately, later it has developed into a recession with negative implications for the economy and, particularly, for the labor market. The global financial and economic crisis encompassed the entire world. Millions of people were dismissed, while those who have managed to maintain employment tries to keep it, working overtime and receiving lower wages.

According to the Lithuanian employment agency's publication 'Labor market forecast' (2009, 2010, 2011, and 2012) situation in the labor market over the last four years has changed dramatically: in year 2008 rapidly rising unemployment became difficultly solved problem. Reduced purchasing power lowered domestic consumption, had a negative impact on development of service sector, reduced the demand for labor in various sectors. Economic and financial crisis has lead the country's GDP downward, which encouraged the rise of unemployment in the country. At the beginning of the year 2011 and 2012 situation has improved, only export goods producing sectors firstly felt it. Situation in the labor market is improving much more slowly: unemployment rate since 2009 decreased an average of only 3.5 percent point when compared to GDP growth in 2010.

As, the experts of Lithuania free market implies, even in the remarkable economic growth, improvement in the labor market can be expected only after 1,5 to 2 years remembering Lithuanian situation a decade ago.

In summary, labor market indicators varies cyclically, that is, employment is increasing and decreasing the same way as the country companies' products are created. Unemployment and vacancies show the highest volatility of business cycle. Meanwhile S. Millard and others (1997, p. 74) find that unemployment tends to rise faster during recession period than to decline in the economic growth period.

It should be noted that economic growth and labor market situation depends on demographic processes occurring in the country for a longer period, particularly on migration, which, today, is very important for the Lithuanian labor market. The main cause of migration – a chance of higher income, better situation in the labor market and so on. Labor migration is associated with labor market condition – employment, unemployment, income level, social security; people's living standard, overall national economic and social situation is important.

Although emigration contributes to the reduction of official unemployment, but its specific impact's assessment on the country's labor market – there is not much in scientific literature. It is believed that emigration affects not only unemployment rate, which significantly reduces during economic growth, but also the absolute number of employed. According to A. Pocius and J. Moksvina (2006) employable people, who have no difficulties to find a job in the domestic market, leave the country. Very high unemployment rate reflects in emigration and in the labor market. In times of economic downturn, the importance of social motives is increasing; it encourages emigrants to return to their families, relatives, and friends, who can help them to survive a difficult period. According to R. Glinskienė, E. Petuškienė (2009), it is likely that significantly changed labor market situation, returning from foreign countries forces to join them, to already, high unemployment rate. Maintenance of unemployed for taxpayers and the state have increasingly become a burden. And on the contrary, in the economic growth working age population concerning economic motives are more likely to leave the country and create added value in emigration countries.

Regarding these studies we can imply that populations' economic well – being is quite closely related to country's economic growth. Economic development and demographic changes (ageing, emigration, and low birth rates) have a significant impact on the labor market. Employment in both economic and social terms is important assessing country's welfare and labor market situation, not only nationwide but in its individual regions too.

3. Regions and Local Economic Development Theory

The region as a concept in the scientific literature is not strictly defined. Lithuanian scientists give region's definitions which are based on foreign authors. Bruneckienė and Klijonienė (2011) identify region as a bigger component of economic – social space, which, from other surroundings, is different in material and information links related with economic, social, demographic, cultural – historical, natural, political or infrastructural systems. These researchers in her article mentions that region can be seen as a territorial unit directly under central government. Region's, as social – economic system's, balanced regional development and its impact on national economy and regional policy Lithuania's scientists began to examine after Lithuania regained its independence.

Assessing a regional concept from Lithuania's aspect, it can be said that region is an integral part of the state, smaller than the state itself, where country consists of a number of regions. Currently, the region is identified as a complex, open and vibrant social economic system in a wider area. The above description is also applied in the European regional policy, where regions are defined according to 1972 adopted Nomenclature of Territorial units for Statistics (NUTS), which breaks into five levels (Department of Statistics, 2011). For example, in case of Lithuania NUTS 1 and 2 levels match country – Lithuania, NUTS 3 level – counties, NUTS 4 level – municipalities and NUTS 5 level – neighbourhood.

According to the law of territorial administrative units and their boundaries article 5, Lithuania consisted of (there was a reform from 2010, July 1st) 10 counties (county's territory is kept as a region): Alytus, Kaunas, Klaipėda, Marijampolė, Panevėžys, Šiauliai, Tauragė, Telšiai, Utena and Vilnius.

Scientific literature distinct society development stages, resources, export, back – country and urbanization level regions' economic theories. Though in each of these theories role of regional labor market is, undoubtedly, important, but it is poorly studied in scientific literature. According to Kilijonienė and Simanavičienė (2010) developed regional economic theories are exceptional due to regional GDP and common national income difference reduction (convergence) or increase (divergence) development interpretations. Regional development theories analysis allows explaining reasons of regional differences, their increase and decrease. Convergence theories explain poorer countries' or regions' higher growth trend regarding to more developed regions. Regional convergences theories deny the need of regional policy, on the base of supply and demand (including labor) prepared models are emphasized on free market mechanism's ability naturally to solve country regions' discontinuity problem. However, this theory is difficult to apply in practice.

There are two regional economic divergence theories: cumulative growth and growth pole. In cumulative growth theory, when there is no state regulation on the market due to economic cyclicality and no market mechanism itself, differences between them are increasing. This theory is supplemented by another divergence theory, i.e. growth pole, which implements that economic growth is the most concentrated in urbanized (urban) areas (Kilijonienė, Simanavičienė, 2010). These authors say that Lithuanian regional economic divergence in the period of economic growth increased and at the occurrence of economic crisis there was noticed a decrease. Currently Lithuania has achieved a take – off phase (when economy is starting to evolve more rapidly), but despite this, large inter – regional differences still exist, which occur comparing both labor marker and macroeconomic indicators. As the studies show, situation in labor market constantly affects domestic and its regional socio – economic life and vice versa, complex long – term studies are required to evaluate this interaction from aspects in dynamic, cyclical and structural changes. This article presents the study that allowed having a look at Lithuania regions' labor market and economical situation's possible interaction applying region's ranking method.

4. Comparative Analysis of Lithuanian Regions

Lithuania is a small country, but surveys show, that there are considerable economic, demographic and infrastructural conditions regional differences, which lead to substantial employment, income level and other socio – economic indicators of regional development disparities. There are numbers of stronger economic growth centers – the capital Vilnius, international sea port of Klaipėda, traditionally strong – commercial centre Kaunas and Telšių region which already has the largest oil refinery in the Baltic countries. These regions attract a bigger part of country's direct foreign investment and this strongly raises region's development level. The remaining six regions are economically less strong and are similar in many demographic and economic indicators.

Aiming to compare Lithuanian regions, according to their labor market and interaction of macroeconomic situation, there was made an analysis. The selected analysis period (2001 – 2011) allowed eliminating analyzed indicators' cyclical fluctuations, since it includes economic boom after the Russian crisis (1998 – 1999) and global economic crisis (2008 – 2010). For regional ranking and comparison, two groups of test facility features have been chosen:

- Labor market indicators (unemployment level, employment, work force participation and poverty level);
- Macroeconomic relative indicators (net earnings, GDP, FDI, export flows per citizen).

For regions' ranking assessing average analyzed period, indicators scores. The most favorable situation has been evaluated by the lowest scores (1, 2 ...) and unfavorable – the highest scores (10, 9 …). Study results are presented in table 1 below:

Table 1: Lithuania regions rank by the most important labor market and macroeconomic indicators

	Alytus region	Kaunas region	Klaipėda region	Marijampolė region	Panevėžys region	Šiauliai region	Tauragė region	Telšiai region	Utena region	Vilnius region
Unemployment, %	6	4	3	1	8	7	2	8	5	3
Employment, %	10	3	2	5	7	8	4	9	6	1
Labour force participation rate, %	10	3	2	9	5	6	8	7	4	1
The risk of poverty, Litas	8	2	3	9	5	6	4	4	7	1
The average net wage per capita, Litas	7	3	2	9	6	8	10	4	5	1
GDP per capita in thousand of Litas	8	3	2	9	6	7	10	4	5	1
The average of FDI per capita in thousand of Litas	6	4	3	9	5	8	10	2	7	1
Export per capita in thousand of Litas	6	3	2	7	4	8	10	1	9	5

The results confirmed Lithuanian regions differentiation and, in addition to the four strongest regions, "the average" – Panevėžys, Šiauliai and Utena regions showed themselves as well as economically weakest regions – Alytus, Tauragė and Marijampolė.

From macroeconomic indicators gaps it is observed that greater difference occurs between the economically strongest regions and the national average, than between the weakest regions and the national average. This shows that in four economically strongest regions is created significantly higher added value per 1 citizen (in terms of FDI, export and GDP) than in the remaining regions. For example, in Vilnius region the average citizen generates twice the share of GDP over the country. Even greater differences are observed in the assessment of FDI and export flows per 1 citizen. Opposite situation is in evaluation of regional poverty level: economically weaker regions' gap with the national average is higher than economically stronger ones. As wages differences per 1 citizen are coherent to other macroeconomic differences, we can assume that these poverty risk differences can be lead to lower work force participation (and thereby less disposable income) in weaker regions.

Comparing the areas under labor market indicators was noticed that gaps from similar average country indicators are smaller, but they appear to be "more sensitive" for a stronger impact on other indicators. For example, when employment increases by just 1 percent, citizens' disposable income will increase, as well as, poverty level decrease and there is a growth of their created GDP.

The analysis of unemployment showed that even in the weakest regions this indicator can be good enough – in Marijampolė and Tauragė regions the average unemployment rates over the analysis period was the smallest. In these regions a few years in row was recorded the highest number of long – term unemployed. According to studies, this inactive part of labor force is most prone to emigrate to other regions of the country and to other countries. For this reason, in those regions registered unemployment rate could be lower and this led to a lower level of unemployment there.

Assessing the situation on the labor market, during the period of analysis, it can be stated that only in the economically strongest and average strong regions, labor market situation is coherent for the economic development level. Meanwhile, in economically weaker regions situation in the labor

market is similar or even better than the national average. However, the opposite case has been determined – in economically strong Telšiai region situation in the labor market is one of the least favourable. This shows that it is "one factory's area" and good economic performance is determined solely by this factory production's selling for Lithuania and foreign markets.

The opposite relationship identified when economically stronger Alytus region's labor market situation is much worse than the economically weakest Tauragė region.

5. Findings

Lithuanian regions over the past decade of economic development are characterized by differences in polarity. In the three economically strongest regions is generated 70 percent GDP. Vilnius region, alone, creates 1, 5 – 2, 5 times more GDP per citizen. Calculating together with Telšiai region, whose high economic indicators are determined by Mažeikiai oil refinery plant sold production, these four regions are exporting 80 percent of goods and services sold in foreign countries. Direct foreign investment, over a decade, entirely Vilnius got 64, 2 percent, and together with Kaunas and Klaipėda regions – 85, 7 percent. The average salary was, also, the highest in Vilnius region – it is 20 percent above the national average and more than 30 percent above wages, which are paid for the economically weakest – Tauragė and Marijampolė regions' citizens.

Situation on the labor market show that only in the economically strongest regions is the highest employment and labor force participation. However, in the economically weaker regions employment is closer to "stronger" regions than labor force participation. This indicates that during the decrease or stop of region's economic development, population structure changes in the labor force downward, i.e. working age population is declining and, accordingly, bigger part of population is becoming inactive in the labor market. This may be due to general demographic trends – ageing population, lower birth rates and so on. Yet, regional differences should not, signally, differ from the general situation in the country.

The study results allow drawing a conclusion that in Lithuania during the last decade existing uneven regional economic situation strongly affects labor market – economically strong regions "attract" well-educated and skilled labor force from other regions, thus becoming much stronger and weakening their "donors". Declining of donors develops less employment, less labor force participation. There is an increase of poverty risk and unemployment. Some people (especially working-age), again, go back to economically stronger regions or foreign countries. This vicious circle is a fundamental problem not only for weak region's population, but for stronger regions too, whereas it is necessary to expand and develop infrastructure, to ensure appropriate living and working conditions to arriving workers. Authorities, population's social security experience constant pressure of the need of increasing unemployment benefits and other welfare funds. Regional disparities also determine irrational use of resources, such as, in economically weaker regions, institutions providing public service (schools, kindergartens and other educational institutions) resulting in shrinking population using them, often work bad and\or cannot provide the required level of service.

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Information Technology as a Source of Competitive Advantage - Are We Sure?

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Extended Abstract

Many of us will recall Nicholas Carr's seminal and somehow provocative article *IT Does Not Matter* from 2003. His inquiry into whether IT has strategic value and into the existence of a positive connection between IT and competitive advantage raised significant interest, although it has also met with indignation from scholars and practitioners according to their numerical responses. Carr's seminal paper addresses the question of why IT has lost its strategic importance despite its growing power and ubiquity. He refers to findings that show a negative relationship between IT spending and firm performance, and quoted the views of practitioners such as Larry Ellison, the CEO of Oracle Corporation, "That most firms spend too much on IT and get very little in return". Carr concluded his perspective by appealing to management to think twice before committing to overhasty IT investments.

Nowadays, many firms are under pressure to demonstrate and justify the business value of IT since it still presents one of the major investments in a firm's life. IT vendors, on one side, are faced with the rapid development of technology and demand for their quick adaptation and implementation while, on the other, they have difficulties explaining the business value of constant investments in IT, especially to management that expects immediate results and a fast return on the investment. In today's environment IT represents a critical success factor in knowledge management and plays a dominant role in the decision-making process. Accordingly, Carneiro (2000) argue that the understanding, interpretation and use of IT may enable fundamentals to be created so as to sustain competitive advantage. However, a brief overview of the literature indicates that a variety of IT terminologies is in currency, along with range of differences in the use of data, measurement, sample size, selection of dependent variables etc. Exploring the value of IT in firm performance and trying to show its dominant role in sustainable competitive advantage is the focus of numerous articles already, yet the field still remains inadequately researched and empirically tested. Evidently, findings show that some scholars claim IT can be a source of competitive advantage and its impact can be either direct or indirect, others suggest that IT cannot be a source of competitive advantage since it does not fulfill the requirements of the competitive advantage concept while, finally, some even argue that IT has a negative impact on firm performance and thus does not create competitive advantage. Generally, we argue that IT can hold the potential for and be a source of competitive advantage, but not automatically. As many scholars acknowledge (e.g. Ray et al., 2004), IT alone will not improve performance or create a competitive advantage. In addition, the same applies to any other resource or capability of a firm.

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In recent years many scholars trying to develop the idea of IT as a source of competitive advantage have been focusing on IT capabilities as a source of competitive advantage (e.g. Bharadway, 2000; Dehning and Stratopoulos, 2003; Mata et al., 1995; Ray et al., 2004; Santhanam and Hartono, 2003). Wade and Hulland (2004) provide a review of research conducted between 1988 and 2000 that relates IT to firm performance and/or competitive advantage. They found out that there is diversity in results and little agreement of the strategic value of IT, even among similar studies. Their overview indicates on four different relationships: (1) IT has a direct and positive effect on firm performance/competitive advantage; (2) IT has a direct and negative effect on firm performance/competitive advantage; (3) there is no connection and no effect between IT and firm performance/competitive advantage; and (4) IT has a contingent effect on firm performance/competitive advantage. Most research indicates a positive impact of IT on firm performance and competitive advantage, either directly (e.g. Bharadway, 2000) or indirectly (e.g. Clemons and Row, 1991). However, some other research shows no relationship between IT and firm performance and competitive advantage (e.g. Venkatraman and Zaheer, 1990) or even a negative relationship (e.g. Warner, 1987). Some research has been inconclusive, such as that by Powell and Dent-Micaleff (1997) that reveals a direct negative linkage between IT and firm performance but an indirect positive impact of IT on firm performance.

Current research has not shown any progress in uncovering the relationships between IT and performance. For instance, Duh et al. (2006) and Merono-Cerdan and Soho-Acousta (2007) suggest a direct and positive relationship, Santhaman and Hartono (2003) and Neirotti and Paolucci (2007) show an indirect/contingent and positive relationship, Martinsons and Leung (2002) and Huang and Liu (2005) were unable to show any significant relationship or link between IT and firm performance, whereas Chen (2000) even show that the relationship is elusive. As Tippins and Sohi (2003) ascertain, most of the literature indicates that IT has been examined as a stand-alone resource. For instance, Duh et al. (2006) explore the extent of IT applications and find a significant direct effect on firm performance. Merono-Cerdan and Soho-Acosta (2007) study the extent of the Internet use showing a positive relationship between external web content and firm performance. Similarly, previous research by Amit and Zott (2001) show how the Internet can influence a firm's value chain, and even change firm and industry boundaries. They cite Amazon as a reference case, although they point out that seeing it via value chain analysis may be too simplistic for today’s environment. They even suggest that no strategic management theory can fully explain the value creation potential of e-business (p. 493) that is becoming a major force in today's economy. Jeffery and Leliveld (2004) demonstrate how well-structured IT models have positive effects on firm performance. Neirotti and Paolucci (2007) assert that IT as a resource can contribute to improved growth and productivity; however, the question of whether IT can be a source of competitive advantage remains unresolved since they discovered that IT spending was not correlated with competitive advantage. Santhaman and Hartono (2003) find that firms with high IT capabilities have greater overall profitability (firm performance) while Ray et al. (2004) show how IT management capabilities can create competitive advantage without necessarily being reflected in performance at the firm level. Huang and Liu (2005) find that IT has no significant impact of firm performance, although in interaction with innovation capital a positive effect on firm performance does exist.

Carr's seminal paper has indeed had a great impact on scholars and practitioners and raises some important questions; however, his remark that *IT does not matter* is not new. Many scholars in the past recognized the same issue, for instance Neo (1988) argues that IT itself does not lead to success. His study confirms the importance of customer needs and management support as factors facilitating the use of IT for competitive advantage, or Powell and Dent-Micallef (1997) who stated that "Technology alone is not enough" (p. 396). We agree that there is something more than just the technology itself. IT has fundamentally changed over the last few years and become embedded in every sphere of our lives. So, any simply argument that IT has no impact or a negative one cannot be easily accepted. IT is an endogenous strategic resource that is bundled with other resources and thus

its influence can be, and mostly is, indirect. Of course, measuring the effect of IT, especially because of the indirect links involved, is not easy and there is no verified framework for that.

The RBV has been recognized as a useful tool for exploring the value of resources, although some scholars have criticized it for being too static, tautological, and too focused on resources and not on capabilities. Consequently, they suggest some improvements to the RBV and new approaches as an extension of the RBV such as the dynamic capabilities view. Barney (2007) importantly contributed to development of the RBV in his latest work by acknowledging that the RBV is not really about resources but about characteristics that resources must possess, and that resource is just a label and different labels have not changed the central proposition of the RBV. Something similar can be said about researching the value of IT since its value may not be visible at first sight and returns are unlikely to be reimbursed the next day. Brown and Hagel (2003) pointed out that many CEOs have looked at IT as a commodity because they have not thought enough about how IT can bring value to the business. We agree with Barney and Clark (2007) who asserted that, despite case studies showing spectacular IT successes, not much has been done to help IT managers in real life.

Our suggestion is for scholars to look from the practitioner's point of view and be more pragmatic. A similar suggestion was made by Jacks et al. (2011) based on their 20-year comprehensive snapshot research of IT on firm performance. In addition, every firm is particular and expecting that buying the software that one's competitor has successfully adopted will also improve the firm's condition and competitiveness is unreasonable. In conclusion, we hope that our short review highlights how important it is to build a coherent framework that can enable the synthesis, comparison and create implications of theoretical and empirical findings. However, it has to be emphasized that the constructs being studied are complex and context-specific, and that this could present a challenge for further research, perhaps by also offering some new conceptualizations.

Keywords

Information technology, competitive advantage, firm performance, resource-based theory

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Applying the Theory of Value-Attitude-Behavior to Young Chinese Consumers' Intent to Purchase Luxury Brands

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Abstract

The market of internationally known luxury brands has grown rapidly since the 1990s without much influence from the recession. During this phase, consumers from Asia, especially from the Greater Chinese market, have made significant contributions to this trend. This research modified the value-attitude-behavior hierarchy model to investigate the factors that contribute to young Chinese consumers' behavior regarding the consumption of luxury brands. Through 388 respondents' views on six internationally known luxury brands and the use of structural equation modelling (SEM), this research confirms the following: 1) brand attachment will influence purchase intention; 2) social influence will affect brand attachment and purchase intention; 3) a luxury brand's experiential and functional value will positively affect a consumer's brand attachment; and 4) a luxury brand's symbolic value will negatively affect a consumer's attachment with the brand and a consumer's purchase intention. The findings and implications of this study are discussed within consumer behavior and branding literature.

Keywords:

Luxury value, value-attitude-behavior, brand attachment, social influences

Contemporary Concepts of Innovation Competition in the Context of Globalization Influence

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Abstract

Globalization involves emergence of new forms of innovation competition that respond to challenges of global market. Among the most appreciable effects of globalization influencing innovation competitive sphere, the following interdependent phenomena can be noted: reduction of trade barriers between countries, high level of knowledge proliferation, development of communication technologies, and as a result, sharpening of competition and forming of complex competitive system. Market responses to these effects are represented mostly with the tendency of consolidation of technological, financial, and other resources. It is concerned with creation of strategic alliances, innovation networks and other forms of cooperation of economic agents, in innovation advantages of large organizations as a rule. Consideration on contemporary approaches to analysis of innovation competition demonstrates an equal significance of external (market structure, specifics of the industry, etc.) and internal factors (company structure, market policy of the company, innovation management) for the outcome of innovation activity of firms.

Keywords

Innovation, innovation competition, globalization

Globalization process entails variety of consequences that modify the economic world. Some tendencies of globalization result in different phenomena reflected in changes in competition mechanisms in the innovation field. Analysis of such phenomena and their effects is significant in view of the fact that innovations are one of the important determinants of the effectiveness of the economic system at whole. Also understanding of competition mechanism in innovation markets under the impact of globalization is useful in making decision at the level of company management. The paper analyses variety of concepts that reveal correlations between changes in innovative behavior of economic agents and factors concerning some of effects of globalization.

The aim of the paper is to clarify following questions:

- what tendencies of globalization have an influence on competition mechanism in innovative markets;
- how does competition mechanism in innovative markets respond to tendencies of globalizing world economy and what new form and means of competition appear in new economic conditions;

Global economy is characterized with more complex competitive dynamics that requires firms to react promptly to changes in technology and to respond to market needs enough quickly. Such specific of economic globalization as wide dissemination of knowledge spurs innovation development as well as it impedes keeping technology advantage for companies. Knowledge dissemination allows new companies to enter the market easier because of declining information barriers, facilitated access to technology, cheap labor and market information (Hosein F.M., Lecher T.G., 2008); Gomory R.E., Baumol W.J. (2004) suppose knowledge dissemination to be the most important element of globalization process. Global market brings potential of effective reallocation and consolidation of resources between markets of different countries. This is associated with appearance of far strong competition on local markets where numerous external agents enter into the rival.

Agents in markets of innovative products (innovation markets) react to global changes with development of new organizational form and new types of relations with competitors in order to form and implement optimum global strategy. Variety of concepts devoted to research on innovation behavior of companies emphasize different aspects of such problems as effective allocation of financial, labor and capital resources, of forming effective structure of business, and other problems. There is regarded question of effectiveness of radical and nonradical innovation strategy and imitation strategy (Acemoglu & Dan Vu Cao, 2010, Grossman & Helpman, 1991, Aghion, 2005). Researchers Luttmer (2007),Atkeson and Burstein (2010) suppose that impact of changes in costs of international trade can vary on microeconomis and macroeconomic level, that means that individual firms's decisions depends on such changes but aggregate welfare does not. Chandy and Tellis (2000) estimate the prevalent thesis about radical innovation inactivity of large firms and incumbents named "incumbent's curse" and conclude that large firms are considered to be inclined to non radical innovations but however during about last 50 years large firms introduced majority of radical product innovation unlike the period before the second half of the XX century. This fact can be estimated as an evidence of significance of access to strong technological capabilities.

Astebro T. and Serrano C., (2011) notice the positive effect of business partnership on innovation outcome that means successful commercialization of inventions and increase in project revenues that substantially exceeds increase without partners' human and social capital invested in the project. Stuart (2000) analyses effects of strategic alliances. The finding is that in general case alliances improve results of innovation activity, but it strongly depends on technological capabilities of the partner, and small technologically weak partners don't add any considerable value within alliance. Researches Das and Van de Ven (2000) analyze two types of innovation strategies, namely technical and institutional ones, and conclude that the first strategy allows to benefit from technological development, and the second one allows to take advantage of making influence on

market agents' decisions, and the choice of the strategy to implement is determined with the nature of the product or technology and the nature of the market. Empirical evidence of knowledge-sharing strategies, examined by Spencer (2003), confirms high innovative performance demonstrated by firms sharing knowledge; author also notes that interacting with global innovation system results in higher outcome of innovative activity than interacting with only national innovation system. Hagedorn and Shakenraad point out the fact that there is a positive correlation between firm size and its inclination to strategic partnership. Dussage, Garrete and Mitchell distinguish different types of alliances – they are link alliances that units firms contributing different capabilities and scale alliances that units firms contributing similar capabilities. Authors suppose that link alliances are more widespread because of desire of firms to acquire new information, technologies and skills in such an alliance. Authors Rycroft&Kash (2004) are close to the idea of strategic alliances and note that globalization caused proliferation of such form of innovation cooperative systems as self-organizing innovation network (including firms, universities, government organizations) that allow to develop innovation development without centralized management what is convenient in conditions of complexity of global regulation. Archibugi&Iammarino (2002) distinguish three categories of globalization of innovation according to market behavior of economic agents: internationally exploitation of nationally produced innovation (the competitive strategy is based on exporting of innovative goods or internal developing of foreign innovative products or benefiting from licensing foreign firms, and specific technological competence is supposed to be a competitive advantage), global generation of innovations (this category includes innovation activity of multinational corporations), and global techno-scientific collaborations (joint innovation projects, scientific and technological exchange are included as forms of innovation activity).Gnyawali and Park (2011), and Tsai (2008) developed the concept of co-opetition that describes the situation of competitors' collaboration and investigated factors of co-opetition, extent of sharing information, positive social effects of co-opetition and effects that require correction. Nicholas (2003), Aghion&al. (2001) analyze innovation behavior of firms from the market point of view; authors show that in some industries competition may stimulate innovation activity, unlike some other industries. Jensen (2001) demonstrates that dominating type of market structure in innovative field is oligopoly. Also Niosi&Bellon (1994) estimate innovative behavior I the global context at the level of markets and conclude that international innovation networks are based on developing local and national innovation systems.

Some researches develop dynamic concepts of competition in innovation markets, analyzing properties of market entry and market withdrawal. For instance, in the dynamic approach researches of Acemoglu D., Dan Vu Cao (2010)conclude that potential competitors are more inclined to radical innovations than incumbent firms are. Ryan S. and Tucker (2011) developed dynamic model of technological adaptation in conditions of network effects. Etro (2004) analyses "patent race" and concludes that market leader can provide radical innovation in order to maintain the leadership after closing the patent race, what is considered to be one of evidence of monopoly persistence and innovative advantages of incumbent monopoly.

Significant role of information in the global economy causes the interest to influence of information asymmetry on types of strategies on innovation markets that is new and not well developed area in researches on innovation competition questions. Innovation markets are characterized with irregular information distribution among agents, which is conditioned by the nature of this type of market and influences competition mechanism peculiarities. Information asymmetry can be observed among sellers and buyers of innovative product, among agents inside the production cycle (for instance among developers of innovation and investors, i.e. buyers of an innovation), inside the production alliances between its partners, among innovation pioneers and their followers. Since information factors finally make an influence on the quality of the end product, on the rate of innovation diffusion, on supporting incentives to innovation activity of firms, then it is important to understand how the competition forms in these conditions, how the economic agents' behavior modifies in

response to the changes in information distribution on the market, what are positive and negative consequences of information asymmetry that occur on innovation markets, and what methods and instruments are employed by firms in order to correct information uncertainty and irregularity.

In conclusion, globalization involves emergence of new forms of innovation competition that correspond to challenges of global market. To summarize the most appreciable effects of globalization that influence innovation competitive sphere, it is appropriate to note the following interdependent phenomena: reduction of trade barriers between countries, high level of knowledge proliferation, development of communication technologies, and as a result, sharpening of competition and forming of complex competitive system. Market responses to globalization effects are represented in the main with the general tendency of consolidation of technological, financial, human and information resources, what is concerned with creation of strategic alliances, innovation networks, 'co-opetition' partnerships and other forms of cooperation of economic agents, in innovation advantages of large organizations (i.e. large firms as well as different forms of partnerships) as a rule. Contemporary concepts of innovative behavior of firms contain analysis of variety of strategies that define features of such consolidation of resources from points of view of firms and markets (analysis of types of alliances, strategy types, types of markets). Consideration on contemporary approaches to analysis of innovation competition demonstrates an equal significance of external (market structure, specifics of the industry, and others) and internal factors (company structure, market policy of the company, innovation management in the firm) for the outcome of innovation activity of firms.

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Personal Perception of the Impacts of the Global Crisis Based on the Results of Quantitative Research

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Abstract

According to many people global economic crisis, which started in 2008, has already come to a halt although it has its impacts felt even today especially nowadays when a next crisis is due. The greatest crisis of the new millennium has had a unique effect on all the players of macro economy. It has also made a sensitive impact on public finances through the financing of public debt and created some vital turning points for companies and households alike resulting in higher credit repayment costs and cutting back on consumption and investment, which, finally, can be assessed as a factor undermining well-being and prosperity. The present study is aimed at illustrating the impacts on households through the results of a questionnaire carried out in 2010 and summarizing the most important effects made on the respondents from different age groups.

Keywords

Global crisis, national crisis, effects, households, primary research

1. Review of Literature

The credit crunch that originated in 2006 from the United States of America reaching its peak by 2007 took a lot of 'tolls' all over the world. By that time the amount of credits taken by the Americans had exceeded 13,000 billion USD (Király – Nagy – Szabó, 2008). Unfortunately, this amount was not only concentrated in the hands of the so-called positive debtors as there were a lot of such debtors who were regarded as problematic, i.e. sub-prime even when asking for loans. The amount of credit itself would not have meant an immediate problem if the real estate market had not started its unexpected, dramatic decline in parallel. Due to bad debt and the problems of macro economy more and more American financial institutions became insolvent. Losoncz (2009, p. 9) in his paper interpreted the emerging crisis mainly as a bank crisis rooting in the banking system that first appeared as lack of trust and later took the form of a liquidity crisis and credit crunch.

The demand for credit dramatically risen in the 2000's was coupled by new financial products and mortgage portfolios described with different mathematical formulae by the banks in the background. As mathematical constructions were very well planned and practically non transparent and they could also be rated as excellent investment opportunities by credit assessors, they proved to be attractive investment forms for every region of the world. In this way almost all the players of the monetary world bought some of them and Europe possesses 39% of it (Király – Nagy – Szabó, 2008).

Soros traces the reasons for the crisis visible even in 2007 back to three mistaken measures and likens it to bursting a super bubble (Soros, 2009, pp. 130-131):

1. long-lasting and dynamic credit expansion,
2. globalised financial markets without borders and
3. not regulated financial markets that gives ground to novel financial constructions.

Quoting Soros, due to the global financial markets and the significant amount of mortgage stock Europe also felt the first impacts of the crisis in 2008. The financial players were compelled to suffer huge losses deriving from their portfolio. Besides, it also gave a headache to the states, companies and households given their enormous debt in foreign currency denominations (Muraközy – Muraközy, 2008). Indebtedness in foreign currency made the countries even more exposed due to the constant exchange rate fluctuations so countries with debt in foreign currency became strongly affected by the ongoing impacts of the crisis as a consequence of their connection to international financial markets. In our country the scenario was similar and the impacts were felt by all the economic sectors especially by the households to a great extent. The crisis also had a great impact on the micro-, small-and medium-sized enterprises whose number is strikingly high in Hungary as of the average of the EU (Bak-Szira, 2011., Fodor et.al., 2012.).

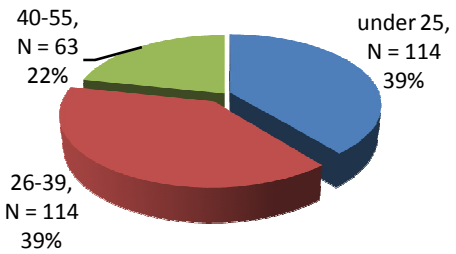
2. Material and Method

Our quantitative research[1] was carried out on the basis of the national survey that was conducted in 2010 and 2011 when the impacts of the global crisis became obvious and experienced. The research was conducted through a pre-tested standardised questionnaire compiled by us and written responses were collected. The questionnaire did not include open questions where respondents could select answers provided by the researcher to make the process of analysis better and easier. Furthermore, care was also taken to avoid such questions that would reduce or impair the willingness of the respondents to answer or would violate their personal rights. Answers were sought to such questions that were not covered in details by the press or media so we mainly relied on the

[1] The title of the research and names of researchers: Dr. Ágnes Csiszárik-Kocsir – Dr. Mónika Fodor (2010): Questionnaire on the impacts of the crisis (Dr. Csiszárik-Kocsir) and its implications on institutional catering (Dr. Fodor).

personal opinions and experience of the respondents. It was also our objective to incorporate such questionnaires in the sample that could convey information for the researcher on the basis of valuable experience. To sum it up, a relatively wide range of respondents by age, position and qualification were preferred to be subject to analysis. The composition of the sample is illustrated by the figure below.

Figure 1: The composition of the sample by age, N = 291



Source: own research, 2010-2011.

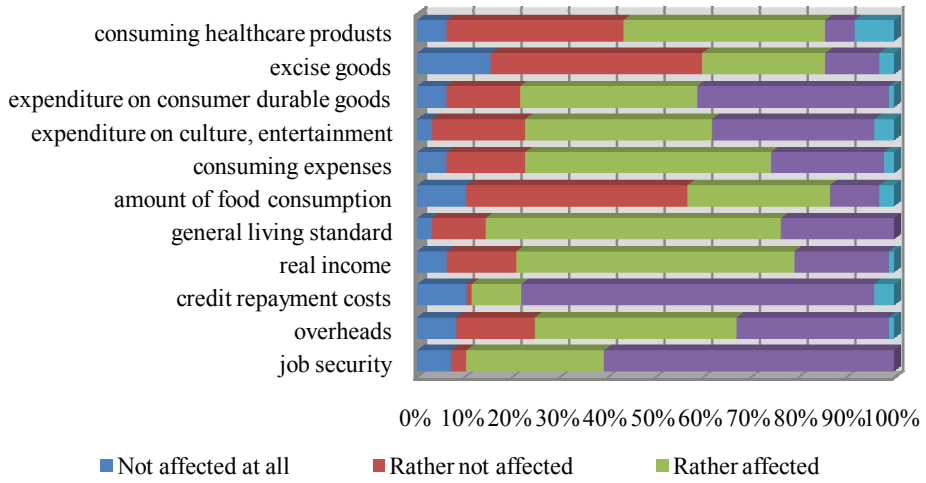
In the first part of the questionnaire an answer was sought what impacts the crisis brought for the respondents, i.e. what has changed in their living conditions. The results and conclusions were analysed by means of basic statistics and cross tab analyses. The questionnaire was processed by SPSS (Statistical Package for Social Sciences) 14.0 and Microsoft Office Excel 2007 programmes. In total, 400 questionnaires were distributed, 61 of which were not returned, 48 were partly filled in so altogether 291 of them could be assessed.

3. Results

3.1. The perception of the impacts of the crisis in the case of respondents by age

The questionnaires were directed at examining the extent to which 'ordinary' people were affected by the crisis regarding job security, growing overheads or changing expenditure on healthcare products among others. The responses are illustrated by Figure 2.

Figure 2: The interpretation of the impacts of the crisis on the entire sample (N = 291, measurement: interval scale)

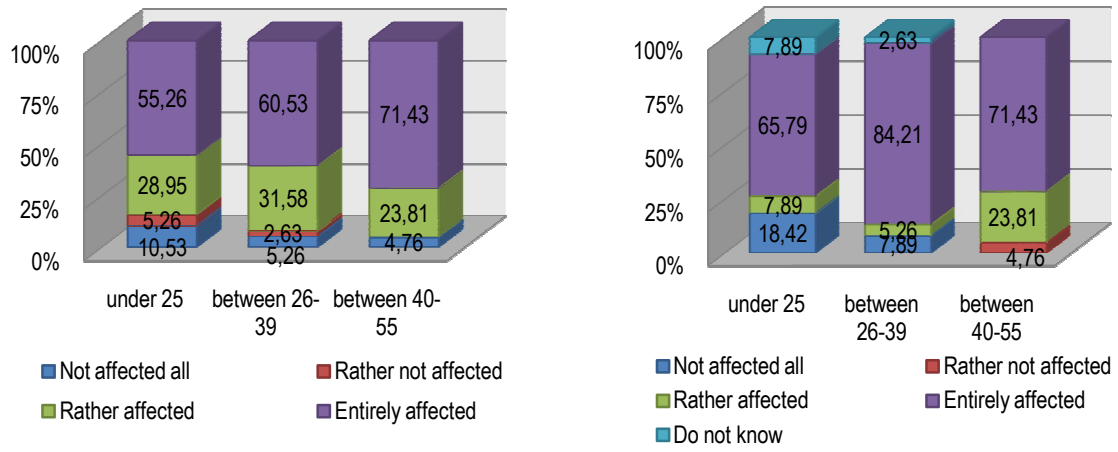


Source: own research, 2010-2011.

The changes in job security were practically experienced by all age groups as all the respondents expressed their personal opinions and involvement in this respect. Considering the sum of the single segments as 100 % it can be seen that a great part (55-72%) of respondents were entirely affected by the loss of job security as an impact of the crisis. It can also be stated that 84% of the young under 25 years of age, 92% of those aged between 26 and 39 and 95% of the elderly experienced the uncertainties in job security.

Regarding the costs of credit repayment respondents also expressed their opinions markedly. Almost all of them possessed a certain type of foreign source when filling in the questionnaire and only 7.89% of the young and 2.36% of those aged between 26 and 39 did not express their opinion due to lack of credit funds. As it is illustrated by Figure 3 more than 65% of the respondents of different age groups were affected by increasing credit repayment costs and interest rates. To sum it up, it can be concluded that 74% of the respondents under 25 years of age, 89% of those above 25 and 95% of the elderly could personally experience financing difficulties as a result of increasing credit repayment costs.

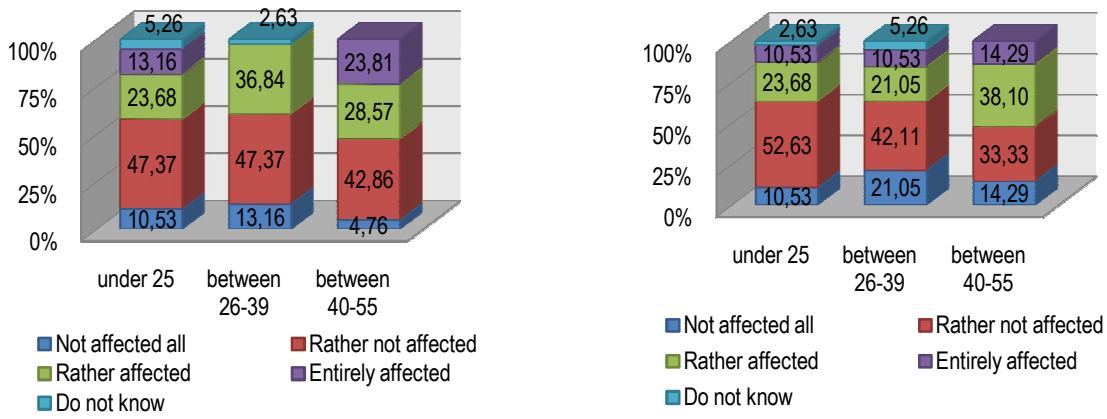
Figure 3: The impact of changes in job security and credit repayment costs in the single age groups (N = 291, cross tab analysis, measurement: interval scale)



Source: own research, 2010-2011.

A further interesting result of the research is that most respondents thought the crisis had not at all had or only made a slight impact on the amount of the food or excise goods consumed. According to the opinions of 58% of the young respondents the crisis had a slight impact on the amount of food consumed and this impact was even slighter in the case of excise goods such as alcoholic drinks, tobacco etc. (63%) The crisis did not make a considerable impact on the food and excise goods consumption of the next age group, either (61% and 63%, respectively). However, those above 40 years of age were affected to a greater extent regarding these two areas as 52% of the respondents felt the impacts of the crisis on food and excise goods consumption as it is illustrated by the following figure.

Figure 4: The changes in the amount of food and excise goods consumed by the single age groups (N = 291, cross tab analysis, measurement: interval scale)



Source: own research, 2010-2011.

Classifying the respondents by age it can be stated that regarding the impacts of the crisis there are significant differences in job security, real income, decrease of the general living standards and expenditure on culture and entertainment in the groups formed by age as shown by the table below. The uncertainties in job security were best felt by those aged between 26 and 40 years of age and the greatest impact was made on this latter group. The reason for this is the general phenomenon in the Hungarian economy. i.e. jobs are mostly filled by the cheaper, younger generation who take over the older but more experienced employees due to financial constraints. Likewise, the changes of the real income had a greater impact on these two segments as a result of the phenomenon described above. The decrease in the living standards affected the segment of those above 40 years of age the most as they are the stratum of society who has to support a bigger family on the given amount of salary. The impact can entirely be explained by the decreasing real income and increasing costs of living. The decrease in the expenses on culture and entertainment was obviously ranked higher by the young in the sample such as those above 40 years of age.

Table 2: The assessment of the impacts of the crisis in the single age groups (N = 291, One-way Anova, measurement: interval scale)

	F	Sig.	Total, N = 291	under 25, N = 114	26-39, N = 114	40-55, N = 63
Job security	3.22	**0.041**	3.433	3.289	3.474	3.619
Overheads	2.02	0.134	3.052	3.026	2.947	3.286
Credit repayment costs	0.28	0.753	3.771	3.763	3.838	3.667
Real income	3.08	**0.048**	2.990	2.816	3.079	3.150
General living standard	3.06	**0.048**	3.062	3.053	2.974	3.238
Amount of food consumption	1.91	0.150	2.619	2.763	2.421	2.714
Consuming expenses	0.14	0.868	3.072	3.026	3.105	3.095
Expenditure on culture, entertainment	4.35	**0.012**	3.330	3.395	2.974	3.857
Expenditure on consumer durable goods	0.08	0.922	3.186	3.184	3.211	3.143
Excise goods	0.05	0.954	2.546	2.526	2.579	2.524
Consuming healthcare products	1.42	0.244	3.062	3.211	3.105	2.714

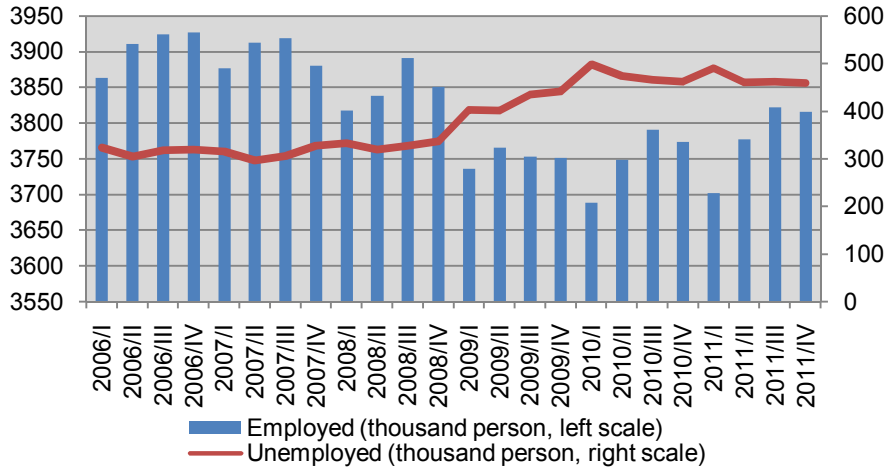
Source: own research, 2010-2011.

3.2 The perception of the crisis based on the education of the respondents

In the first part of the questionnaire an answer was sought how the crisis affected the respondents with different levels of education. The crisis had multiple impacts on households but one of the most general and obvious impacts is the sudden and dramatic rise in the cost of credit repayment and the

drastic fall in the number of jobs (Csiszárik-Kocsir et.al, 2011.). The repercussion of these effects resulted in decreasing living standards and well being and curbing consumption.

Figure 5: Changes in the number of employed and unemployed between 2006-2010

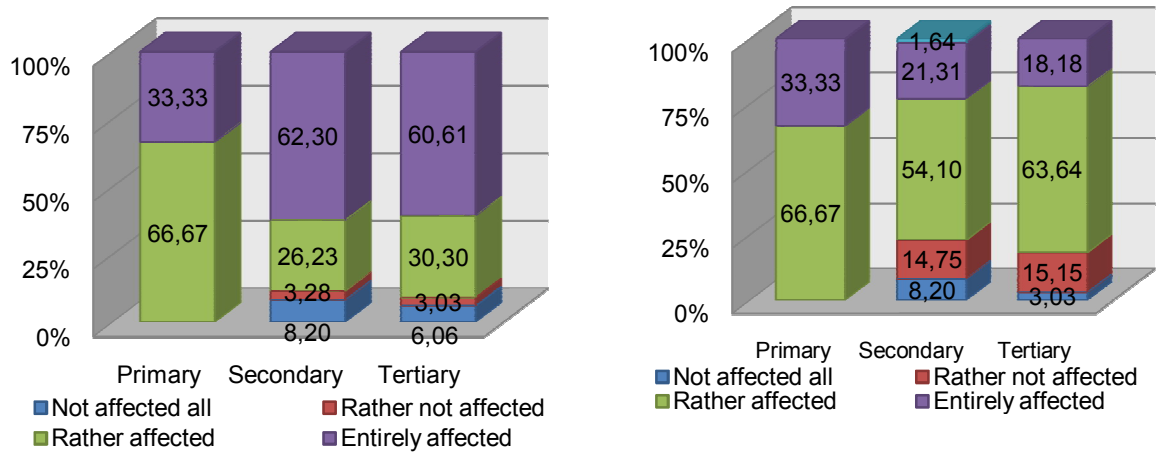


Source: own compilation based on the data of the Central Statistical Office (2011b)

The decrease in job security was mostly experienced by those with elementary education where unemployment rate is the highest. Regarding those with higher education the chances of losing a job were also high as 91% of the respondents that belong to this segment were partly affected while only 89% of those with secondary education were involved in this issue.

Most enterprises tried to manage the negative effects of the crisis that instead of mass redundancies they were about to make a compromise, i.e. by reducing either the working hours or payment. Changes in real income also made an impact on all the respondents with elementary education. Again those with secondary education were the least affected although their proportion can be regarded high as the real income of three quarters of them decreased to a slighter or greater extent. Surprisingly, the real income of 82% of those with higher education decreased, which illustrates that employers were committed to finding alternatives to maintain the relatively low level of salaries for those with secondary education even if it meant curbing higher payment.

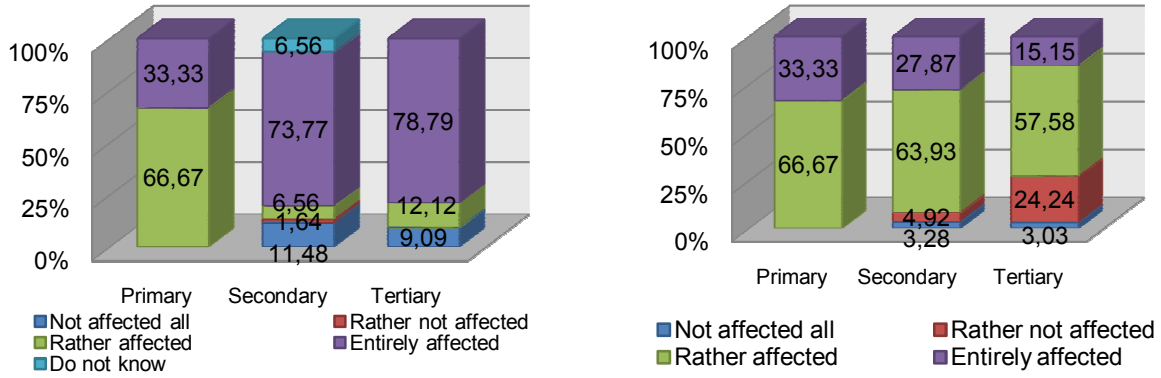
Figure 6: Changes in job security and real income by education (N = 291, cross tab analysis, measurement: interval scale)



Source: own research, 2010.

Like in the case of the previous two factors, the increase in credit repayment costs was also experienced by all the three sectors to a slighter or greater extent. In this case also it was those with elementary education who were the most affected but the increasing burdens also had a great impact on the other two groups, as well. The interesting fact in the sample is that respondents who did not have loans and as a result, opinions either on this impact were only present among those with secondary education. The decrease in general living standards was also experienced by all respondents with elementary education. On the contrary, the segment of those with secondary education was the second in the rank as nearly 64% of them have experienced or currently experiencing a reduction in the living standards. Those with higher education were affected to a slighter extent but even in this case three quarters of the sample were affected.

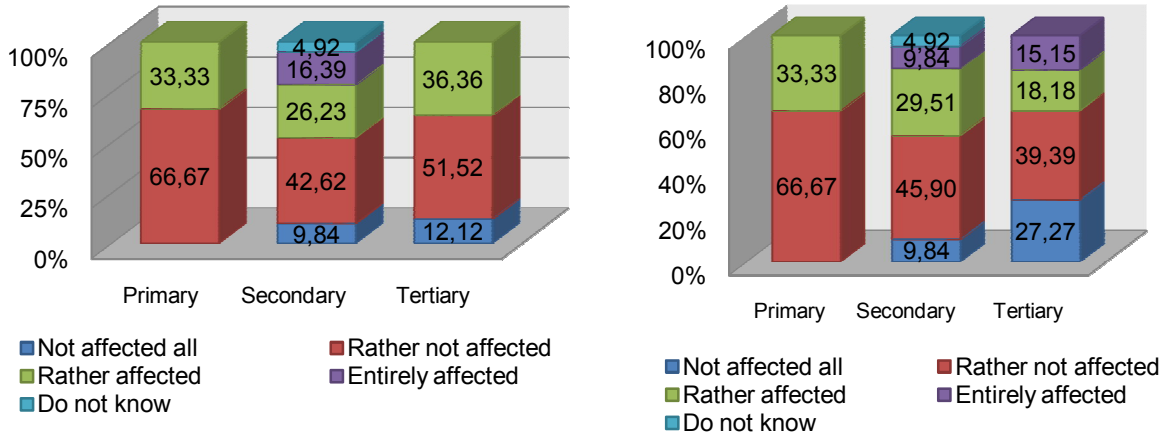
Figure 7: Changes in the cost of credit repayment and general living standards by education



(N = 291, cross tab analysis, measurement: interval scale)
Source: own research, 2010.

An interesting result of the research is that despite the several negative impacts most respondents were not compelled to curb on food and excise goods consumption when filling in the questionnaire. On the whole, it can be stated that households reduce costs on basic food only in the most extreme case. Two thirds of those with elementary and higher education were not affected by the problem although regarding those with secondary education the proportion is nearly half (53%). The same tendency can be discerned in the case of consuming excise goods such as alcohol or cigarette but the number of those with secondary education nearly reaches the other two segments (56%).

Figure 8: Changes in food and excise goods consumption by education



(N = 291, cross tab analysis, measurement: interval scale)
Source: own research, 2010.

4. Conclusion

As presented above we can see that the impacts of the crisis beginning in 2008 and lasting even today have been felt by all age groups of the population. The deteriorating standard of living for the employees who have become more exposed after having lost their job security is the source of enormous social losses, which could only be cured in a long lasting process closely supervised by the government.

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CEO Incentive Compensation Has Assets as Well as Liabilities

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Abstract

In a seven year research project with our colleagues involving longitudinal data analyses and behavioral simulations, we find CEO incentive compensation has some very important positive consequences for society. And these findings may be a cause for a "go slow" response to the plethora of popular media denunciations of excessive CEO bonus compensation. These results are not just for the USA. Rather they are found to be ubiquitous and robust globally.

Our findings demonstrate nations around the world benefit from enhanced GDP growth when many of the firms within their borders had offered CEO incentive compensation programs a year earlier. Nations with less proportion of firms offering CEO incentives experienced relatively slower future GDP growth. The inverse was found not to be true. That is, enhanced GDP growth does not result in greater CEO incentive compensation.

Interestingly, our research indicates the dynamics of greater GDP growth associated with CEO incentive compensation are not as straightforward as one might think. We do not find, for example, enhanced financial performance in each firm whose CEO received bonus compensation. Rather we do find a host of other CEOs, who observe a colleague CEO receiving a bonus, double down on their own efforts. These observing CEOs learn from observation that they may also earn a bonus, and so they hustle more, working harder to meet their Board's objectives. It is much like a chain reaction in nuclear physics. A bonus in one firm bombards five, seven or ten other CEOs to hustle more. A few of these hustling CEOs receive bonuses, and the cycle multiplies. Some of the firms benefit from the enhanced CEO efforts, and profit. However, the link between CEO effort and firm financial performance is a convoluted and complex relationship heavily influenced by random and uncontrollable events. Not all of the firms with the harder working CEOs achieve enhanced financial

performance. But those firms that do benefit contribute to the enhancement of national GDP. Thus, in nations where a higher proportion of firms offer CEO incentive compensation, we find enhanced GDP growth in later years.

Our research also surprised us with a second result. CEOs who received excessive compensation incentives actually slowed down their future efforts, and hustled less. So bottom line: A high proportion of firms offering CEO incentive compensation is good, and yes, there is virtue in some the denunciations found in popular media over excessive CEO bonuses.

To recap: A compensation bonus to one CEO acts as an incentive to other CEOs. Some firm's financial performance benefit from the newly motivated CEOs, but not all firms benefit, as uncertainty in the economic environment assess it's tax. The societies in which CEO incentive bonuses are frequently offered have stronger GDP growth than societies inclined to discourage CEO incentives. However, CEO incentive programs must be wisely designed, and not result in such excessive rewards to CEOs such that they retire while still on the job.

Keyword

CEO pay

Social Media Marketing in terms of Central European Market

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Abstract

The aim of the paper is to verify the effectiveness of selected modern means of communication on a selected online shop of a real brick and mortar company from the environment of small and middle-sized business in the Slovak market and, at the same time, compare results of the research carried out with the same research conducted in previous two years. Selected marketing communication tools used in the research have focused on increasing traffic of the selected online shop. Analyzed relationships were then compared on a year on year basis.

The research object is the online shop of the real company which core business is in bath salts. Using selected internet marketing tools we have tried to raise awareness among potential customers about the online shop and also increase its traffic and growth in number of orders.

The main purpose of this research is to verify the effectiveness of new low-budget promotional possibilities using modern means of communication such as email, blogs, social microsites and social networks. Also, the aim is to compare research results with the same research from March 2011 and March 2010 using secondary data.

Keywords

Marketing, social media marketing, social networks

1. Importance of Marketing Communication

Marketing is the study of exchange processes especially those with goods and services associated, marketing is the human activity directed at satisfied needs and wants, can be also defined as management process in which it is possible to identify and anticipate satisfaction of customers. Based on the literature it is possible to define these activities as a managerial process about obtaining goals through creating and exchanging value on the market place (Adcock, Halborg, Ross, 2001). Marketing activity is one o the most important on the field of attracting the costumer, maintain and enhance long term costumer relationship between both parts business and the market. What's we should take into our consideration on the way of establishing good links is the level of profits, but important is that marketing activities should not destroy mutual respect between businesses but should make it stronger. A climate of cooperation is perhaps most desirable within a channel which is build by business, cooperation can lead to a feeling of satisfaction and partnership, one of give and take. Marketing is giving an opportunity to make stronger cooperation between the partners and leads to personal and organizational ties, ultimately all decision are made between people in organization (Wierzbinski, 2010). Cooperation and interaction in social networks consists of formal and informal relations between actors. Formal cooperation most commonly involves collaboration between firms and public research bodies, while informal cooperation usually occurs through social and personal networks (Waxell, Malmberg, 2007). The functioning of the company in today's competitive environment is largely dependent on develop of innovative approach to marketing solutions and appropriate relations with the environment in which marketing activities are an important factor in building a competitive advantage (Wierzbinski,2011). Possibility to create value within the marketing channel first of all depends on the changeable environment of the marketplace when firms try to reach their aims. In this unstable situation many entrepreneurs deciding to improve competitiveness of the firm by innovation (eg. marketing innovation familiar with new ways of communication process) which has importance for growth and development. (Wierzbinski,2009).

1.1. Social media marketing

In this paper we focus on finding the efficiency of existing low-cost promotion options, such as Viral Marketing, Word of Mouth and Buzz Marketing. Previous findings in this area bring interesting results. The following is a processed overview of knowledge, findings and results of specific studies, which largely highlight the current situation in the area of Social Media Marketing.

Global research and consulting company Forrester Research (in VanBoskirk, 2009) predicts 34% annual growth in Social Media Marketing in 2014, which surpasses all other forms of internet marketing. The reason why this type of marketing is getting on top is large number of people who use social media sites like Facebook, Twitter, MySpace etc. These sites present traders with exponentially larger audience. Another reason is the ability to communicate with consumers immediately via the Internet.

The power of social media can be seen in concrete and real situations. An example of this is a story of Thomas Hawk. This is a blogger who wrote a blog about how PriceRitePhoto refused to sell him a camera if had not bought any accessories with it. The story ultimately led to a heated online debate on portals of the New York Times, Forbes and New Yorker, which resulted in complete abolition of PriceRitePhoto (Hawk, 2005). It was only a spontaneous activity of people using online tools for networking and gain their own experience based on what they need - information, support, ideas, products and power to negotiate with one another. These people have no inhibitions and speak freely on blogs about products of any company and form Facebook or Twitter groups that bear the

name of a product or a company - and nothing can be done about this. This phenomenon is called the groundswell (Li and Bernoff, 2010). Erik Qualman (2009) in this regard argues that only 14% of people trust the information in advertisements. In contrast, only 78% of people trust each other's recommendations and reviews on the Internet. According to Raush (2011) social media have turned traditional the marketing and public relations upside down so now the most important is what people say and not what the companies say. The Word of Mouth (WOM) marketing has recently attracted great attention among marketing professionals. Many consider WOM to be a viable alternative to the traditional marketing communication tools (Bačík, 2009). Many businesses in the United States want to replace traditional forms of communication, because they are losing their effectiveness continuously. This trend is also confirmed by studies of other authors (Grzebyk, 2002, Grzebyk, Kaliszczak, 2008). Trust, Bucklin and Pauwels (2009) indicate that up to 40% of people do not share the view that traditional advertising is a good way to learn about new products and 59% of people even claim that they are buying less of certain products just because their ads are boring and do not provide necessary information to the customer. The survey also pointed out that from September 2002 to June 2004 traditional forms of advertising has seen a significant drop. WOM communication strategy is much more attractive because it provides a better chance to overcome consumer resistance with significantly lower costs and faster delivery - especially through technology as the Internet. Internet provides a space for consumers to share their opinions, preferences, and experiences with others, as well as providing opportunities for companies to use WOM marketing.

Michael Trusov of the University of Maryland carried out a research in 2008 entitled "Effects of Word-of-Mouth Versus Traditional Marketing: Findings from an Internet Social Networking Site", in which information from the Internet social networking were used. The purpose of this research was to describe short-and long-term effects of WOM marketing using data from online social networks. The results were then compared with the results of traditional marketing activities and it was found that WOM marketing has a very strong impact on acquiring new customers. In the long term WOM activities attracted 2.5 times more customers than traditional advertisements. Due to the growth of Internet traffic to social networking sites, such development can be expected in the future. The results of this research point to the fact that WOM communication is crucial for companies seeking new customers because it has greater and more lasting effect than traditional marketing activities. In spite of that it cannot be argued that traditional advertising is already outdated. We believe that good companies should prioritize cooperation of traditional and internet marketing. In print and television advertising they should give people a reason to visit their websites or social network profiles, where they could learn more about the company and its products.

2. Research Objectives and Methods

The article discusses the research task where the effect of low-cost promotion possibilities on the Internet for a particular company was tested. The object being analyzed is an online store specializing particularly in aromatherapy products.

2.1. Formulation of research objectives

The main objective was to verify the effectiveness of current low-cost promotion possibilities, such as Viral Marketing, World of Mouth and Buzz Marketing on the selected company. Research results were then compared with data from previous surveys carried out in March 2010 and March 2011, which goal was the same as ours.

We will explore the possibility of using modern means of communication such as e-mail, blogs, microsites and social networks in e-commerce. Based on the objectives we formulated the following hypotheses:

H1: We assume that annual growth of total traffic of the online store comparing to years 2010 and 2011 will be recorded

H2: We assume that traffic of the online store will increase interannually via mediated messages.

2.2. The research object

The object of research is online store of the selected Internet company operating in the Slovak virtual market. Using selected Internet marketing tools we have sought to raise general awareness about the online store and increase the overall traffic at the same time.

2.3. Data collection methods

Considering the fact that it was a continuation of researches conducted in 2010 and 2011, on-line services such as social networking site Facebook, microsites and blogs were used again as research tools. For evaluating the research, analysis tool Google Analytics was used, by which we monitored the development of individual indicators during the research period. The results were processed and graphically displayed using descriptive statistics.

2.4. Research realization

Word of Mouth – in this part 51 research participants were to spread the good word about the selected online store. The following tools were used for approaching potential customers:

- Email – which included eye-catching text aimed at drawing recipients' attention to the extent that they visit the given online store or further spread the information about it.
- Personal recommendation – this included personal communication with friends and family about the products of the EZO Company.
- Blog – in this part of the task the research participants were tasked to create a blog or a microsite, whose name and description would correspond with keywords such as aromatherapy, esotericism, scented bath salt, sea salt, live salt, oil baths, massage oil, natural hot water bottle, home fragrances, books on esotericism etc. Blog was to refer directly to the online store of the selected company.
- Social network - we decided to use the world's most popular social network Facebook for research purposes.

The above mentioned 51 research participants approached more than 800 randomly selected potential customers via Facebook. Research participants were to invite potential customers (users of the social network) to the "I love a hot bath" group. Subsequently, they were to repeatedly (at least once every 3 to 4 days) share links to any products from the online store of the selected company on their Facebook profiles.

3. Results and Discussion
3.1. Traffic analysis

In this case, we consider Total Traffic to be the key indicator. This indicator is considered to be the primary tool for measuring the effectiveness of low cost advertising. It provides information on the number of users who visited a certain website during the reporting period. Charts 1 and 2 show the development of total traffic of the website of the selected company for the period between 2010, 2011 and 2012.

Chart 1: Development of total traffic in 2010 and 2012

Legend: Návštevy - Visits, marca – March, apríla – April, Graf podľa - Chart by, Návštevy/deň – Visits/Day, Predchádzajúca - Previous
Source: Google Analytics

Chart 2: Development of total traffic in 2011 and 2012

Legend: Návštevy - Visits, marca – March, apríla – April, Graf podľa - Chart by, Návštevy/deň – Visits/Day, Predchádzajúca – Previous
Source: Google Analytics

In these charts we can see that 2010 was the most successful year in terms of traffic, which saw up to 2,465 visitors, which represents more than 30 percent difference comparing to 2012 and 7.6 percent comparing to 2011. This result can be justified by a shift in the preferences of potential customers, as well as the fact that low-cost promotion for the online store reached its limits with regard to the reference market. Despite the identical research methodology, we did not manage to increase the total number of visits of the online store interannually.

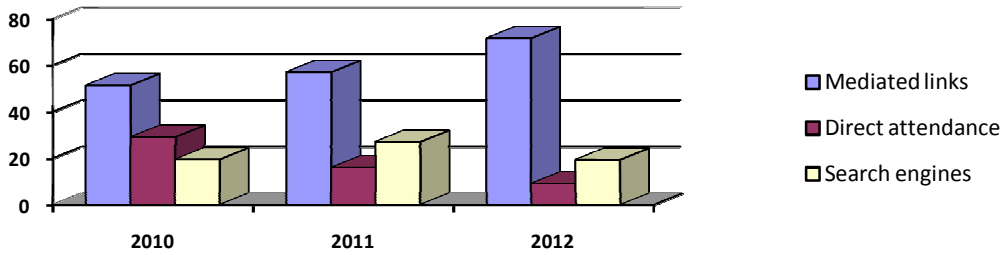
The following H1 hypothesis is rejected: We assume that annual growth of total traffic of the online store comparing to years 2010 and 2011 will be recorded. Changes can also be observed in the development of increase and decrease in traffic. While in 2010 changes in traffic were quite evident, in 2011 a continuous development was witnessed rather than significant variations. Year 2012 shows sudden changes in the first week of the research period, but the following days have been mostly quiet. Attenuation at the end of the research period can be attributed to surfeit of information and attenuation of activity by the research participants.

3.2. Analysis of traffic sources

This part of the research included investigation on where the potential customers got to the online store website from. On Chart 3 we can see that most users came to visit through all the research periods via mediated messages. Links were primarily mediated via Facebook and blogs and microsites, which were to be created by our participants as a part of their task. In 2010, 51.4 percent of visitors got to the company website via the abovementioned tools. In 2011 the number of visitors increased by 6.4 percent comparing the previous period and in 2012 mediated links accounted to 71.6 percent.

This confirmed our H2 hypothesis: We assume that traffic of the online store will increase interannually via mediated messages. It is interesting that while in 2010 direct attendance was ranked second with 29.2 percent; in 2011 the rank was occupied by search engines with 27 percent, while direct traffic reached only 16 percent. This trend is reflected also in 2012, which direct traffic accounted for only 9.1 percent of the total share of traffic.

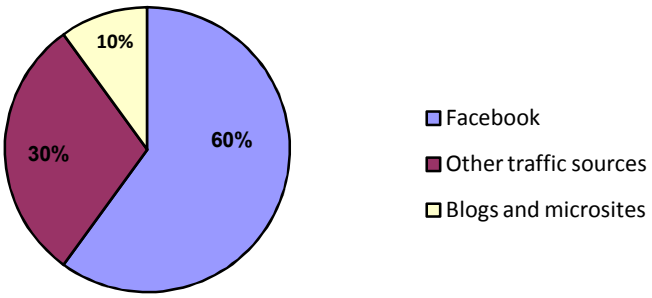
Chart 3: Share of individual traffic sources



Source: Google Analytics

The biggest source of mediated links during the research period (2012) was the social network Facebook, which accounted for up to 59.7 percent of total traffic. Blogs and microsites in the form of engaging articles created in 2012 by the research participants which aimed at spreading the good word, accounted to 10.33 percent of the total traffic. While the comparison of 2010 and 2011 registered a decrease of the number of visitors attracted via blogs and microsites by almost 30 percent, in 2012 nearly 50 percent increase was registered compared to 2011 and 26 percent increase compared to 2010.The reason of this could be more activity on the part of research participants, as well as sufficiently motivating character of blogs and microsites, by which participants tried to reach potential visitors this year.

Chart 4: The share of traffic of Facebook, microsites and blogs on the total traffic in 2012



Source: Google Analytics

4. Overall Evaluation

In this paper we discussed the possibilities of using different types of Internet marketing for a specific company. Using the chosen Internet communications means such as e-mails, blogs, microsites, and last but not least, social networks, we verified the effectiveness of low-cost promotion possibilities and at the same time compared the results of our research with previous researches from 2010 and 2011.

Based on the research results we have reached the following findings: total traffic of the selected online store fell by 30 percent compared with the research period of 2010 and by 22.4 percent compared to the research period of 2011. This result can be justified by shift in the preferences of potential customers, as well as by the fact that low-cost promotion of the given online store in the given form reached its limits with regard to the reference market. Despite the identical research methodology, we did not manage to increase the total number of visits of the online store interannually.

It can be stated that in case of low-cost promotion complementation or innovation of an advertising message as well as forms of dissemination of this message is necessary. Using identical forms of promotion and related identical procedures in the third research year is was simply impossible to achieve the interannual growth of total traffic of the given online store.

The factor of saturated market and the absence of surprise or innovation is a deadly combination in marketing. This applies to the brick-and-mortar, as well as virtual market. At the same time our research had shown the direct impact of social networks (in this case it was the social networking site Facebook) on the traffic of the selected virtual store with the largest source of mediated links during the research period (2012) being the social networking site Facebook, which accounted to 59.7 percent of total traffic (in total, mediated links accounted to 70 percent of the total traffic in 2012). Taking into account the fact that mediated links as a source of total traffic of the researched online store recorded continual growth up to 2010, whereas the social networking site Facebook accounted by a dominant share to the total traffic, it is desirable to draw attention of the online store keepers on promotional activities carried out via this virtual social medium. In this case blogs and microsites account to the total traffic by a negligible share. Therefore, adequate effort or sources from the whole package allocated to promotion are to be provided for those.

We can argue with certainty that the Internet can be a very effective and cost-effective assistance for marketing purposes, if companies learn how to use it effectively. Therefore, in our opinion, a lot of attention is to be given to marketing on the Internet. The results of our research can be beneficial to other researchers, or to expound the issue to professional and lay public.

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Marginal Cost Pricing as a Standardized Public Pricing Rule of Public Firms[1]

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Abstract

Welfare maximizing leads to standardized pricing rule of marginal cost pricing also to be applied by public monopoly enterprises, using price as a parameter of marketing. However, many public firms operate under conditions of fierce competition from other public and, private firms. The difficulties for application of marginal cost pricing that stem from competition get evolved in this article.

Competitive situations in public firm pricing have been considered. In the UK as "commercial rules" where pricing is oriented towards marginal costs but prices should not equal marginal costs. In France, public enterprises should apply what is referred to as péage, which means that mark-ups on marginal costs should be used to avoid losses. These attempts do not consider market processes and competition.

Here, marginal cost pricing under oligopolistic conditions is modeled and debated. The existence of different types of managers leads to very different competitive marginal cost pricing solutions. They demonstrate the difficulties in the application of marginal cost pricing according to the autonomous behavior of oligopolistic suppliers, to other oligopolistic behaviors and with respect to losses and adaptation processes. If competitors try to achieve no welfare goals, use delivery times as a parameter of competitive actions, do not apply the procurement rule, face other market forms and external effects additional difficulties have to be overcome. Suggestions for further research activities are formulated. Key words: Standardized pricing rule, marginal cost pricing, public firms, public firms in competition.

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Accumulation of Capital vs. Dynamics of Economic Growth in Polish Economy

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Abstract

In terms of social and economic development, Poland is placed relatively low in classification as compared with other countries in the European Union. The GDP per capita in Poland in 2010 equaled only 65.0% of average amount for the European Union, and only 59.1% in comparison with the situation before the enlargement of the Union.[2] In 2010, Polish economy generated highest annualized GDP growth in Europe, amounting to 3.8% - which was 2.0% higher value than the average value for the European Union. Such a good result of Polish economy resulted, mainly, from the increase in domestic demand, both in terms of households and the business sector. Unfortunately, increased expenditures in the business sector were connected, to a great extent, with rebuilding supplies and not with investments.[3] Despite relatively good results, it seems that the foundations of Polish economic growth are not stable.

The growth potential of economy depends, primarily, on its accumulation and adaptation abilities.[4] The accumulation ability is determined by the capital resource, which can be used for investment purposes. The accumulation of capital in national economy is a component of national savings from all institutional sectors and net capital inflow from abroad, i.e. in form of direct foreign investments, EU financial support, or foreign loan facilities. The problem discussed in this paper is the low level of accumulation, especially domestic accumulation in Polish economy, which results in low investment rate. Increase in the accumulation abilities in an economy is necessary for maintaining high development dynamics in the long run.[5] Competitiveness of an economy is, apart from performance and macroeconomic balance, also accumulation, investment and allocation of factors of production market.[6]

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[4] Akumulacyjna bariera rozwoju polskiej gospodarki, Ministerstwo Gospodarki i Pracy, Departament Analiz i Prognoz Ekonomicznych [The accumulative barrier of development of Polish economy, the Ministry of Economy and Labour, Economic Analyses and Forecasts Department], Warszawa 2004, p. 4
[5] G. W. Kołodko, Instytucje i polityka a wzrost gospodarczy [Institutions and politics vs. economic growth], in: Strategia szybkiego wzrostu gospodarczego w Polsce [Strategy for rapid economic growth in Poland], ed. G. W. Kołodko, Tiger, Warszawa 2004, p. 24
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The significance of investments varied in different theoretical models of economic growth. Undoubtedly, however, there is a positive relationship between the rate of economic growth and the rate of investment in the physical capital. Increase in investment is necessary for maintaining high pace of economic growth in a long time-perspective, since - thanks to high investment capital - there is the increase in innovation and international competitiveness of companies which, consequently, results in increased production capacity of the whole economy.[7]The dependence of economic growth on rate of physical investment is determined by the creation of increased production capacity which, in turn, allows for removal of bottlenecks and leads to the increase in potential GDP without causing inflationary tension.

Empirical studies also indicated positive relationship between the economic growth dynamics and investment rate. It is especially crucial in case of countries whose economic development is not advanced.[8] Such countries can dynamise the growth process and eliminate the development gap between them and economically developed countries in terms of permanent investment increase. It is a result of the so-called conditional convergence effect. It is obvious that the scale of positive relationship of the increased investment rate is different and depends on many factors such as operational performance of market and its institutional surrounding. Certainly, the internal structure of investment in terms of its material and business scope is of high significance. For instance, the increase in speed of GDP growth in Latin America by 1 percentage point required the increase in investment by 10 points, whereas, to obtain the same result in South-eastern Asia, an increase by only 5 percentage points was required.

The influence of material investments on developmental dynamics of an economy is twofold: On one side, investments influence an increase in capital resource as a component of aggregated demand; on the other side, they lead to an increase in productivity of remaining production factors. Investments, influence, in fact, an increase in quality of accumulated capital by replacing old sources with new, more productive ones. The positive influence of the investment process on the effectiveness of the whole economy takes, of course, place only in case of allocating capital in those economy branches whose effectiveness is above average; otherwise, the investment process does not increase the efficiency of economy as a whole.

Recently, the relationship between accumulation and GDP was at a relatively stable level, between 18 and 25%. The most significant decrease was observed in 2002, when the accumulation rate reached the level of 18.0%. It is a characteristic value for most economies of highly-developed countries, yet too low to start an impulse to dynamise the economic growth.

The economic practice indicates that the main source of funding development should be the domestic accumulation. Such was the approach of classics of economy.[9]The importance of external sources as an element responsible for dynamising economy cannot be diminished. However, incorrect control of inflow of foreign capital may result in too which dependency there from, which may have a negative impact on the long-term development. In extreme cases, it may lead to the so-called "dependent capitalism".

[7] M. Krzak, Czas na inwestycje [Time for investment], Nowe Życie Gospodarcze no. 1/2005, p. 12

[8] R. Rapacki, Możliwość przyspieszenia wzrostu gospodarczego w Polsce [Possibilities of increase in Polish economic growth], Ekonomista 2002, no. 4, p. 478

[9] U. Żuławska, Finansowanie wzrostu gospodarczego [Financing economic growth], in: Ekonomia rozwoju [Economy of development], ed. R. Piasecki, Polskie Wydawnictwo Ekonomiczne, Warszawa 2011, p. 94

In economies of low potential of development, own resources are usually too low to increase the dynamics significantly. Then, taking advantage of external surplus is necessary.[10] Lack of possibility to generate appropriate level of domestic savings translates into limited possibilities in terms of investing in development of production and services, and, consequently, being competitive on the international market. Thanks to foreign investments, this gap is fulfilled.

Subject-related literature indicates even that thanks to the inflow of foreign capital, the limited amount of domestic accumulation ceased to hinder development and the improvement of Polish competitive position.[11]Foreign capital means, usually, introduction of new technologies, know-how, and new management methods.[12]Attention is to be paid to the fact that a major part of foreign capital was an aid for traditional and stagnating, and not for modern sections.[13]

Negative effects of inflow of foreign capital to the host country are especially visible in the case of poor economic situation. Due to crisis and uncertainty on world markets, investors often consider withdrawal from the market or changing priorities to protect their own business. Such a situation can be observed in case of activity of commercial banks in Poland, main shareholders of which were foreign owners. The parent banks, due to the financial problems and incurred losses in other countries, were not able to capitalize their subsidiaries because of the intention to maximize profits in the shortest possible period of time.[14]

[10] Kazimierz Meredyk, Sprawność akumulacji na obszarach aktywizowanych [Efficiency of accumulation in stimulated areas], in: Proces tworzenia kapitału w gospodarce peryferyjnej [The process of creation of capital in peripherial economy], ed. Kazimierz Meredyk, Wydawnictwo Uniwersytetu w Białymstoku, Białystok 2004, p. 43

[11] W. Bieńkowski „Zmiana czynników konkurencyjności Polski w związku z nowymi uwarunkowaniami instytucjonalnymi„ [Change of factors of Polish competitiveness in relation to new institutional conditions] in: Rozważania o rozwoju gospodarczym Polski [Considerations on Polisgh economic development], red. W Bienkowski, K. Szczygielski, Wyższa Szkoła Handlu i Prawa, Warszawa 2009, p. 74

[12] Compare E. Frejtag-Mika, Wpływ bezpośrednich inwestycji zagranicznych na konkurencyjność polskiej gospodarki [Influence of direct foreign investments on competitiveness of Polish economy], Polskie wydawnictwo ekonomiczne, Warszawa 2009, p. 107

[13] K. Janasz, Kapitał w finansowaniu działalności inwestycyjnej przedsiębiorstw w Polsce, Źródła i modele, [Capital in financing the investing activity of companies in Poland, Sources and models], Diffin, Warszawa 2010, p. 63

[14] W. I. Jaworski, Służebna rola banków w warunkach kryzysu [Ancillary function of banks in time of crisis], in: Finanse i zarządzanie przedsiębiorstwem w warunkach kryzysu [Finance and management of company in time of crisis], ed. F. Orechwa-Maliszewska, J. Paszkowski, Wydawnictwo Wyższej Szkoły Finansów i Zarządzania w Białymstoku, Białystok 2010, p. 231

The Relationship Between Corporate Citizenship Behavior and Whistleblowing

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Abstract

Whistleblowing can be expressed as reporting the situation to the authorized bodies and persons inside and-or outside the organization by an employee or a group working in the organization for preventing all damages caused by illegal, unethical and unscrupulous attitudes and behaviors in the organizations.

Whistleblowing behaviors in the organizations come from situational reasons such as interpersonal controversies, organizational reasons resulting from inadequate organizational commitment and non-adaptive organization culture or personal reasons due to any person's overdependence to the ethic and moral values.

Also, corporate citizenship behavior is the whole of active and productive efforts by persons for providing benefit and improving organization. In this behavior pattern, a person displays some behaviors in the organization above the duties and roles assigned to him/her voluntarily. Ultimately, corporate citizenship can be thought as a result of a person's organizational commitment.

In this context, it is really possible to interrelate corporate citizenship behavior with Whistleblowing. Because both of these behavior types can be seen in persons who have high organizational commitment. A person can report any negative situation which is determined by himself/herself in the organization to the authorized bodies and persons easily without considering any interests because of his/her high dependency to the organization.

This study deals with the relation between corporate citizenship and whistleblowing behaviors which are closely related with organizational commitment.

Keywords

Whistleblowing, corporate citizenship

Introduction

Our world is changing continuously, parallel to this change businesses have some changes in their production and management structures in order to catch up with the latest developments and achieve a competitive advantage. While these innovations are increasing, ignoring the work ethics and moral values cannot be something acceptable. The businesses should give importance to work ethics and moral values.

In some businesses, unethical behaviors and their being continuous sometimes cause the disturbance and feeling uncomfortable for some people. In such kind of an event, the employee reports the situation witnessed that is unethical or illegal to some external and internal authorities who has the ability to solve problems and has the power. This situation, reporting a bad or wrong situation by an employee, is called whistle blowing in literature.

Although there are some different definitions of whistleblowing, it can be defined as calling the internal and external authorities (employees, shareholders) having the ability of solving problems and power to inform about the illegal and unethical behaviors and actions in the organization (Aktan, 2008:1).

The term whistleblowing is first used in a legal document that has security risks and hazards in 1963 (Hersh, 2002: 243). After 1990s it has started to be used in academic literature. In literature, "organizational wrongdoing" or "organizational misconduct" terms are used to define whistleblowing. It is seen that the whistleblowers, which is inclined to whistleblowing act, show some behaviors mostly. One of them is organizational behavior.

In organizational citizenship, individuals show extra effort and work as well as their tasks, there is no law or rule for their work. These behaviors are the choice of the person and an entire voluntary act. Such a commitment to the organization causes the employee to do some acts for the benefit of the organization. Naturally, when the 'civic virtue' is considered, it is expected from an employee who has organizational citizenship to call for the authorities in the event of a negative situation.

1. The Concept of Whistleblowing

Whistleblowing is the act of calling for the authority or institutions outside the organizations that have power to change the misconduct against the illegal behaviors or actual/suspected/ foreseen injustices that are seen within the organization or related to that organization by a person who has access to information or data in the organization (Jubb, 1999, 78). In other words, whistleblowing is reporting the wrong behaviors in the organizations to internal or external authorities (Eaton and Akers, 2007, 67). According to another definition, whistleblowing is the reporting of the illegal, unethical or non legitimate activities of group leaders by current or previous employees to the authorities that are willing to take action and powerful enough to reclaim (Keenan, 2007, 85).

In the situation of having o other alternative, whistleblower reflects the unethical behavior to outside in order to perform the common justice based on individual or institutional agreements. This option is chosen after having tried the legal procedures within the organization. Whistleblower can not reject the principals of organizational structure or to the agreement directly. On the contrary, he chooses this way to give voice to his anxiety in the event of violation of contrats. That is why, whistleblowing is against the organizational security but something legitimate (Arendt vd., 2000: 10).

Micelli and Near (1992) state that whistleblowing has two types. These are internal and external ones. If an employee tries to overcome, solve the problems, wrong applications within the organization through informing the managers or executives, it is called internal, if he reports the information to authorities, individuals or organizations, (e.g. media, public interest groups or regulatory agencies) outside, it is called external whistleblowing (Buchholz-Rosenthal, 1998, 399). Both internal and external whistleblowing have similar risks, problems or challenges (Ray, 2006, 438).

Detailed and comprehensive definition of Whistleblowing (Gercek, 2005: 30):

- An alleged crime (fraudulence, theft, etc.), discrimination (race, religion, nation, gender, etc.) or retortion,
- Formation against law, policy, politics, moral values, ethical rules and edification,
- is an act especially to reveal or complain about the subjects that endanger the health and security of the society and it is a verbal or written communication with a person who works at a public institution or private sector.

The term whistleblowing became popular after 1990s. One of the world's most respected weekly news magazine, Time, has had a tradition to declare a person as 'the person of the year' at the end of each year, in December. Although there are no criteria for the person to be chosen to do something 'positive' or to be 'popular', the basic criteria are person's history that how much his deeds affected the people (especially the American society) (Gercek, 2005:30). Shortly before nine years, Time has chose three women Watkins, Cynthia Cooper and Coleen Rowley as the heroes of the year (Verschoor, 2010:15).

Sherron Watkins, chosen as one of the heroes, was a senior manager in Enron, one of the biggest companies of USA. During her management, she realizes the corruption in accounting and informs the top managers about the situation but after that Watkins is discharged from her management position and given a low status position. After that, she declares the fraud to the responsible authorities and institutions and leaves the job. As a result, the collapse of Enron starts (Krishnan, 2011:5).

The other person that is declared as the hero of the year by Time is Coleen Rowley. She was an FBI agent and she confesses that she knew about the 11 September attacks prior to the event. She has reported to the chief that some suspicious people has been taking flight courses and she has been suspicious of Moussaoui, but her sentences has not been noticed by the superiors. After the 11 September attacks, she has written a 13 page report and given it to enate Intelligence Committee. Despite the oppression and discrimination she has continued to pursue her task (Aydin, 2003:80).

The reason why Cynthia Cooper is chosen as a hero of the year has the story that starts with the end of the process that she started to work at WorldCom as financial controller and vice president. She has realized the fraud for $ 9 billion in the accounting and informed the Arthur Anderson, auditor company. The auditor company ignores the situation. After that, Cooper informs the government and the fraud is revealed. At he end, the finance manager of WorldCom is judged with 65 years prison sentence. Cooper is promoted and her salary is doubled (Aydin, 2003:80).

The great scandal uncovered by Jeffrey Wigand's in 1993 is an example of whistleblowing, too. Wigand uncovered that the cigarette company he has been working has put cancer and addictiveness causing chemicals into nicotine. In his confess, he stated that the top managers already knew all about this situation (Miceli, 2004:364-365).

1.1. Types of Whistleblowing

It is possible to classify whistleblowing in two categories, internal whistleblowing and external whistleblowing.

1.1.1. Internal Whistleblowing

Internal whistleblowing is the reporting of unethical or illegal problems to some people within the organization. Reporting the problem to the manager of the organization and asking for solving the unethical and illegal problem can be an example of internal whistleblowing. If the manager knows the problem and does nothing to solve it, the employee can inform the top manager. Therefore, all kind of notifications made within the organization to stop or terminate the events are called internal whistleblowing (Mansbach and Bachner, 2010: 484).

1.1.2. External Whistleblowing

External whistleblowing is the reporting/disclosure of unethical problems within the organization to the responsible authorities outside. The disclosures to government, police and written and visual media or legal authorities are the outside authorities. But there is something that should be kept in mind that it is not appropriate to chose external whistleblowing before internal whistleblowing. So, if internal whistleblowing is not enough to solve the problem, external whistleblowing can be considered (Mansbach and Bachner, 2010:484).

1.2. The Factors that affect Whistleblowing

The studies conducted on whistleblowing focuses on five factors that affect the reporting activities. These factors are (Hassink, Vries and Bolle, 2007, 29-30):

Psychological factors: The psychological factors include features like organizational commitment and loyalty. For example, the more loyal an employee is to his company, the more likely it is that he will report organizational misbehavior, as long as this is advantageous to his employer (Larmer, 1992; Mesmer-Magnus and Viswesvaran, 2005; Miceli and Near, 1988; Street, 1995; Vandekerckhove and Commers, 2004). Overall, the findings of studies on whistleblowers' characteristics indicate that whistleblowers usually hold professional positions, have longer service, and are male. The link between organizational commitment and the intent to blow the whistle is unclear.

Cultural and ethical factors: Individuals from certain nationalities and belonging to specific cultures perceive whistleblowing in another way than people from other cultures might (Brody et al., 1998; Ergeneli, 2005; Gernon, 1993; Thomas and Miller, 2005). In general, studies on culture, nationality and ethics Show significant diversity in the way people from different countries perceive whistleblowing. In this context, collectivism plays a major role, which means that the interest of the company is more important than that of the individual. Therefore, employees from Asian countries, like Japan and China, are more likely to blow the whistle than their Western counterparts, like Americans, are. Besides culture and nationality, a person's decision to blow the whistle is also influenced by the level in which a person perceives this action as ethical.

Structural factors, including policies and regulations concerning whistleblowing: If an organization pursues a policy that stimulates whistleblowing, an individual is more likely to actually blow the whistle. Given the focus of our study, the role of structural factors in whistleblowing behavior will be discussed in more detail below.

Retaliation: When an individual faces harsh punishment for his reporting behavior, or fears such effects, he will be discouraged in blowing the whistle (Arnold and Ponemon, 1991; Dworkin and Baucus, 1998; Miceli and Near, 1994; Mesmer-Magnus and Viswesvaran, 2005; Near and Miceli, 1986). Generally, there is no clear link between retaliation and whistleblowing behavior. It seems that most whistleblowers do not face any penalty, and therefore they do not fear such negative consequences to their actions.

Type of wrongdoing: The decision to blow the whistle depends on the type and severity of the wrongdoing (Near et al., 2004).

2. Organizational Citizenship Concept

Organizational citizenship behavior is a kind of individual behavior that is not taken into consideration directly in formal award system but helps the functions of the organization work properly and based on voluntariness. The voluntariness is used to stress that it is a personal preference of the individual not a behavior that exists in the description of the work. Therefore, organizational citizenship behavior does not require a punishment (Organ, 1988: 4).

Organizational citizenship behavior should be a behavior that is not awarded directly or formally or not be punished. For example, a sales manager is expected to have a good level of job knowledge of ability that is needed for his work. No pressure can be put on him increasing this level. Still, most of the sales managers work a lot to increase their sales capacity. This should be known that if their willingness to increase the sales is related to salary or the promotion, this behavior cannot be considered as organizational citizenship behavior. The increasing performance of one is really appreciatable but it should be known that this is something different than the organizational behavior (Organ, 1988: 5).

Organizational citizenship concept stands for the activities improving the operation of the organization done by the individual as a whole. As a whole is an important term at this point. Most of the organizational citizenship behaviors may not be enough to improve the performance of the organization alone. Organizational citizenship behaviors are considered as unimportant behaviors. This aspect of organizational citizenship behavior can be understood well when the behavior is compared to voting. A vote by an individual seems unimportant but when this considered as a whole it is obvious that elections underlies the democratic systems (Organ, 1988: 6).

2.1. Dimensions of organizational citizenship behavior

Altruism: An employee helps the other employee to accomplish his work under unusual circumstances, taking the responsibility of other if one gets sick and cannot come to work, helping the failed employee, teaching the work rules to a new employee by an experienced employee even if he has no obligation, an employee on holiday comes back earlier and starts work to support his manager are some examples of altruism (Podsakoff, MacKenzie and Hui, 1993).

The altruism dimension of organizational citizenship is not related only with colleagues also with customers, sellers and managers. However, each assistance should not be considered as altruism. Some researchers have defined some criteria for altruism. First of all, the reason of the assistance should be related with organization and as in all the other types of citizenship it should be based on voluntariness. (MacKenzie, Podsakoff and Fetter, 1993 : 70).

Conscientiousness: Beyond the minimum requirements of a role, it is action oriented, helpful and responsible behavior. Conscientiousness are helpful, useful as a whole, focusing to do more than necessary and target oriented behaviors (Organ, 1988). Although one do not receive extra payment, his working overtime to complete a project, one's calling his colleague, who did not come to work, in order to learn whether everything is okay, even if he has no obligation and on holiday, his starting the work eagerly are some behaviors seen in this dimension (Podsakoff, MacKenzie and Hui, 1993).

Conscientiousness is using up the time efficiently to increase the productivity of individuals and groups; in this dimension the employees allocate time for their organizations and make an extra effort (Dipaola and Da Costa Neves, 2009: 492).

Courtesy: this can defined as the warning, consulting and reminding activities of employees that should be in communication as a result of their duty or decisions in the organization (Organ, 1988: 47). This includes all kind of activities as helping the other for the sake of assistance in order to prevent a problem. For example, trying to protect the people who will be affected from an event, informing the other about the rules that should be cared and etc. can examples of this dimension (Podsakoff and Mackenzie, 1994: 513-563).

Sportsmanship: This includes some behaviors such as not complaining and being tolerant in the event of an annoying situation, not accusing the others, commitment to the organization and the leader, being optimistic in a negative situation, defending the organization against the people outside the group, correcting the misunderstandings, etc. (Organ, 1988).

Finally, sportsmanship encompasses behaviors that focus on what is right rather than wrong in an organization (Lin, Lyau, Tsai, Chen and Chiu, 2010: 358). Sportsmanship also includes, not focusing on the wrong issues, being respectful to colleagues, willingness to overcome the obstacles and not seeking for much help (Konovsky and Organ, 1996: 255).

Civic Virtue: Civic virtue includes the behaviors such as employee's learning about the events that affect the organization, attending the meetings and participating to decisions, having arguments on the issues of organization and offering solutions to the behaviors. Taking responsibility and being constructive are some behaviors that are expected from an employee in the organizational citizenship behaviors of this dimension Organ, 1988).

Civic virtues are the responsibilities of the workers as a citizen of an organization; interest or responsibility in macro level towards the entire organization. It shows the willingness of taking a part (attending meetings, explaining the strategies that should be followed by the organization) in the organization. Following the industrial changes and defining the opportunities and threats even if it costs high etc. these behaviors reflects the responsibilities such as being a citizen of a country. This dimension is called 'organizational participating' and 'organizational protection' in some studies (Podsakoff vd., 2000).

2.2. The results of organizational citizenship behaviors

Organizational citizenship is accepted as a key factor for organizational performance. In the organizations having high organizational citizenship levels, satisfaction and commitment to work is seen (Chahal and Mehta, 2010: 29). Organizational citizenship behavior helps to increase the productivity of the employees and managers, use the sources for productive goals, enable the coordination between group members and groups and makes the workplace more attractive to the employees. Therefore, organizational citizenship behavior helps to have creative and productive employees and keep those people in the organization (Motowidlo, 2000: 123).

The core of organizational citizenship behavior is assistance and voluntariness. Fr that reason, having assistance during a hard period or having cooperation has a preventive effect for a non constructive conflict. In the organizations where the employers and employees work in harmony, managers do not spend time on solving the problems. Orientation to the new employees by an experienced one, support by the senior workers, preventing the conflicts, participating the decisions, representing the organization in the activities voluntarily, supporting the organization outside and informing the management about the threats against the organization, all these mean gaining time by the managers (Dipaola and Hoy, 2005:39).

Organizational citizenship may have an effect on the productivity of the employees. In the dimension of civic virtue, employees' recommends for improving the productivity or giving feedbacks makes it easy for management and increase productivity. Employees' assisting the others, mood, adaption and having the feeling of belonging can have an effect on organizational citizenship behavior. Employees' taking responsibility of colleagues when they are off duty or help the colleagues when they are overloaded can have an effect on the balance of organizational performance (Podsakoff and MacKenzie, 1997: 136).

In addition, the contribution of organizational behavior to organizational success can be summed up as in the following way (Cohen and Vigoda, 2000):

- Enhancing coworker and managerial productivity,
- Freeing up resources so they can be used for more productive purposes,
- Reducing the need to devote scarce resources to purely maintenance functions,
- Helping to coordinate the activities both within and across groups,
- Strengthening the organization's ability to attract and retain the best employees,
- Increasing the stability of the organization's performance and enabling the organization to adapt more effectively to environmental change.

3. The Relation of Organizational citizenship and Whistleblowing

It is not easy to report or reveal the bad and wrong behaviors within the organization is not as easy as it is thought. The personal characters and organizational culture are extremely important and decisive (Aktan, 2006).

The employees working at an organization react to the bad behaviors in three ways (Kolarska and Aldrich, 1980).

- **Silence (being silent, ignoring)**: One sees and knows about the wrong behavior, but he avoids report that to the responsible people or authorities. This is like thinking in the way that 'let sleeping dogs lie' or saying the only thing i want you to do not to be around.
- **Rejection and Struggle**: In this behavior, one reports the illegal and unethical behaviors and actions to the responsible person or the authorities within the organization and follows the

situation. If he believes that the event will not be terminated, he uncovers the situation outside the organization.

- **Running away**: This can be an example of third behavior. Victims of psychological terror or mobbing avoid to struggle and believes that the problem can be solved if he leaves the job.

Whistleblowing refers to the second behavior. Civic virtue and organizational citizenship behaviors are seen significantly in the background of this behavior.

Personal virtue is the commitment of a person to moral and virtue. Person always and everywhere objects and reacts against the unethical and illegitimate actions and applications. For one, who has civic virtue, legitimacy is more important than legality. He feels disturbed by the misconducts consciencetiously and as a result have a dispute with the managers and colleagues and rejects the wrong applications. This kind of a behavior is called conscientious objection in literature (Beardshaw, 1981).

Whistleblower is always less powerful than the person he is addressing to in terms of position, seniority, etc. No body urges him to uncover the unethical problem, he thinks it is a task of him. Because he has the behavior of 'conscientious objection'. Whistleblower use his right of speech and freedom to freedom of thought and against the unethical situations, he chooses honesty to tricking himself and others, reality/truth to silence and fraudulent, disappearance from work life to continuity of work life, criticism to ingratiation himself with the organization or the administrators and his moral task to individual benefits and indifference (Foucault, 2005: 17).

The most important feature of organizational citizenship is its having volunteer behaviors. The employee, even if he has no benefit, thinks about the organizational benefits and their volunteer efforts for the organization can be an example of organizational citizenship behaviors. The revealing of unethical /illegal behaviors such as malversation and misuse of the belongings in the organization can be considered as organizational behavior, as well.

RESULT

The concept whistleblowing, which means reporting the unethical and illegal behaviors and activities in order to make the necessary measures to be taken and has a behavior of conscience, is a prime importance subject for public. Public interest that emphasizes that the health and security of people are more important than the finance and personal benefits has a structure including also the environment we live in. Shortly, it covers the essence of the subject in terms of ensuring the health and security of people in the event of psychological harassment, derangement in the financial records (fraudulence), producing harmful products (products having carcinogenic effect and addiction) for human health and harming the environment.

As a result, it is an undeniable fact that there is great relation between organizational citizenship and whistleblowing. In the studies conducted it is observed that the whistleblowers have a high degree of commitment to their organizations. The employee considers calling the attention of external and internal authorities about a witnessed situation or a negative event as a civic task in terms of organizational citizenship and as a volunteer reveals this behavior as a task. He has no expectation. The disappearance of the negative situation is enough for him.

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The Impact of Size on the Quality of Transaction Multiples – Evidence from European Empirical Data

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Abstract

Transaction multiples are a method to generate an estimate on the transaction price of a business that is planned to be sold. During the process of pricing there have to be found comparable businesses that serve as an indicator for the derivation of the needed transaction multiples. Parameters for the identification of the comparables are among others the industry and the size of the business. On the basis of the theoretical background this paper shows the framework of the mothology of pricing businesses by the multiple model and within that the presented study gives empirical evidence whether a size classification of the businesses can improve the quality of the generated transaction multiples either solely (that means whether the transaction multiples face a size effect) or in combination with the widely used industry classification.

Keywords

Transaction-multiples, mergers & acquisitions, size effect, business valuation, valuation of privately held businesses

1. Theoretical Background

1.1. Pricing of privately held businesses by transaction multiples

In a transaction of a business buyer and seller finally have to agree about the transaction price. This transaction price has to be distinguished strictly from its value. The price shows the amount of money that is bargained and finally paid in the transaction and therefore represents the value expressed in an amount of money that is given for the achievement of control over the business. The value of the business however represents only a potential price. It just shows the price at which the business should be transacted but it does not say whether the business finally is really transacted at that specific price.

The common method to generate indications on transaction prices for privately held businesses is the Recent Acquisitions/Transaction Method (RAM/RTM), a specific method of the Market Approach. In this method an indication on the transaction price is generated in a comparison with the recently realized transaction prices of comparable businesses, that means the prices can be derived from the prices at which entire companies or operating units of companies have been sold or the prices at which significant interests in companies have changed hands (Pratt and Niculita, 2008, p. 310). Therefore the comparable businesses that are used as surrogates must be similar to the appraisal subject (Trugman, 1998, p. 125; Pratt, Reilly and Schweihs, 1998, p. 310). The result of this comparison is calculated in terms of a transaction multiple which derives an indication on the individual transaction price for the appraisal subject as a multiple of a specific financial reference figure (especially operating Turnover, EBIT or EBITDA). To choose the relevant businesses in the peer group two different methods can be used. On the one hand, on the basis of an analytical selection process, only a few – but therefore highly comparable businesses – can be added to the peer group. On the other hand, the peer group can consist of all business of the specific industry in question (this method is also called Direct Market Data Method; Miles, 1999, pp. 163).

Transaction multiples (also called deal multiples or acquisition multiples) derive the indication of the transaction price of a appraisal subject (target) on the basis of a comparison with recently realized prices of comparable businesses (comparables, peers). The price of the target is therefore generated as a result of successfully closed transactions on the “free” market for businesses. The starting point of this technique is the basis thought of *Jevons’* “Law of one price” that “similar assets should sell at similar prices”. In a conclusion of that the RAM/RTM follows the assumption that business that are comparable in terms of their essential economic parameters should also be transacted at the same prices.

The RAM/RTM is a highly market-oriented method that is based on already existing prices in the market for businesses and therefore focuses on all integrated market information. In theory the M&A market is the true reflection of current interaction between willing sellers and willing buyers. The use of this method is therefore an expression of trusting in the functionality and the efficiency of the market mechanism (Pratt and Niculita, 2008, p. 313).

The individual transaction price for the target is technically derived in a multiplication of the known financial reference figure (fundamental) of the target (that must be a representative indicator of its economic performance) with the multiple derived from the comparables. This multiple itself is the quotient of the known transaction prices of the comparables and their also known reference figures. In other words the multiple represents the many times the reference figure was paid. By the multiplication of the multiple with the reference figure of the target this relationship between the price and the reference figures of the comparables is transferred directly to the target. It is assumed that there exists a linear relationship between the transaction price and the reference figure. All components of the economic performance that have no influence on the reference figure will therefore also not be transferred to the target. For these factors it is assumed that they either do not

exist or they are equal. Therefore the reference figure must contain all factors that have an (at least essential) influence on the economic performance of the target.

1.2. Types of transaction multiples

Transaction multiples reflect the market price of the total capital and of ownership interests and therefore lead to the Deal Enterprise Value (DEV) of the business. The big advantage of these transaction (Deal Enterprise Value) multiples therefore is their independency from the debt to equity ratio.

The different types of transaction multiples differ in view of the regarded factors that have an influence on the transaction price. Widely used reference figures (because there exists a statistically sufficient amount of information concerning the transaction data) are the Turnover, the EBIT and the EBITDA. As a result of that reference figures the common Deal Enterprise Value Multiples are the DEV/Turnover (it assumes that all businesses have an identical economic growth rate, identical net investing quotes and identical profit margins), the DEV/EBITDA (it represents the purely operative performance of the business in view of the profit) and the DEV/EBIT (it shows the performance of the business in view of the profit before, that means independent of, all financing activities) (for further types of transaction multiples and details on the several types of transaction multiples see for example Pratt, Reilly and Schweihs, 1998, p. 311; Schwetzler, 2010, pp. 574; Aschauer and Purtscher, 2011, pp. 250; Grbenic and Jansa, 2009, pp. 365).

2. Contribution to Literature

The quality, the representativeness, the homogeneity and as a result the reliability of the multiple is highly dependent on the comparability of the peers. Up to now there do not exist any binding guidelines how to assess a business to be considered as a comparable. It is only said that the sample of comparables has to be comparative enough to the target. As a whole the businesses have to be comparable in their overall business model. A guideline for the selection process can give *Porter's* „Five Forces“. Usually the industry, the size of the business, the expectations of growth and the profit and financial situation of the business are used as „primary“ selection criteria (Aschauer and Purtscher, 2011, pp. 246).

Besides these primary selection criteria there are listed several other factors to be considered in determining the similarity of the comparables (the so called elements of comparison), especially: Legal rights of business ownership or business equity, degree of industry specialization, past growth of sales and earnings, rate of return on the physical, functional, human capital and economic characteristics, invested capital, stability of past earnings, quality of management, nature and prospects of the industry, competitive position and individual prospects of the company, basic nature of the activity, general types of products produced, years in business, geographical diversification etc. (for example see Trugman, 1998, p. 126; Pratt, 2001, p. 134; Houlihan and Tack, 1997, p. 153; Behringer, 2009, p. 153).

Up to now there does not exist any reliable procedure for selecting the comparables at least for European data. The theory only presents checklists of parameters to be considered, but these checklists either do not present a reliable ranking of the factors to be considered nor are they based on empirical evidence (Pratt, Reilly and Schweihs, 1998, pp. 315; Ballwieser, 2011, p. 209).

3. Methodology of the Empirical Analysis
3.1. Sample construction and research methodology

The data basis used is a set of data extracted from the M&A database ZEPHYR. All usable data of deal values and corresponding reference figures are extracted from the database and matched to each other. The ZEPHYR database gives the largest number of available transaction data for Europe. In the US there exists a far longer history of collecting such M&A data. Sources of large company transactions are especially the Mergerstat Review, The Merger Yearbook, Mergers & Acquisitions Magazine and SDC Platinum. Sources for middle market and smaller company transactions are especially Pratt's Stats database, Done Deals database, Bizcomps, The IBA Market database and Business Brokers.

The hypothesis tested is whether the classification of the transaction prices in view of the size of the business has an influence on the quality of the multiple. In addition to that it is also examined whether the quality of the common classification of the multiples according to the industry classification can be enhanced by combining the industry classification with a size classification.

At first the transaction multiples are calculated according to the industry classification and the results are presented in form of the first, second (median) and third quartile. Secondly, the same procedure is done according to the classification of the transacted business in view of their size (following the recommended size classification of the European Union 2003/361/EG divided in Small Sized, Medium Sized and Large Sized enterprises). Finally, the two classifications are combined, that means that the multiples are calculated for each industry classified for the different sizes of the businesses.

To be able to evaluate the quality, the representativeness, the homogenity and the reliability of the calculated multiples the variation coefficient is used. The lower the variation coefficient, the higher the quality, the representativeness, the homogeneity and therefore the reliability of the multiples are.

The multiples are calculated for all European countries that deliver a statistically sufficient number of transaction data. They are calculated on the one hand for Europe aggregated and on the other hand for seven regions for which it is assumed that there exist significant differences in the levels of the multiples. These seven regions are 1. Central (Germany, Austria and Switzerland), 2. West (France and Benelux), 3. South (Italy, Spain and Portugal), 4. North (Norway, Sweden, Finland, Danmark and Iceland), 5. Central East (Poland, Czech Republic, Slovakia, Hungary, Slovenia, Croatia, Latvia, Lithuania and Estonia), 6. South East (Turkey, Greece, Cyprus, Bulgaria, Romania, Serbia and Bosnia-Herzegowina) and 7. East (Russia and Ukraine).

The transactions have to fulfill the following criteria to be taken into consideration: The headquarters is situated in the specified region; The transaction (merger or acquisition) was closed within the time period January 1st 2007 to December 31st 2011; The transaction either refers to the transfer of a majority stake and therefore enables the buyer to control the target directly or the transaction refers to the transfer of a minority stake and this stake gives the buyer in combination with the already existing minority stake a majority stake; The transaction of minority stakes (that even not give the buyer a majority interest in combination with eventually already existing minority stakes) are transferred into the level of a majority stake by adding a control premium on the basis of the Mergerstat/Shannon Pratt's Control Premium Study (Median Premium without negatives; see for example Pratt, 2009, pp. 41; Pratt and Niculita, 2008, p. 404); The EBITDA or the EBIT (or the Turnover) have to be positive.

The calculated transaction multiples therefore reflect the Deal Enterprise Value (DEV) of a controlling interest of a privately held business.

3.2. Limitations

Since there is no centrally organized mechanism for collecting and making such price information available, the number of registered transactions is limited. The results of the analysis therefore are dependent on the quality (especially dispersion of the calculated multiples and skewness of the distribution) of the transactions registered. Furthermore it is questionable whether the trend of the multiples in the past will also be continued in the next years.

4. Results

4.1. The impact of the industry classification on the transaction multiples

In the first step the Analysis is carried out for the following six industries: 1. Banking, Insurance & Financial Services; 2. Chemicals, Petroleum, Rubber & Plastic; 3. Computer, IT and Internet Services; 4. Industrial, Electric & Electronic Machinery; 5. Personal, Leisure & Business Services; 6. Retailing and Wholesaling and in addition aggregate. These industries follow the ZEPHUS Industry classification code and represent the industries with the largest number of recorded transaction data.

Table 1 shows either the six specified industries and in addition aggregate the number of the regarded transactions (n), the first (Q1), second (Q2, median) and third (Q3) quartile and the variation coefficient (v) (Other usable statistical measures are the arithmetic mean, the geometric mean or the harmonic mean. Median or harmonic mean is often the better statistical measure, since they eliminate outliers that may skew the average. See for example Trugman, 1998, p. 141; Schwetzler, 2010, pp. 582; DVFA, 2012, pp. 23). The variation coefficient represents an indicator for the quality, the representativeness, the homogenity and the reliability of the calculated multiples. The lower the variation coefficient, the higher the quality, the representativeness, the homogeneity and therefore the reliability of the multiples are. Furthermore the extent to which the multiples are highly clustered or widely dispersed tends to indicate the extent to which the market focuses on that particular multiple.

The analysis shows that the classification of the transactions according to the different industries in most cases leads to a lower variation coefficient (see the shaded areas in Table 1) in comparison to an aggregated calculation. Transaction multiples that are based on an industry classification therefore are higher in quality, representativeness and homogeneity and more reliable. There is empirical evidence found that justifies the industry classification as a (primary) selection criteria for the comparables.

Table 1: Transaction multiples according to the industry classification

Region / Industry	DEV/Turnover (operating)					DEV/EBITDA					DEV/EBIT				
	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v
Central															
Banking, Insurance & Financial Services	138	2,93	9,99	46,73	12,28	51	8,45	17,81	29,91	6,09	62	9,09	19,39	33,90	5,76
Chemicals, Petroleum, Rubber & Plastic	111	1,49	10,33	126,54	4,63	55	8,16	15,57	61,25	2,60	48	10,84	27,11	79,74	1,27
Computer, IT and Internet services	233	1,11	2,48	22,07	3,08	103	9,85	15,10	40,28	1,40	89	11,77	22,27	62,51	1,33
Industrial, Electric & Electronic Machinery	369	0,84	2,02	7,31	3,83	213	6,85	16,48	41,46	4,16	196	9,35	22,07	69,57	5,56
Personal, Leisure & Business Services	297	1,64	11,52	45,49	5,00	93	7,66	13,74	35,41	2,31	86	12,13	21,04	54,59	2,67
Retailing / Wholesaling	153	0,44	0,99	23,37	8,69	90	4,46	8,56	24,23	6,68	85	6,84	12,28	45,80	6,48
Aggregate	**1.301**	**1,02**	**3,40**	**34,17**	**15,48**	**605**	**6,79**	**14,75**	**37,68**	**15,99**	**566**	**9,79**	**20,93**	**61,55**	**13,35**
West															
Banking, Insurance & Financial Services	226	11,02	39,13	325,51	6,39	66	13,91	23,31	173,10	5,11	100	14,25	17,85	38,32	6,73
Chemicals, Petroleum, Rubber & Plastic	267	1,27	8,41	45,11	5,38	173	10,34	35,64	134,55	3,51	158	14,70	43,70	97,50	5,33
Computer, IT and Internet services	788	0,99	2,17	7,36	6,29	551	8,21	22,42	51,79	5,08	474	13,22	38,46	80,65	6,06
Industrial, Electric & Electronic Machinery	571	0,67	2,10	11,60	8,75	378	5,84	14,68	36,31	10,30	372	7,67	21,72	55,13	6,58
Personal, Leisure & Business Services	916	0,75	3,50	33,19	5,94	579	6,67	17,61	38,51	3,89	547	10,35	26,11	60,87	7,82
Retailing / Wholesaling	661	0,67	2,13	32,34	14,98	443	6,07	11,91	34,66	16,66	410	8,59	14,05	47,50	3,21
Aggregate	**3.429**	**0,85**	**3,01**	**27,91**	**24,59**	**2.190**	**6,84**	**17,70**	**44,23**	**21,06**	**2.061**	**10,06**	**24,71**	**70,76**	**14,24**
South															
Banking, Insurance & Financial Services	402	12,22	70,08	324,31	3,93	129	5,99	14,02	62,97	2,70	123	9,04	14,31	56,18	4,15
Chemicals, Petroleum, Rubber & Plastic	303	1,38	4,19	16,41	10,25	211	14,14	41,32	73,60	2,21	150	14,86	29,67	117,65	1,20
Computer, IT and Internet services	391	1,33	4,02	28,43	5,30	271	8,14	22,36	136,32	1,54	232	11,18	44,67	257,60	3,31
Industrial, Electric & Electronic Machinery	605	1,35	6,20	35,00	7,73	352	7,83	20,61	52,06	4,48	317	10,29	29,06	82,23	4,22
Personal, Leisure & Business Services	766	1,68	10,82	31,26	6,80	519	10,25	22,88	51,27	6,85	444	12,67	25,73	50,27	3,64
Retailing / Wholesaling	765	1,49	3,43	20,95	15,74	496	11,83	20,61	63,81	3,33	423	13,65	24,03	98,97	3,85
Aggregate	**3.232**	**1,64**	**7,10**	**39,53**	**10,24**	**1.978**	**9,72**	**21,50**	**66,52**	**6,04**	**1.689**	**11,49**	**25,14**	**82,46**	**4,24**
North															
Banking, Insurance & Financial Services	321	5,97	26,99	125,01	11,84	85	8,94	33,53	60,83	1,73	110	6,29	17,19	58,58	2,14
Chemicals, Petroleum, Rubber & Plastic	86	2,63	13,65	70,67	2,65	38	11,70	20,15	65,10	1,20	38	15,28	30,15	146,68	4,06
Computer, IT and Internet services	817	1,28	4,47	22,12	4,05	350	5,82	19,45	72,68	11,37	311	6,85	22,03	112,93	3,06
Industrial, Electric & Electronic Machinery	758	2,32	7,98	51,09	4,59	227	11,59	25,05	103,14	3,87	236	12,65	33,28	208,93	3,42
Personal, Leisure & Business Services	1.049	2,29	12,45	50,56	5,85	278	7,01	23,79	71,24	9,79	287	7,94	27,20	107,69	3,65
Retailing / Wholesaling	620	1,08	14,81	73,71	6,04	217	5,03	15,43	39,20	6,08	233	6,38	19,98	66,47	4,46
Aggregate	**3.651**	**1,91**	**9,41**	**51,12**	**11,02**	**1.195**	**7,16**	**21,05**	**68,41**	**8,76**	**1.215**	**8,07**	**25,12**	**101,35**	**4,78**
Central-East															
Banking, Insurance & Financial Services	197	2,77	5,45	35,04	8,49	53	11,69	17,02	28,14	1,90	90	9,52	20,05	39,09	4,32
Chemicals, Petroleum, Rubber & Plastic	179	0,57	1,11	3,03	3,04	43	5,04	8,66	21,32	2,04	122	9,97	14,26	32,43	1,65
Computer, IT and Internet services	302	0,92	1,95	4,54	5,71	99	5,65	8,38	22,99	2,38	189	6,75	13,07	27,51	3,27
Industrial, Electric & Electronic Machinery	172	0,61	1,05	2,80	3,35	45	4,12	10,95	12,92	1,32	100	6,31	15,71	25,83	3,94
Personal, Leisure & Business Services	306	0,62	1,46	4,26	3,78	101	4,74	11,31	35,62	3,23	187	6,27	12,32	30,15	2,32
Retailing / Wholesaling	565	0,42	0,92	2,35	4,96	155	5,17	11,55	25,47	3,68	345	9,46	16,07	26,02	3,03
Aggregate	**1.721**	**0,60**	**1,46**	**4,38**	**14,22**	**496**	**5,17**	**11,39**	**23,41**	**3,72**	**1.033**	**7,97**	**15,10**	**28,07**	**8,42**
South-East															
Banking, Insurance & Financial Services	187	0,02	6,35	50,73	4,08	69	0,76	14,98	72,33	6,10	92	0,96	12,18	37,97	3,46
Chemicals, Petroleum, Rubber & Plastic	145	0,38	1,13	2,89	4,42	96	6,89	11,49	19,28	1,46	94	7,48	12,63	25,37	1,93
Computer, IT and Internet services	84	0,90	1,97	5,67	6,30	46	5,32	9,57	19,98	2,23	50	6,01	17,97	40,44	4,64
Industrial, Electric & Electronic Machinery	159	0,71	1,63	5,22	3,72	97	5,53	14,23	24,95	2,49	102	8,47	19,97	53,96	3,60
Personal, Leisure & Business Services	214	0,87	2,50	7,00	14,48	131	4,57	10,13	14,70	3,15	148	4,87	13,74	26,46	3,86
Retailing / Wholesaling	414	0,46	1,09	2,75	7,20	240	5,33	12,11	31,19	3,13	243	4,34	12,36	22,14	6,21
Aggregate	**1.203**	**0,50**	**1,51**	**5,93**	**28,28**	**679**	**5,23**	**11,34**	**23,85**	**4,72**	**729**	**4,99**	**13,56**	**26,94**	**5,27**
East															
Banking, Insurance & Financial Services	181	1,27	9,70	152,29	3,18	11	5,02	15,58	59,22	2,24	91	14,50	252,49	534,51	1,70
Chemicals, Petroleum, Rubber & Plastic	219	0,50	1,19	4,66	10,29	7	14,43	20,58	25,02	1,69	195	2,94	9,14	32,50	10,85
Computer, IT and Internet services	91	1,41	2,19	5,06	6,28	4	10,29	13,49	745,78	1,70	79	6,90	14,04	54,78	8,37
Industrial, Electric & Electronic Machinery	168	0,42	0,81	1,99	2,66	13	2,38	3,89	23,13	3,00	125	3,84	9,63	17,76	3,41
Personal, Leisure & Business Services	414	0,54	1,28	7,68	5,37	7	4,74	5,94	36,77	2,36	289	4,83	10,15	58,78	14,98
Retailing / Wholesaling	581	0,48	1,89	8,75	6,09	28	6,83	9,27	28,67	2,03	471	6,26	18,55	53,57	11,77
Aggregate	**1.654**	**0,54**	**1,57**	**8,12**	**6,21**	**70**	**4,68**	**10,18**	**30,54**	**3,65**	**1.250**	**5,15**	**13,76**	**53,05**	**11,56**
Europe aggregate															
Banking, Insurance & Financial Services	1.652	3,78	21,48	165,64	17,00	464	8,59	17,18	53,33	6,04	668	8,85	18,16	76,23	5,00
Chemicals, Petroleum, Rubber & Plastic	1.310	0,76	2,54	14,46	8,16	623	8,73	20,58	73,41	3,44	805	9,14	17,49	57,78	8,21
Computer, IT and Internet services	2.706	1,12	2,85	14,00	5,71	1.424	7,38	17,84	54,66	11,95	1.424	9,54	25,19	80,78	29,35
Industrial, Electric & Electronic Machinery	2.802	0,98	2,89	23,89	8,09	1.325	6,98	17,22	44,24	8,34	1.448	8,39	21,42	68,58	11,45
Personal, Leisure & Business Services	3.962	1,03	4,80	31,96	38,62	1.708	7,03	16,99	45,58	9,93	1.988	8,59	20,16	55,11	32,71
Retailing / Wholesaling	3.759	0,65	2,06	16,79	11,65	1.669	6,54	14,38	40,24	18,43	2.210	8,38	17,07	48,35	18,66
Aggregate	**16.191**	**0,97**	**3,51**	**26,46**	**46,25**	**7.213**	**7,21**	**16,68**	**48,67**	**18,35**	**8.543**	**8,73**	**19,37**	**61,30**	**18,82**

4.2. The impact of the size classification on the transaction multiples

The size of the business is viewed as another primarily selection criteria for the comparables. In general appraisers believe that it is helpful to place a size restriction of no more than 10 to 25 times the sales volume of the target (Trugman, 1998, p. 128). The classification of the size of a privately

held business can be based on different criteria, especially the (operating) turnover and the sum of the balance sheet. In the following analysis the classification is based on the operating turnover following the recommended size classification of the European Union 2003/361/EG that divides businesses into the classes Small Sized, Medium Sized and Large Sized enterprises.

Table 2: Transaction multiples according to the size classification

Region / Size	DEV/Turnover (operating)					DEV/EBITDA					DEV/EBIT				
	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v
Central															
Small Sized Enterprises	448	4,21	20,41	90,78	9,48	74	14,59	33,45	88,71	5,81	69	21,04	51,63	186,62	5,63
Medium Sized Enterprises	301	1,36	4,65	36,90	2,03	122	9,39	15,50	32,36	2,88	114	11,94	18,97	56,54	2,60
Large Sized Enterprises	552	0,58	1,32	3,03	2,96	409	5,96	12,56	35,38	1,65	383	8,91	17,44	57,79	7,43
Aggregate	**1.301**	**1,02**	**3,40**	**34,17**	**15,48**	**605**	**6,79**	**14,75**	**37,68**	**15,99**	**566**	**9,79**	**20,93**	**61,55**	**13,35**
West															
Small Sized Enterprises	940	2,81	17,04	123,81	12,93	295	10,47	34,10	165,78	10,06	260	14,26	47,58	185,49	5,38
Medium Sized Enterprises	828	1,18	4,09	41,28	18,62	474	9,27	25,99	87,39	3,02	448	12,53	33,23	109,62	7,16
Large Sized Enterprises	1.661	0,55	1,46	6,94	2,87	1.421	6,21	13,85	34,63	3,55	1.353	9,44	19,91	49,79	4,11
Aggregate	**3.429**	**0,85**	**3,01**	**27,91**	**24,59**	**2.190**	**6,84**	**17,70**	**44,23**	**21,06**	**2.061**	**10,06**	**24,71**	**70,76**	**14,24**
South															
Small Sized Enterprises	1.025	5,02	47,50	239,54	6,08	333	10,16	46,66	163,78	3,13	291	13,41	66,89	246,94	3,11
Medium Sized Enterprises	570	0,93	3,21	23,74	2,60	433	8,81	21,04	113,77	1,68	389	11,76	40,40	202,84	3,29
Large Sized Enterprises	1.637	1,49	3,76	16,98	2,99	1.212	10,14	19,54	47,85	6,98	1.009	11,34	20,14	48,71	4,86
Aggregate	**3.232**	**1,64**	**7,15**	**39,53**	**10,24**	**1.978**	**9,72**	**21,50**	**66,52**	**6,04**	**1.689**	**11,49**	**25,14**	**82,46**	**4,24**
North															
Small Sized Enterprises	2.182	4,17	22,67	103,20	8,80	437	7,39	26,69	159,27	6,04	414	7,78	37,03	167,82	4,08
Medium Sized Enterprises	642	1,08	5,68	24,08	9,25	306	9,11	23,50	48,49	2,93	274	10,13	25,09	69,28	3,13
Large Sized Enterprises	827	0,91	2,47	7,24	3,83	452	5,56	17,79	58,16	1,72	527	6,10	21,84	82,65	3,86
Aggregate	**3.651**	**1,91**	**9,45**	**51,12**	**11,02**	**1.195**	**7,16**	**21,05**	**68,41**	**8,76**	**1.215**	**8,07**	**25,12**	**101,35**	**4,78**
Central-East															
Small Sized Enterprises	841	0,94	3,24	15,47	10,33	216	4,94	14,27	37,57	3,41	328	7,97	18,09	49,30	3,74
Medium Sized Enterprises	442	0,51	0,99	2,33	3,94	118	7,25	11,03	27,03	2,20	316	8,42	14,69	26,02	3,02
Large Sized Enterprises	438	0,49	0,89	1,69	1,11	162	5,00	10,51	15,49	2,85	389	7,67	14,97	20,98	8,44
Aggregate	**1.721**	**0,60**	**1,46**	**4,38**	**14,22**	**496**	**5,17**	**11,39**	**23,41**	**3,72**	**1.033**	**7,97**	**15,10**	**28,07**	**8,42**
South-East															
Small Sized Enterprises	634	0,96	3,41	19,16	20,54	343	5,03	11,39	25,14	6,18	342	6,58	16,75	47,57	4,44
Medium Sized Enterprises	184	0,43	1,08	3,90	2,09	119	4,35	10,34	27,41	2,36	135	6,52	12,05	26,23	2,01
Large Sized Enterprises	385	0,30	0,74	1,52	3,23	217	6,74	12,01	18,08	3,36	252	1,79	10,66	20,74	6,92
Aggregate	**1.203**	**0,50**	**1,52**	**5,93**	**28,28**	**679**	**5,23**	**11,34**	**23,85**	**4,72**	**729**	**4,99**	**13,56**	**26,94**	**5,27**
East															
Small Sized Enterprises	635	0,64	4,18	40,00	3,99	29	6,70	41,33	67,37	2,64	375	7,51	33,46	306,46	11,14
Medium Sized Enterprises	304	0,50	1,18	3,78	2,83	15	3,55	15,58	20,58	3,26	201	6,47	17,76	103,02	2,81
Large Sized Enterprises	715	0,54	1,26	4,42	2,02	28	4,01	6,95	9,38	0,90	674	4,04	9,85	23,75	4,53
Aggregate	**1.654**	**0,54**	**1,57**	**8,12**	**6,21**	**72**	**4,56**	**9,38**	**28,67**	**3,70**	**1.250**	**5,15**	**13,76**	**53,05**	**11,56**
Europe															
Small Sized Enterprises	6.705	2,10	13,48	93,55	30,06	1.727	6,92	22,69	91,19	12,33	2.079	8,72	28,53	131,09	19,30
Medium Sized Enterprises	3.271	0,81	2,59	18,23	24,02	1.587	8,15	19,00	65,98	3,23	1.877	9,92	21,61	87,01	8,87
Large Sized Enterprises	6.215	0,67	1,73	6,40	3,47	3.901	6,85	14,81	37,22	8,03	4.587	8,33	16,37	44,60	7,16
Aggregate	**16.191**	**0,97**	**3,51**	**26,46**	**46,26**	**7.215**	**7,19**	**16,66**	**48,55**	**18,35**	**8.543**	**8,73**	**19,37**	**61,30**	**18,82**

Table 2 shows either the three specified size classes and in addition aggregate the number of the regarded transactions (n), the first (Q1), second (Q2, median) and third (Q3) quartile and the variation coefficient (v). The variation coefficient again represents an indicator for the quality, the representativeness, the homogenity and the reliability of the calculated multiples.

The analysis shows that the classification of the transactions according to the size of the businesses leads in most cases to a lower variation coefficient (see the shaded areas in Table 2) compared to an aggregated calculation. Transaction multiples that are based on an industry classification therefore are higher in quality, representativeness and homogeneity and more reliable. There is empirical evidence found that justifies also the size classification as a (primary) selection criteria for the comparables (an analysis solely for Central Europe (Austria, Germany and Switzerland) see Grbenic and Zunk, 2012, pp. 29).

In addition to the finding that the classification of the businesses according to their size can improve the reliability of the transaction multiples the analysis also shows that smaller businesses are regularly sold at higher multiples than larger businesses. This is remarkable in so far as the valuation

theory is nowadays trying to find any empirical evidence and according to that methods to reduce the (fair) value of small and medium sized enterprises (in the US empirical evidence is found on the stock market according to the Morningstar Studies and the Duff & Phelps Studies; see Pratt and Grabowski, 2010, pp. 233), especially the adjustment of the beta in view of the weaker or even lagging capability of the owner of a smaller business to diversify his investment in the form of the total beta or in the form of a combination of the standard and the total beta (Balz and Bordemann, 2007, pp. 737; Kniest, 2010, pp. 303), the modification of the Capital Asset Pricing Model by integrating a size premium to take the higher risk of smaller businesses into consideration (Schulz, 2009, pp. 135; Baetge, Schulz and Klönne, 2010, pp. 47) or to raise the market risk premium as a result of the reduced leverage of the owner of a smaller business and/or as a result of the higher cost of equity (Knoll, 2010, pp. 365; Gleißner and Knoll, 2011, pp. 2283). The justification of all these efforts is said to be found in the facts that different sizes of businesses lead to different growth rates and as a result of that regularly to higher risks for smaller business, that smaller businesses usually show a poorer cost structure, that the management of smaller businesses is less professional and effective, that smaller businesses face a poorer diversification of products and markets and that larger businesses often diversify by playing on several markets and/or industries (Pratt, 2001, p. 242; Damodaran, 2010, pp. 105; Wagner, 2005, pp. 10).

The finding that smaller businesses sell at higher multiples than larger businesses leads to the conclusion that the transaction prices and as a result of that also the transaction multiples generated for smaller businesses reflect a larger number of effects than there are reflected for larger businesses (in the US it is also believed that smaller companies in most industries tend to sell at lower multiples of most financial variables than larger companies; see for example Pratt, 2001, p. 243). While the multiples of larger businesses reflect especially financial effects covered in the cash flow, the multiples of smaller businesses also reflect non-financial factors. This empirical evidence leads to the further conclusions: The (fair) values calculated in accordance with the nowadays used valuation methods provide a far poorer validity for smaller businesses than for larger businesses, the size of the business has to be taken into consideration absolutely by choosing the comparables and the target and the comparables have to belong at least to the same size class.

4.3. The capability for improvement of the transaction multiples through a combination of industry and size classification

On the basis of the presented empirical evidence that either the industry classified and the size classified calculation of the transaction multiples it is now given an empirical evidence whether a combination of the two classification criteria leads to a further improvement of the quality of the transaction multiples.

Table 3: Transaction multiples according to the combination of industry and size classification

DEV/Turnover (operating)																				
Region / Industry	Small Sized Enterprises					Medium Sized Enterprises					Large Sized Enterprises					Aggregate				
	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v	n	Q_1	Q_2	Q_3	v
Central																				
Banking, Insurance & Financial Services	73	6,31	16,82	86,00	10,17	35	6,31	15,44	42,47	1,21	30	1,16	2,06	6,56	2,48	138	2,93	9,99	46,73	**12,28**
Chemicals, Petroleum, Rubber & Plastic	30	18,38	229,45	259,98	2,95	13	1,29	2,46	5,33	1,57	68	1,02	4,93	66,33	1,42	111	1,49	10,33	126,54	**4,63**
Computer, IT and Internet services	92	2,32	14,20	84,15	2,14	76	0,94	2,27	35,39	2,49	65	0,66	1,81	2,39	0,97	233	1,11	2,48	22,07	**3,08**
Industrial, Electric & Electronic Machinery	80	3,41	14,05	59,79	2,21	77	1,18	2,95	19,44	2,09	212	0,62	1,32	2,62	3,90	369	0,84	2,02	7,31	**3,83**
Personal, Leisure & Business Services	150	10,23	38,32	90,78	3,62	71	1,70	6,02	35,57	1,93	76	0,70	1,30	3,38	1,47	297	1,64	11,52	45,49	**5,00**
Retailing / Wholesaling	23	1,98	5,57	82,04	3,27	29	1,90	35,72	37,55	0,75	101	0,38	0,66	2,40	2,19	153	0,44	0,99	23,37	**8,69**
Aggregate	**448**	**4,21**	**20,41**	**90,78**	**9,48**	**301**	**1,36**	**4,65**	**36,90**	**2,03**	**552**	**0,58**	**1,32**	**3,03**	**2,96**	**1.301**	**1,02**	**3,40**	**34,17**	**15,48**
West																				
Banking, Insurance & Financial Services	119	41,18	98,54	682,61	4,59	44	10,57	22,56	205,36	2,36	63	8,99	11,25	13,11	1,95	226	11,02	39,13	325,51	**6,39**
Chemicals, Petroleum, Rubber & Plastic	43	2,31	42,41	622,04	2,40	74	1,58	23,09	187,32	1,35	150	1,17	2,72	16,87	2,09	267	1,27	8,41	45,11	**5,38**
Computer, IT and Internet services	275	1,87	5,75	57,67	3,97	179	0,94	2,48	9,20	2,61	334	0,70	1,46	3,18	1,89	788	0,99	2,17	7,36	**6,29**
Industrial, Electric & Electronic Machinery	130	4,19	11,87	77,44	4,47	148	0,95	2,99	26,37	1,90	293	0,51	1,32	2,62	2,26	571	0,67	2,10	11,60	**8,75**
Personal, Leisure & Business Services	232	2,81	18,65	73,64	15,04	221	1,41	6,34	33,51	2,08	464	0,45	1,52	17,03	2,39	916	0,75	3,50	33,19	**5,94**
Retailing / Wholesaling	142	4,14	28,36	155,75	3,16	162	1,08	3,59	46,60	11,57	357	0,48	1,02	11,05	2,46	661	0,67	2,13	32,34	**14,98**
Aggregate	**940**	**2,81**	**17,04**	**123,81**	**12,93**	**828**	**1,18**	**4,09**	**41,28**	**18,62**	**1.661**	**0,55**	**1,46**	**6,94**	**2,87**	**3.429**	**0,85**	**3,01**	**27,91**	**24,59**
South																				
Banking, Insurance & Financial Services	229	52,20	76,45	466,31	2,99	59	5,68	10,68	20,69	2,66	114	2,85	20,27	125,05	1,33	402	12,22	70,08	324,31	**3,93**
Chemicals, Petroleum, Rubber & Plastic	43	3,55	13,06	35,51	5,30	29	0,99	3,12	7,97	2,16	231	1,24	4,19	14,11	1,31	303	1,38	4,19	16,41	**10,25**
Computer, IT and Internet services	168	2,10	11,63	54,96	4,67	98	1,25	5,69	70,80	1,33	125	1,09	1,93	4,15	1,52	391	1,33	4,02	28,43	**5,30**
Industrial, Electric & Electronic Machinery	133	7,73	40,41	141,60	4,68	126	1,03	2,50	22,31	2,74	346	1,25	3,74	32,02	2,25	605	1,35	6,20	35,00	**7,73**
Personal, Leisure & Business Services	241	2,80	26,35	132,72	4,25	128	0,92	2,76	27,61	2,13	397	1,78	9,97	19,36	3,62	766	1,68	10,82	31,26	**6,80**
Retailing / Wholesaling	211	4,26	147,13	403,20	8,44	130	0,61	1,46	5,76	3,47	424	1,58	2,80	6,05	1,73	765	1,49	3,43	20,95	**15,74**
Aggregate	**1.025**	**5,02**	**47,50**	**239,54**	**6,08**	**570**	**0,93**	**3,21**	**23,74**	**2,60**	**1.637**	**1,49**	**3,76**	**16,98**	**2,99**	**3.232**	**1,64**	**7,15**	**39,53**	**10,24**
North																				
Banking, Insurance & Financial Services	245	8,54	44,73	153,69	10,46	39	4,46	11,76	27,00	1,87	37	3,22	4,97	10,74	0,71	321	5,97	26,99	125,01	**11,84**
Chemicals, Petroleum, Rubber & Plastic	44	15,86	67,96	195,65	1,95	16	8,00	11,62	40,35	1,19	26	1,48	2,48	4,37	1,77	86	2,63	13,65	70,67	**2,65**
Computer, IT and Internet services	497	2,33	9,17	40,16	3,45	159	1,13	3,42	13,40	2,20	161	0,44	1,14	2,75	7,52	817	1,28	4,47	22,12	**4,05**
Industrial, Electric & Electronic Machinery	411	6,39	34,06	158,83	3,50	84	0,87	2,62	27,26	3,06	263	1,73	2,93	6,75	1,79	758	2,32	7,98	51,09	**4,59**
Personal, Leisure & Business Services	697	4,48	22,12	92,48	5,05	219	1,02	5,32	15,84	7,13	133	0,85	1,98	13,36	1,46	1.049	2,29	12,45	50,56	**5,85**
Retailing / Wholesaling	288	2,94	35,42	170,42	4,08	125	0,90	11,61	43,77	1,31	207	0,72	2,27	26,61	1,99	620	1,08	14,81	73,71	**6,04**
Aggregate	**2.182**	**4,17**	**22,67**	**103,20**	**8,80**	**642**	**1,08**	**5,68**	**24,08**	**9,25**	**827**	**0,91**	**2,47**	**7,24**	**3,83**	**3.651**	**1,91**	**9,45**	**51,12**	**11,02**
Central-East																				
Banking, Insurance & Financial Services	130	3,58	14,53	104,12	7,04	40	2,67	4,22	7,67	2,46	27	1,52	2,89	3,62	0,50	197	2,77	5,45	35,04	**8,49**
Chemicals, Petroleum, Rubber & Plastic	52	1,40	4,35	17,88	2,27	58	0,58	0,70	1,61	2,67	69	0,38	0,78	1,43	1,39	179	0,57	1,11	3,03	**3,04**
Computer, IT and Internet services	191	1,08	2,90	11,10	4,58	68	0,20	1,18	1,80	1,11	43	0,93	1,67	2,64	0,69	302	0,92	1,95	4,54	**5,71**
Industrial, Electric & Electronic Machinery	74	0,72	2,97	38,15	2,12	68	0,61	0,83	1,27	2,07	30	0,62	0,93	1,60	0,63	172	0,61	1,05	2,80	**3,35**
Personal, Leisure & Business Services	200	0,78	2,05	7,93	3,08	60	0,42	0,71	1,33	1,22	46	0,58	1,35	1,77	1,05	306	0,62	1,46	4,26	**3,78**
Retailing / Wholesaling	194	0,58	2,32	5,99	3,37	148	0,34	1,05	2,62	2,16	223	0,43	0,79	1,27	1,25	565	0,42	0,92	2,35	**4,96**
Aggregate	**841**	**0,94**	**3,24**	**15,47**	**10,33**	**442**	**0,51**	**0,99**	**2,33**	**3,94**	**438**	**0,49**	**0,89**	**1,69**	**1,11**	**1.721**	**0,60**	**1,46**	**4,38**	**14,22**
South-East																				
Banking, Insurance & Financial Services	101	6,26	26,38	279,47	2,94	26	2,89	19,38	50,30	0,82	60	0,00	0,01	0,67	2,48	187	0,02	6,35	50,73	**4,08**
Chemicals, Petroleum, Rubber & Plastic	51	1,21	2,46	8,36	2,85	21	0,44	0,72	1,45	1,96	73	0,30	0,49	1,95	1,25	145	0,38	1,13	2,89	**4,42**
Computer, IT and Internet services	40	1,97	4,00	24,99	4,41	13	0,47	1,69	1,96	0,93	31	0,48	1,24	2,06	1,01	84	0,90	1,97	5,67	**6,30**
Industrial, Electric & Electronic Machinery	104	0,93	2,97	9,66	2,98	35	0,33	0,93	1,71	1,79	20	0,79	1,11	1,61	0,99	159	0,71	1,63	5,22	**3,72**
Personal, Leisure & Business Services	146	0,97	3,23	10,15	11,95	35	0,75	1,80	8,10	0,93	33	0,85	1,43	2,50	1,09	214	0,87	2,50	7,00	**14,48**
Retailing / Wholesaling	192	0,71	1,79	7,47	4,87	54	0,34	0,70	1,43	2,59	168	0,37	0,77	1,52	4,17	414	0,46	1,09	2,75	**7,20**
Aggregate	**634**	**0,96**	**3,41**	**19,16**	**20,54**	**184**	**0,43**	**1,08**	**3,90**	**2,09**	**385**	**0,30**	**0,74**	**1,52**	**3,23**	**1.203**	**0,50**	**1,52**	**5,93**	**28,28**
East																				
Banking, Insurance & Financial Services	89	6,74	74,16	410,19	2,40	72	1,06	1,45	24,50	1,69	20	0,75	1,69	2,21	0,91	181	1,27	9,70	152,29	**3,18**
Chemicals, Petroleum, Rubber & Plastic	25	2,01	8,48	57,54	3,47	36	0,34	0,53	0,88	1,48	158	0,50	1,22	4,27	1,27	219	0,50	1,19	4,66	**10,29**
Computer, IT and Internet services	33	1,53	5,05	15,17	3,77	12	1,37	2,16	2,78	1,52	46	1,40	1,89	2,55	1,42	91	1,41	2,19	5,06	**6,28**
Industrial, Electric & Electronic Machinery	56	0,40	1,14	2,75	2,19	44	0,41	0,87	2,08	2,72	68	0,42	0,65	1,66	1,99	168	0,42	0,81	1,99	**2,66**
Personal, Leisure & Business Services	217	0,54	3,86	32,03	3,90	65	0,65	2,16	5,21	1,41	132	0,50	0,86	1,23	1,91	414	0,54	1,28	7,68	**5,37**
Retailing / Wholesaling	215	0,43	2,43	27,91	3,85	75	0,37	0,80	3,05	2,61	291	0,62	1,95	7,18	1,78	581	0,48	1,89	8,75	**6,09**
Aggregate	**635**	**0,64**	**4,18**	**40,00**	**3,99**	**304**	**0,50**	**1,18**	**3,78**	**2,83**	**715**	**0,54**	**1,26**	**4,42**	**2,02**	**1.654**	**0,54**	**1,57**	**8,12**	**6,21**
Europe aggregate																				
Banking, Insurance & Financial Services	986	10,36	66,56	394,24	13,13	315	2,48	10,68	39,25	3,02	351	1,33	3,77	13,47	2,23	1.652	3,78	21,48	165,64	**17,00**
Chemicals, Petroleum, Rubber & Plastic	288	2,14	11,85	67,72	4,47	247	0,63	1,62	12,52	2,34	775	0,65	2,10	8,28	2,45	1.310	0,76	2,54	14,46	**8,16**
Computer, IT and Internet services	1.296	1,89	7,33	36,21	4,36	605	0,96	2,29	11,14	2,36	805	0,73	1,49	2,92	8,73	2.706	1,12	2,85	14,00	**5,71**
Industrial, Electric & Electronic Machinery	988	2,59	14,83	100,11	5,20	582	0,75	1,74	11,60	3,35	1.232	0,78	1,88	5,83	2,81	2.802	0,98	2,89	23,89	**8,09**
Personal, Leisure & Business Services	1.882	2,03	12,80	72,83	28,11	799	0,90	3,64	19,36	9,01	1.281	0,69	1,91	13,53	3,31	3.962	1,03	4,80	31,96	**38,62**
Retailing / Wholesaling	1.265	0,96	7,12	117,37	6,97	723	0,57	1,71	17,32	22,96	1.771	0,56	1,42	5,11	3,18	3.759	0,65	2,06	16,79	**11,65**
Aggregate	**6.705**	**2,10**	**13,48**	**93,55**	**30,06**	**3.271**	**0,81**	**2,59**	**18,23**	**24,02**	**6.215**	**0,67**	**1,73**	**6,40**	**3,47**	**16.191**	**0,97**	**3,51**	**26,46**	**46,26**

Table 3 again shows (solely for the DEV/Turnover-Multiple) on the one hand (in the different columns) either the three specified size classes and in addition aggregate and on the other hand (in the different lines) the six specified industries and in addition aggregate the number of the regarded transactions (n), the first (Q1), second (Q2, median) and third (Q3) quartile and the variation coefficient (v). The variation coefficient again represents an indicator for the quality, the representativeness, the homogenity and the reliability of the calculated multiples.

The analysis shows that the combination of the industry-classification and the size classification can in most cases improve the quality either of the solely industry classification and of the solely size classification. The dark-shaded areas show the improvement of both classification criteria, the light shaded areas show the improvement of one of the two previous classification criteria. Transaction multiples that are based on either an industry classification and on a size classification in combination therefore are higher in quality, representativeness and homogeneity and more reliable.

There is empirical evidence found that both the industry classification and the size classification have to be used in combination as (primary) selection criteria for the comparables.

5. Conclusion and Further Research

The presented analysis gives empirical evidence on the impact of the selection criteria industry and size of the business on the quality of the generated transaction multiples. The analysis is carried out for all European countries that deliver a statistically sufficient number of transaction data. The analysis shows that the industry classification can improve the quality of the multiples. It also shows that the multiples depend on the size of the transacted business which means that the size is also an important classification criteria. Finally it is given empirical evidence that the combined classification of industry and size leads to the best multiples.

Further research has to be done especially on the impact of further selection criteria on the peer group both solely and on their dependencies. This should give the appraisers a set of factors to be considered when choosing the peers and furthermore a calculation formula to assess the fit of the several comparables in question.

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Economics of Craft Businesses in the Republic of Croatia

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Abstract

The paper deals with the issue of business economics in craft businesses and the poor knowledge level on craft business's internal economics by craft owners and craft employees in the Republic of Croatia. It is assumed that the owner of a craft business is an entrepreneur who manages the business venture and that a craft business is a small company. The authors' main hypothesis is that craft businesses that sell more different trade items (products, services and/or goods) do not know the economics of internal operations and the profitability of individual business segments, the profitability of different groups of trade items or the profitability of each individual trade item. The authors believe that there are two reasons why this is so: poor knowledge/nonexistence of control of indirect costs and financial model which evaluates different items (products, services and/or goods). The second raises a question if there is a financial model which solves this problem?

The second part of this paper deals with the issue whether the owners/managers of craft businesses (craftsman) apply the know-how and skills from strategic management or they solely make decisions on operational basis. The authors explore whether craftsman consider the information about internal economics of their craft businesses as important for further business decisions? This paper is based on a tested statistical sample of craft businesses in three regions in the Republic of Croatia: eastern Croatia, central Croatia and southern Croatia. The authors argue the impact of poor knowledge of crucial information which is necessary for business decision making on craft business's activity. In addition, the paper explains the causes of this poor knowledge level and gives a conclusion as a recommendation of how the authors consider it necessary to solve this problem.

Keywords

Internal economics of the business, craft business, strategic management

1. Introduction

The number of active craft businesses in the Republic of Croatia in December 2011 was 86.424, which represents 44,2% of totally active business entities (corporations and crafts) and contributes to around 14,5% of total employment in the Republic of Croatia. 93,8% of all active craft businesses are active during the whole calendar year while the rest crafts are engaged in a seasonal business. The main business activity performed by the greatest number of active crafts is intellectual and other services (some 34,4% of all active crafts), followed by catering and tourism (17,3%), trade and commerce (16,2%) and production (11,2%). Around 68% of totally active craft businesses are owned by males.

The number of total business entities in the Republic of Croatia was constantly growing until calendar year 2008 driven mostly by an increase in number of registered corporations while the number of totally active crafts has been constantly falling since 2004. Despite a falling number of active craft businesses, the total number of persons employed in crafts has not changed significantly until 2008, when the number of persons employed in crafts started its sharp downward trend up to the latest available data (December 2011). The sharp decline of persons employed in crafts during the mentioned period amounted 21,5%. During the same period a number of active crafts fell by 14,2%. Crafts, together with a part of other business entities of different legal form (e.g. corporations) belong to a category of "small entrepreneurs". Small entrepreneurs represent more than 98% of total number of business entities in the Republic of Croatia and contribute 33,3% to country's overall GDP. Additionally, crafts represent the simplest way to start an own business venture and are very often the first step of many individuals to enter the world of independent entrepreneurial activity.

The basic hypothesis of this paper is that the largest number of active craft businesses sell two or more different trade items (products, services and/or goods) and that the majority of craft owners and craft employees (who are decision makers) do not know the economics of internal operations and the profitability of individual business segments, the profitability of different groups of trade items or the profitability of each individual trade item. The authors believe that there are two main reasons why this is so: poor knowledge/nonexistence of control of indirect costs and applied financial model which evaluates different trade items (products, services and/or goods). This hypothesis is supported by the fact that the majority of craft businesses in the Republic of Croatia are income taxpayers and that they use single-entry accounting system (craft accounting). In compliance with the mentioned fact, the accounting phrases and terms used in craft accounting are not synonymous with those that are used in double-entry accounting system (corporate accounting) and the terms such as receipts and disbursements have different meaning for those two types of entities. Craft accounting is not familiar with the terms revenues and expenditures (exception are crafts who are profit taxpayers but its number in the population of total active crafts is negligible). On the other side, a detailed cost value calculation implies an exact differentiation between receipts and revenues as well as disbursements and expenditures and should be based on directions prescribed by IAS 2 – *Inventories* -. Every craftsman (owner/manager of craft a business) should additionally register costs of each trade item as prescribed by IAS 2 – *Inventories* – and calculate the cost value of each trade item by using cost accounting methods. In real life, there is a certain degree of discrepancy related to this specific situation since craft businesses (income taxpayers) neither use the double-entry accounting system, nor are familiar with the term "cost", nor do they keep track of all incurred costs. Detailed and complete cost records are crucial for a precise cost value calculation. Furthermore, craft business's accounting documentation prescribed by law aims basically to determine the tax base and it is not a good information basis for business decision making. Another crucial problem related to single-entry accounting system is that receivables are not receipts as long as they are not collected while payables are not disbursements as long as they are not settled. The resources which were acquired by a craft business for its regular business activity are not considered as a disbursement as long as they are not settled while at the same time, those resources can regularly be used in business

operations or even create an added value which furthermore can be recorded as a receipt. Here we face a problem when calculating the profitability of a craft business. A craft business can record high receipts by controlling the revenue collection while at the same time it can stop paying its suppliers and not register the disbursements. This can lead to a positive (overvalued) difference between receipts and disbursements. Therefore, the system of single-entry accounting primarily aims at income tax collection and does not provide categorized data which are necessary for business profitability calculation.

To sum up, the single-entry accounting system cannot provide the information which is crucial for profitability calculation of each individual trade item. Therefore, we raise another reasonable question: which financial model and accounting system can provide such data? It is undoubtedly the double-entry accounting system which clearly differentiates between costs, expenditures, revenues, assets, capital and payables. Even though, the first two authors proved in their other research paper „So fit model and measurement methods of overhead costs" that the application of inventory calculation method for purposes of profitability calculation can incorrectly evaluate the profitability of trade items, they do believe that this is a problem of each individual calculation method rather than the problem of double-entry accounting system itself. We point out that double-entry accounting system provides much better information needed to calculate the cost value and the profitability of each trade item. The main reason for this is that double-entry accounting system categorizes the accounting data in a different way.

Due to all mentioned information is it obvious that by using only the accounting data from single-entry accounting system, the profitability of trade items cannot be precisely evaluated. In addition, we also raise a question whether craft businesses are interested in information related to the internal economics of their businesses and if their business entity is managed in a strategic or in an operational way?

2. Methodology

53 examinees were responding on two groups of survey questions (totally twenty questions). The first group of questions was related to the knowledge level of business's internal economics while the other group referred to the appliance of strategic management know-how. All respondents were craft owners or craft managers and came from three Croatian regions: eastern Croatia, central Croatia and southern Croatia.

The responses that were offered in the survey were categorical variables. The respondents were asked if they can give a precisely enough confirmation to specific questions. Due to the fact that some of the survey questions have been uncomfortable to some respondents, additional face-to-face interviewing and detailed explanation were undertaken during the data collection (e.g. survey question about the contribution of three major trade items to the overall sales were considered by respondents as a business secret while the authors were more interested in categorical responses such as I know – I do not know; in order to explore whether the respondent really knew this contribution, he/she should have been able to specify a very precise value/number/percentage). Furthermore, specific survey questions have been additionally explained as they have been evoking a sort of psychological barrier by a number of respondents when providing answers to those questions. Those were the questions about the trade item calculations and whether they include all incurred costs. Firstly, the responses were affirmative and defensive but after an additional explanation that those survey questions refer to all costs but not only to purchase costs of goods or product components the responses were mostly negative. Such situations demanded additional effort during the process of data collection since the authors had to be present and give additional explanations

while the respondents were filling out the survey. On the other side, such an approach has surely increased the quality of collected data.

3. Research Results

Out of all respondents only 3,77% are 20 years old or younger, 9,43% are 21-30 years old, 30,19% are 31-40 years old, 33,26% 41-50 years old, 20,75 % are 51-60 years old, 1,79% are 61 years old or older.

75,47% of all respondents were able to name craft's three most sold trade items during the last business year while 24,53% did not have such information. However, even 77,36% did not know the contribution of these three major trade items to the overall sales. The selling prices (in accordance with crafts official price list) of three major trade items could not be specified by 16,98% of surveyed respondents. The costs value (with all costs included) of three major trade items was not known by 88,68% respondents.

94,34% of all surveyed craft businesses use fixed assets which is not registered on craft's fixed asset list in their regular business operations.

60,38% of surveyed crafts do not have any kind of written cost calculation for their trade items at the start of a new business cycle. 20,75% of crafts do have a written cost calculation for some of their trade items while only 18,87% of crafts do have a written cost calculation for all of their trade items. 24,53% of all respondents stated that the cost calculations are done by craft owners.

The costs value of trade items at the end of the last business cycle is not known by 62,26% of all respondents while some 20,75% said that they know the cost value for some of their trade items.

49,06% of all respondents claimed that they have never consulted an expert business consultant for questions regarding the internal economics of their craft businesses while some 47,37% stated that they have consulted an expert business consultant more than a year ago.

94,34% of surveyed craft businesses do not have a business plan for a period longer than three years. Some 67,92% haven't even thought about its future business plans for a period longer than three years. 77,36% were not able to specificity two major business goals for a period longer than three years. 98,11% of respondents said that they do not have a written business vision.

More than 94% of surveyed craft businesses are income tax payers while the rest craft businesses are profit taxpayers.

The following questions were answered by choosing one option on a scale from 1 to 5 *(5 - highly important, 4 - important, 3 – intermediate, 2 - less important and 1 - not important).* When asked how important it is to know the cost value of each trade item (all costs included) at the end of a business cycle, 39,62% have answered that it is highly important, 39,62% said that it is important, 7,55% consider it intermediate while the others consider it less important or not important.

When asked how important would it be for them if an expert consultant would calculate the real cost value of their trade items at the beginning of a business cycle 32,08% responded that it would be highly important, 45,28% considered it important, 15,09% said it is intermediate while others claimed that it is less important or not important.

When asked how important would it be for them if an expert consultant would calculate the real cost value of their trade items at the end of the business cycle 39,62% responded that it would be highly important, 41,51% claimed that it is important, 9,43% considered it intermediate while others said that it is less important or not important.

When asked how important would it be for them to use expert business consultancy services on a permanently basis, 7,55% said that it is highly important, 32,08% said that it is important, 20,75% consider it intermediate while the rest respondents said that it is less important or not important.

When asked how important do they consider to have a written business plan for their craft business, only 7,55% said that it is highly important, 33,96 said that it is important, 20,75% consider it intermediate while the rest respondents said that it is less important or not important.

4. Interpretation of the Research Results

The majority of surveyed craft owners are between 31 - 40 and 41 – 50 years old. These results were expected since the population in this age tends more to self-employment and is rather employed than unemployed. The reason for self-employment in this particular age is explored by researchers in the field of entrepreneurial psychology. For purposes of this paper we will just point out few of such reasons as family, work experience, education and need for self-realization.

By responding to survey questions about the three major trade items, the contribution to the overall sales, the selling prices and cost values, the respondents were providing us with the information about their knowledge level of sales economics and whether they analyze their major trade items or not. More than 75% of surveyed respondents were able to name three major trade items during the last business year while ¼of them was not able to provide such information. However, more than 77% of all respondents were neither able to estimate the contribution the three major trade items to the overall sales nor did they have such information in their data bases. This proves that the majority of craft owners/managers are not analyzing sales and that their business decisions making is not based on such analyses. Furthermore, the research results indicate that business decisions are being made more intuitively rather than being based on quality information and analyses from sales metrics. This is supported by the fact that more than 88% of respondents do not know and do not have any information about the cost value (all costs included) of three major trade items. The mentioned research results represent the essence of this paper. Since the respondents do not know the cost value and the contribution of the three major trade items to the overall sales it makes us hard to believe that they have such information for all other (less important)trade items.

Fixed assets that are in craft owner's private ownership (and that are not registered on craft's fixed asset list) are used in craft's regular business operations by more than 95% of surveyed crafts. The costs that refer to the usage of not registered fixed assets are not calculated and taken into consideration when evaluating the cost values. This shows that the disposed accounting data solely, is not providing a complete basis for precise profitability calculations.

More than 60% of respondents claimed that they do not have written cost calculations for all trade items. When they were asked to specify the cost calculations for three major trade items, the response that they do not have it was 28% higher. It means that, when the respondents were asked to provide a detailed cost value, the response of not having such information was much higher as when they were asked a similar question in a more general way. The reason for such a difference in responses is probably of psychological nature. The fact that more than 62% of respondents do not know the cost value of each trade item at the end of a business cycle could be interpreted similarly.

When asked if it would be important for them to know the cost value of their trade items at the beginning of a business cycle more than 77% responded that it would be highly important or important. When asked if it would be important for them to know the cost value of their trade items at the end of a business cycle more than 81%responded that it would be highly important or important. This means that around 80% of respondents consider it important to know the economics of their businesses in terms of past and future costs while around 88% of all respondents neither know nor have a clear information about the real cost value of their three major trade items.

The following questions aimed to explore whether the respondents are familiar with strategic management for small and medium sized enterprises and if they apply this know-how when managing their own craft business. Almost ½ of respondents have never consulted a business consultant while some¼ did it more than one year ago. This means that only ¼ of surveyed craft businesses use expert business consulting services on a permanently basis.

More than 94% of surveyed craft businesses do not have a business plan for a period longer than three years while more than 67% haven't even thought about its future business plans for a period longer than three years. In addition, more than 77% were not able to specificity two major business goals for a period longer than three years while more than 98% of respondents said that they do not have a written business vision. These responses indicate that the majority of respondents do not apply strategic management know-how and skills. This leads us to the conclusion that they manage their craft businesses solely on an operational basis.

When asked if it would be important for them to permanently use business consulting services and to have a written business plan, nearly 40% said that it is highly important or important. It all indicates that craft owners are not fully aware of the importance of management know-how which is needed for successful business managing and decision making.

5. Conclusion

In the introduction we have argued why the single-entry accounting system cannot provide a good information basis for profitability calculation. The needed accounting information should be extracted from the existing accounting documentation and categorized into specific categories as they are known in double-entry accounting system (e.g. costs, assets and revenues). Such processes call for specific know-how and skills.

The gathered responses to our survey indicate that such know-how levels and its application is very low for the majority of surveyed craft owners/managers. It seems that craft owners/mangers spend much more time on solving business problems on an operational/daily basis rather than on serious economic and business deliberation.

On the other side, the gathered responses indicate that respondents are aware of the fact how important it is to know the internal business economics and that they have strong needs for this kind of knowledge. However, it seems that the majority of surveyed respondents manage their business in a way "buy cheap, sell expensively". This is the main reason why they think that it is important to know the real cost value and the profitability of trade items. Yet, their interest in other specific business know-how and crucial skills for successful business decision making is not going further beyond this point.

The fact that only ¼ of surveyed crafts have used expert business consulting services during the past year proves that business/economic know-how and expert consultancy is considered as additional and unnecessary cost. This is supported by the fact that more than 94% of surveyed crafts do not

have a written business plan, more than ⅔ do not think long termly and more than ¾ are not able to clearly specificity two major long-term business goals. Only one respondent had a written business vision and provided a clear response to the question regarding its business plans in the next couple of years.

Less than ½ of surveyed crafts consider it highly important or important to have a written business plan and to use expert business consultancy services. We can draw a clear conclusion now: the majority of craft owners/managers are interested in sales economics and business profitability but they are not interested in other important economic know-how which is crucial for successful business management.

We consider that one holistic business model needs to be developed. It should include three key entrepreneurial domains: marketing, finances and strategic management. Marketing should define the market needs and the quantity of sales needed for price calculations. Financial part of the model should be able to provide basic directions on how to calculate the business and trade items profitability. Strategic management should define the direction in which a craft business is heading and the amount of expenditure needed to achieve the set goals.

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Cultural Aspects of Decision Making On Online Purchase

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Abstract

Empirical studies and e-commerce practice have shown that even in the context of globalization customers still need to feel associated by culture with the seller or the service provider. The aim of the current paper is to identify and bring together the main cultural and psychological aspects that influence the decision making on e-purchase. Cultural adaptation has a great potential in improving the efficiency of communication with customer, thus, e-offer's localization makes positive effects on customer-seller dialogue. The results of conducted analysis show the main cultural aspects, which have to be considered when adapting e-offers to Baltic (Latvia, Lithuania) and Russian markets.

Keywords

Cultural dimensions, decision making, online purchase

1. Introduction

On the one hand, integration and globalization processes allow the companies to access the global market, while information technologies (for example, such as Internet) allow expanding products and services distribution channels. On the other hand, globalization does not mean the unification of products and services, as the consumers all over the world have significant differences in the thinking models and decision making habits due to the cultural, geopolitical etc. differences. Findings from the experiments on economic decision making process allow criticizing the predictions and decisions made based on standard theory of economics. There is a necessity to outline how to make the non-economical factors work for the success of business-consumer communication.

Behavior economists neglect the assumption of rationality and claim the huge impact of psychological factors (as for example, social preferences). Decision making processes have been studied by researchers on the field of economics, psychology, and cultural anthropology, the collaboration between the mentioned disciplines is surprisingly limited. Psychologists acquired deep knowledge on the influence of personality differences on its behavior. Anthropologists identified the cultural dimensions, which help to identify the cultural differences and their impact on perception. However, this information is barely applied to the economic and management studies. Thus, in order to initiate the fruitful communication with potential customers and expand the markets, there is a need to meet customer expectations, like so it is necessary to know the differences of economical issues' perception by individuals in different countries and/or cultures.

The aim of this paper is to identify the main cultural aspects that influence the private decision making in online purchase.

The analysis of scientific literature, comparison, synthesis methods were used to reach paper's aim. The main method of information gathering was a customer survey performed in three countries: Latvia, Lithuania, and Russia; the data were exposed to statistical and valuating analysis. The analysis gave the set of cultural aspects important for customers in decision making in the Internet.

2. Cultural Aspects of Decision-Making

Culture even in the same country may differ, but the differences between countries may be particularly pronounced. The ignorance of cultural specificities in business environment can lead to conflicts in the communication, which in turn leads to a decline in productivity (Pluke *et al.*, 2005). Thus, the concept of culture in the development of international business is quite important: culture is shared values, goals, methods, and totality of relationships. Culture can also be influenced by ethnicity, language, history and level of country's technical development. It becomes clear that the company intended to expand globally must take into account the cultural impact, it is essential to know what changes in marketing communication are needed for each culture: what are the cultural peculiarities, priorities and orientations. The knowledge about cultural peculiarities could be a considerable advantage in marketing campaigns intended to impact the decisions of customers. Like so, this knowledge should be properly organized and adapted to analytical work with it. Thus, the cultural aspects can be organized according to certain categories – dimensions (Marcus, 2004, Soyoung *et al.*, 2006).

2.1. Hofstede's cultural dimensions

World cultures have various sets of social Behavior and interaction; it has led anthropologists and researchers to develop the models of cultures that would allow to describe the existing cultural

differences. One of the most cited anthropologists is Geert Hofstede, who conducted a cultural study in 1970-80 at IBM. His study included 72 national subsidiaries, 38 occupations, 20 languages, 116000 individuals. Based on this study Hofstede identified five cultural dimensions (Hofstede, 1980; Smith *et al.*, 2001):

1) Power distance: the extent to which people accept a high or low power distance in social hierarchy. Power distance index corresponds to the scale of formal power recognition. As the power distance indicates the extent to which less powerful members of the public recognize the uneven distribution of power, and Hofstede claims that countries with high power distance have a centralized political structure and hierarchy developed with considerable differences in status, while countries with low power distance often focus on the ordinary people and the differences in status are not so strong.
2) Individualism vs. collectivism: orientation to the achievements of individual or team. In collectivism the interests of the team have more value than personal; it is the individual's loyalty to the group (Dinev, 2006). In societies with high individualism, the individuals are independent from each other and have their own personal goals. Individualistic culture put much value upon the time, freedom, challenge, personal material reward. Collectivistic culture values the learning, physical conditions, skills.
3) Masculinity vs. femininity: the extent to which the culture separates or not the traditional gender roles. In masculinity's cultures gender roles are more separated than in femininity. Hofstede focuses on traditional gender roles: the masculinity manifests through persistence, competitiveness, hardness, and the femininity – through the home-orientation, children, people, and gentleness.
4) Uncertainty avoidance: the extent to which culture accepts uncertainty. Uncertainty avoidance index assesses the importance of rules and standards and shows how people feel in uncertain situations. High uncertainty avoidance society's individuals are seeking to reduce personal risk, are more opposed to innovation, and respect the rules. Cultures choose different ways of uncertainty avoiding through the various rituals, there are different approaches to the formalities, punctuality, law, religion, social requirements, and ambiguity toleration.
5) Long-term orientation: orientation to the Confucian mindset, which emphasizes the patience. In society with long-term orientation the stability, prudence, long-term agreements have an exceptional value. Long-term orientation is important for Asian countries, which focus on the virtuous Behavior, and the Western countries focus on faith and the search for truth.
6) Indulgence vs. restraint: indulgence stands for a society that allows relatively free gratification of basic and natural human drives related to enjoying life and having fun. Restraint stands for a society that suppresses gratification of needs and regulates it by means of strict social norms[1].

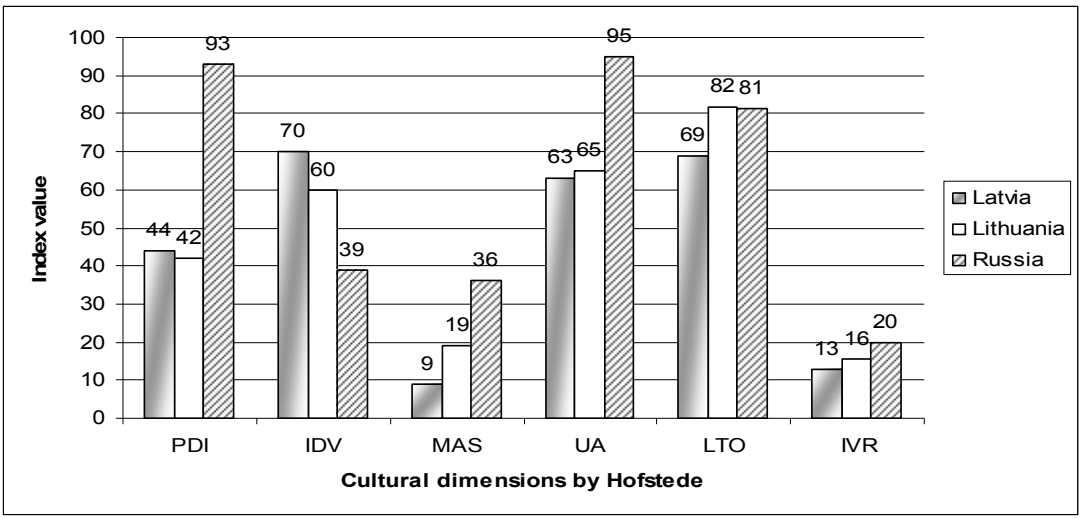
Hofstede explains that cultural orientations are deeply infixed in cultures throughout the centuries, so the modern technology can not eliminate it. These dimensions are widely used in business studies on assessment of gender roles in various business fields, especially in shaping the strategies of advertising, in research of purchase motives and product use, etc. (Baack & Singh, 2007). Whereas, the objects of this research are Russia and two Baltic countries – Latvia and Lithuania, the comparison of Hofstede's culture indexes for mentioned countries is presented on the Fig. 1.

If we look firstly on the indexes of Baltic countries, we can see that three from the six dimensions (power distance, uncertainty avoidance, indulgence vs. restrain) have quite similar values of index. Both countries are mild power distant, tended to avoid the uncertainty, and are quite restricted in gratification. However, there are considerable differences in the indexes of the rest cultural

[1] Description of this dimension is taken from http://geert-hofstede.com/dimensions.html

dimensions: masculinity (difference between indexes is about 53%), long term orientation (16%), individualism (14%). These indexes show that both countries have a low "masculinity" level and are tended to consider genders equally.

Figure 1: Culture indexes by Hofstede for Latvia, Lithuania and Russia



Considering the difference between index values Latvians seams to be more tolerant to the genders' differences than Lithuanians. Both countries are long-term oriented, but still Lithuanians are more minded for long-term relations in business and can be ready to dedicate more time for reaching the goal than Latvians. Both countries are highly individualistic, but this feature is a bit more typical to Latvians than to Lithuanians. The indexes for Russia differ significantly from Baltic States on four dimensions: power distance, individualism, masculinity, and uncertainty avoidance. Like so, Russia is considered to be extremely uncertainty avoiding, power oriented and tolerant to the status differences. Moreover, Russia is more oriented to collectivism than Baltic countries do, and tended to separate gender roles in social life, which is not the case in Latvia neither in Lithuania. Interesting is the long-term orientation index, which is quite the same for Russia and Lithuania, but less expressed for Latvia. Thus, according to analyzed Hofstede's indexes at first glance such general intuitive conclusion for these three countries could be drawn: the most strict, structured and hard in changes seems to be Russian culture, and the most relaxed, individualistic, dynamic and open to the changes – Latvian, when Lithuanian culture would be in-between the two. However, the Hofstede's cultural dimensions are not the only way to analyze the culture.

2.2. Schwartz's cultural dimensions

In the Schwartz's (1994) typology seven dimensions are used to explain the cultural differences: (1) conservatism – describes the importance of the relations between groups in society, of the social balance, security, identity, and traditions; (2) intellectual autonomy – values the individuality, autonomy, creativity; (3) emotional autonomy – emphasizes the personal goals, self-gratification, and pleasure; (4) egalitarian engagement – voluntary commitment to public welfare, equality, social justice, freedom; (5) harmony – highlights the beauty, peace, harmony with nature, environment protection; (6) mastery – values the efforts to adapt the environment, defend own rights, ambitions and independence; (7) hierarchy – assesses the perception of status and hierarchy, social power and authority.

Unlike Hofstede's, the Schwartz's dimensions are intended to analyze culture in the non business environment. Schwartz has used a different method than Hofstede, more examples and newer data

(Baack & Singh, 2007). His content analysis method to evaluate the cultural adaptation is quite often used in international marketing.

Baumgartner's and Marcus' cultural dimensions
Marcus (2004) worked on cultural differences on the web and used the list summarizing the main cultural dimensions, which have been highlighted by Baumgartner (2003). According to expert survey the key cultural dimensions in the web communication were selected from the above mentioned list. On the top of the list is the context dimension, defined as the quantity of information needed in a given situation (3.73 out of possible 4 points). The second dimension is technological development (3.24 points), which is very important for interface design. Uncertainty avoidance is on the 3rd place (3.21 points), it is estimated that each interface should reduce the uncertainty and in particular on the moment of decision making on the Internet purchase, so technological development is closely linked to reduction of uncertainty. The dimensions of time perception and authority conception were assessed as less important (accordingly 3.14 and 2.86 points). Cultural dimensions were collected on the basis of the expert survey, grouped and ranged by statistical average, which shows the importance of each dimension on the web.

Thus, the different authors mentioned above proposed a dimensional approach to the analysis of cultural differences. The main similar dimensions mentioned in different models are linked to the understanding of authority (power distance, hierarchy, and authority conception), relations in the society (individualism vs. collectivism, conservatism and autonomies), context (masculinity vs. femininity, harmony, mastery), uncertainty avoidance, time perception (or long-term orientation vs. short term).

Only Hofstede's method has already been applied to Latvia, Lithuania and Russia. However, these countries were also presented in Lewis' model of world cultures.

2.3. Lewis model of world cultures

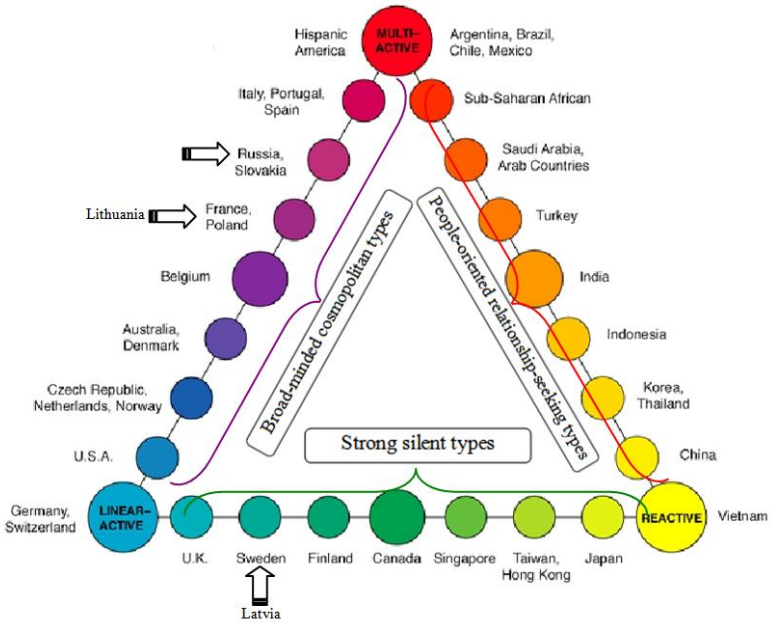
Lewis (2008) invoked a visual approach to the presentation of cultural differences between world countries. He described the culture by action-ability and Behavior of its representatives by dividing cultures between three orientations: multi-active, linear-active, and reactive. By Lewis (2008) for typically multi-active cultures the most important are: hierarchy, family, relationships, emotion, eloquence, persuasion, and loyalty. The representatives of such culture talk a lot and very emotionally, are flexible, people-oriented and are guided more by feelings, not by facts. For linear-active cultures the orientation to law, facts, deadlines, concrete results and planning is typical. Such people are polite, but direct, value the truth more than diplomacy, stick to facts, they like doing only one thing at a time, are job-oriented and plan ahead step by step. Typical representatives of reactive culture are guided by intuition, value the face-saving, they are courteous, oriented to the networking, common obligation and collective harmony. Lewis (2008) put the countries on the ribs of triangle showing cultural orientations and shows the examples of countries with typical or hybrid cultural orientation (fig. 2).

The two Baltic countries, Latvia and Lithuania, are considered by Lewis' typology as quite different ones in the cultural context. Like so, Latvia is assigned to the countries approximate to the linear action orientation, tended to be silent and calm, and relied on facts, less on intuition, but not on the emotions. Lithuania, by contraries, is considered as representative of mixed multi-active and linear-active countries, tended to be broad-minded and quite active in communication, relied on the feelings and on the facts, but not on the intuition. On the same axe Russia is placed, but more approximate to emotional multi-active countries than Lithuania – thus, by Lewis Russia and Lithuania

are considered quite similar in terms of communication activity between them and different from Latvia.

However, Latvia and Lithuania are the only countries belonging to the Baltic languages group and quite often are considered as very similar by their culture, way of thinking and perception of information. Like so, there is a question – do the companies need to adapt their marketing proposals to Latvian and Lithuanian markets separately, or maybe the same marketing strategy can be used with aim to impact decision making of individuals from these countries.

Figure 2: National cultural profiles by Lewis (2008)[2]



Of course, the markets of Baltic countries are quite small and the creation of different marketing strategies can be not cost-effective, like so the alternative possibility could be considered – to use the strategy oriented to big neighboring market – Russian market.

The examples of Baltic countries are taken with aim to find out if (1) the representatives of the countries, which are considered stereotypically as very similar, can differ in online decision making, (2) if yes – what are the differences and how these differences can be used for marketing campaign success, (3) if no – what are the aspects to be considered in common marketing planning.

3. Cultural Aspects in Online Purchase – Methodology and Results of Survey

The exploratory survey was based on the questionnaire, which proposes to the respondents from Latvia, Lithuania and Russia to agree or disagree with 23 given sentences. The sentences were formulated in a way that allows to evaluate by 7-points scale the agreement with proposed sentences (see table 1) and like so to identify the dominant cultural dimensions in perception of respondents during online purchase. This research covered answers of 189 respondents, 27 % of them reside in Latvia, 41 % – in Lithuania, and 32 % – in Russia. The response rate was 25 %. The distribution of respondents by age and their demographic profile by countries are provided on fig. 3.

[2] The basis for this picture is lent from www.crossculture.com

In this survey females were more active and young public prevailed as the survey was targeted to the online purchasers. Thus, conducted survey cannot be considered as presentable for all society, but the results can give an idea of priorities, possible similarities and differences in cultural aspect of online purchase. The sentences, which were presented to the respondents, are provided in table 1 with mean values of agreement assigned by respondents' countries (where "1" means disagreement, and "7" – full agreement), statistical analysis of data was made with SPSS package. As in 7-points scale the center value is "4", the agreement was expressed when mean values exceed 4 points, and disagreement – when mean values are less than 4.

It was considered that when mean values of dimensions are varying around the center-value ("4") and the difference from it is not statistically significant, then respondents are quite indifferent about proposed sentences of such dimensions.

Figure 3: Demographic profile of respondents

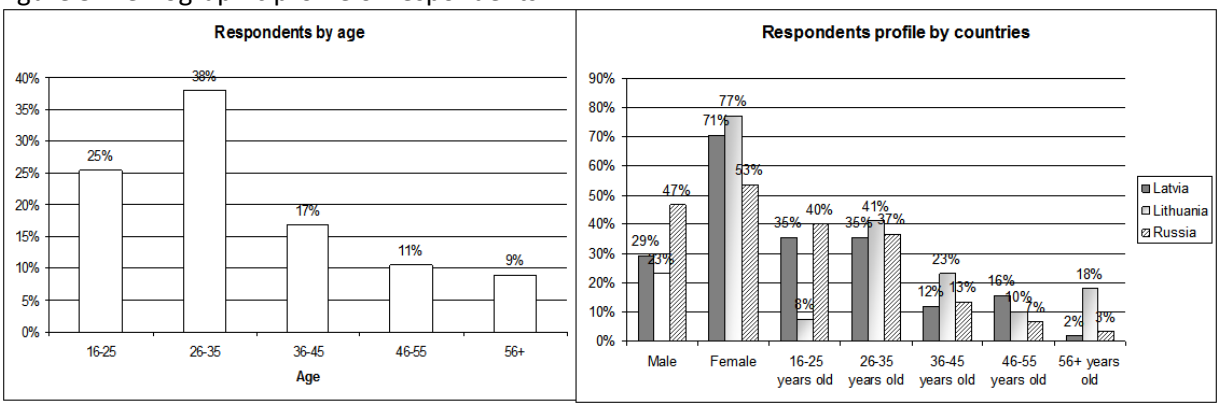


Table 1: Grouped statistics of agreement with proposed sentences

Sentences proposed for agreement/disagreement *[cultural dimension expressed by agreement with sentence]*	Country	N	Mean	Std. deviation	Std. error of mean
1. I am more interested in the online offers presented by high level manager. *[High power distance]*	LT	78	3,08	1,829	,207
	LV	51	3,53	1,554	,218
	RU	60	3,57	1,890	,244
2. I trust more the online offers from the big companies. *[High power distance]*	LT	78	5,38	1,435	,162
	LV	51	4,12	1,829	,256
	RU	60	4,70	1,825	,236
3. I trust more the companies established by Government. *[High power distance]*	LT	78	4,15	1,699	,192
	LV	51	3,47	1,666	,233
	RU	60	4,70	1,825	,236
4. I trust more the companies of local capital. *[High power distance]*	LT	78	3,82	1,421	,161
	LV	51	3,18	1,307	,183
	RU	60	3,47	2,159	,279
Understanding of authority (means of agreement with 1–4 sentences) *[High power distance]*	**LT**	**78**	**4,10**	**,930**	**,105**
	LV	**51**	**3,57**	**1,304**	**,182**
	RU	**60**	**4,03**	**1,260**	**,163**
5. When I choose the product in web shop I keep in mind its effect to the environment (e.g. bio-products, recycled or recyclable products, energy saving products, etc.). *[Collectivism]*	LT	78	4,64	1,432	,162
	LV	51	3,71	1,890	,265
	RU	60	4,03	1,794	,232
6. I prefer the online offers from companies that dedicate part of profit to the charity funds. *[Collectivism]*	LT	78	4,05	1,562	,177
	LV	51	2,88	1,505	,211
	RU	60	3,60	2,010	,260
7. The web-advertisement showing the success of group of people is more attractive than showing the success of individual. *[Collectivism]*	LT	78	4,05	1,794	,203
	LV	51	3,94	1,974	,276
	RU	60	3,47	2,236	,289

8. I trust more companies with strong collective culture. *[Collectivism]*	LT	78	4,67	1,355	,153
	LV	51	3,88	1,829	,256
	RU	60	4,67	1,753	,226
Relations in society (means of agreement with 5–8 sentences) *[Collectivism]*	**LT**	**78**	**4,35**	**1,073**	**,121**
	LV	**51**	**3,60**	**1,313**	**,183**
	RU	**60**	**3,94**	**1,409**	**,181**
9. The offers that accentuate their financial value are more attractive. *[Poor context, Masculinity]*	LT	78	5,10	1,718	,194
	LV	51	4,71	1,501	,210
	RU	60	5,10	1,591	,205
10. I prefer more the online offers, which provide facts and are not overloaded by impressive and colourful information pieces. *[Poor context, Masculinity]*	LT	78	5,67	1,296	,147
	LV	51	5,06	1,529	,214
	RU	60	6,03	1,438	,186
11. I think that stereotypical advertisement (e.g. kitchen tools advertised by women and cars – by men) in internet is not attractive anymore. *[Rich context, Femininity]*	LT	78	3,92	1,871	,212
	LV	51	4,35	1,659	,232
	RU	60	3,90	2,023	,261
12. The gender of online-consultant doesn't affect my trust. *[Rich context, Femininity]*	LT	78	5,51	1,891	,214
	LV	51	4,82	1,905	,267
	RU	60	5,57	2,110	,272
Context (means of agreement with 9–12 sentences) *[Poor context, Masculinity]*	**LT**	**78**	**4,33**	**,804**	**,091**
	LV	**51**	**4,14**	**1,126**	**,157**
	RU	**60**	**4,41**	**1,05**	**,136**
13. I am not interested in cost-attractive online offer if it is not clearly described. *[High uncertainty avoidance]*	LT	78	5,13	1,582	,179
	LV	51	5,12	1,505	,211
	RU	60	5,70	1,629	,210
14. It is very important for me to know in advance the final price of online offer. *[High uncertainty avoidance]*	LT	78	6,64	,980	,111
	LV	51	5,88	1,381	,193
	RU	60	6,67	,795	,103
15. I will not initiate the online purchase if I am not aware about all details of procedure. *[High uncertainty avoidance]*	LT	78	6,00	1,140	,129
	LV	51	5,94	,947	,133
	RU	60	6,30	,908	,117
16. I appreciate the companies providing all information about the online offer, i.e. not only positive, but also negative. *[High uncertainty avoidance]*	LT	78	6,31	1,120	,127
	LV	51	5,47	1,770	,248
	RU	60	6,30	1,197	,155
Uncertainty avoidance (means of agreement with 13–16 sentences) *[High uncertainty avoidance]*	**LT**	**78**	**6,02**	**,909**	**,103**
	LV	**51**	**5,60**	**1,046**	**,146**
	RU	**60**	**6,24**	**,798**	**,103**
17. I prefer to buy goods of the same label I trust. *[Long-term orientation]*	LT	78	5,31	1,292	,146
	LV	51	5,00	1,428	,200
	RU	60	5,77	1,370	,177
18. I prefer to find out more about company before online purchase. *[Long-term orientation]*	LT	78	5,49	1,642	,186
	LV	51	4,71	1,331	,186
	RU	60	5,57	1,466	,189
19. My decision to buy from particular company online is usually based on good relations with it and previous experience. *[Long-term orientation]*	LT	78	5,67	1,234	,140
	LV	51	4,88	1,336	,187
	RU	60	5,90	1,231	,159
20. I prefer to choose offers that foresee the long-term contract and warranties. *[Long-term orientation]*	LT	78	4,85	1,521	,172
	LV	51	4,35	1,383	,194
	RU	60	5,53	1,761	,227
Long-term orientation (means of agreement with 17–20 sentences)	**LT**	**78**	**5,32**	**1,025**	**,116**
	LV	**51**	**4,73**	**1,076**	**,150**
	RU	**60**	**5,69**	**1,028**	**,132**
21. **Feelings:** While making a decision I trust my feelings and expectations.	**LT**	**78**	**4,49**	**1,439**	**,163**
	LV	**51**	**5,24**	**1,069**	**,150**
	RU	**60**	**4,27**	**1,582**	**,204**
22. **Facts**: While making a decision I prefer to draw conclusions based on my knowledge.	**LT**	**78**	**5,92**	**1,277**	**,145**
	LV	**51**	**5,53**	**1,102**	**,154**
	RU	**60**	**6,17**	**1,107**	**,143**
23. **Intuition:** I carefully listen to my deepest feelings (intuition) before making a decision.	**LT**	**78**	**3,85**	**1,773**	**,201**
	LV	**51**	**4,94**	**1,008**	**,141**
	RU	**60**	**4,03**	**1,957**	**,253**

After one-sample t-test with significance level 0.05 such cases of mean's equality to the center of the scale ("4") were identified: for Latvia – Context dimension, for Lithuania – Understanding of authority and Intuition in online purchase, for Russia – Understanding of authority and Relations in society dimensions, as well as Feelings and Intuition in online purchase. Thus, it can be assumed that mentioned cultural dimensions and psychological aspects for e-purchasers from named countries are not pivotal. As concerns the remaining dimensions, the differences from the center are statistically significant, like so respondents are more determined and in particular show their predisposition to high uncertainty avoidance, long-term orientation and facts-based decisions.

Such short characteristics of countries cultural profiles relevant for online purchase can be given according to the survey results:
Latvian respondents could be characterized as low power distance minded in online purchase; they do not consider that e-offers presented by top-manager or guaranteed by Government and local capital are more attractive. Like so, e-offers can be successfully presented by small or medium business in the near-to-people manner. The attitude to collective values in online purchase of Latvian respondents is quite indifferent, the tendency to individualistic values can be observed, like so, Latvians do not keep in mind the possibility to be involved in charity during e-purchase and when making e-shopping decisions they are indifferent to collective culture or common society goals (such as environment protection). It shows that e-offer oriented to the Latvian market should highlight the importance of individuality of each customer and the value of offer for him/her personally. The information provided to e-customer should be clear, exhaustive and procedure of purchase – intuitive, as Latvian respondents showed high uncertainty avoidance and tendency to base decisions on their knowledge. However, the content of e-offer should be emotionally close to potential e-customer, because Latvian respondents indicated feelings and intuition being important for them in decisions on e-purchase. The long-term partnership can be more attractive than short business relations for Latvian customers.

The analysis of Pearson correlation showed the link between long-term orientation and power distance (0.671, Sig. 0.000) – respondents oriented to long-term business relations are minded to high power distance. Moreover, there is a direct correlation between long-term orientation and knowledge importance in decision making (0.525, Sig. 0.000). Like so, Latvian respondents oriented to long-term business relationship trust more facts and are seeking for solid and stable business partner. On the other hand, if customer is apt to follow his/her intuition in decision making, feelings will be important for him/her as well (0.458, Sig. 0.001).

Lithuanian respondents are indifferent to power distance in online purchase, but trust more the big companies. They are keeping in mind environment protection while choosing products and trust more companies with expressed collective values. Lithuanians accept traditional gender roles; in online purchase they are pragmatic and oriented more to the facts and knowledge than to the emotions. Like so, e-offers should include detailed factual information and show an estimated e-offer's value not only for individual, but for society as a whole. Lithuanian respondents demonstrated high uncertainty avoidance and long-term orientation in online purchase. The analysis of correlation showed that there is a link between uncertainty avoidance and knowledge (facts) role in decision making (0.533, Sig. 0.000). Thus, Lithuanians make decisions on online purchase mostly according to the collected information on e-offer and retailer; they can dedicate additional time for research for relevant information allowing better decision making.

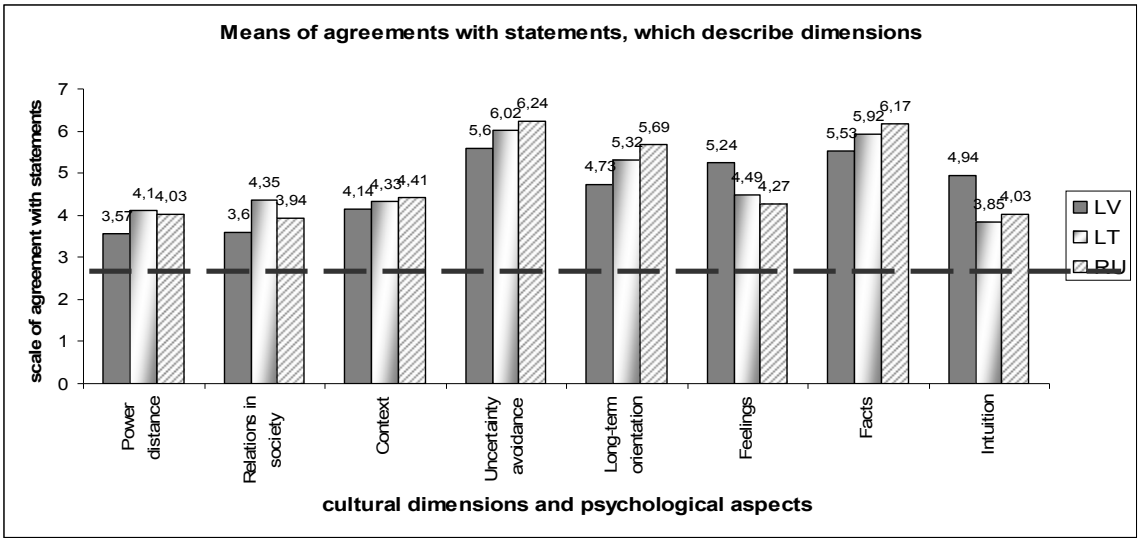
Russian respondents are inclined to traditional gender roles and information providing in poor context mode. Knowledge and available factual data impact on e-purchase decisions more than feelings and emotional effects. There is quite considerable inverse correlation between the disposition to poor context and roles of feelings (-0.449, Sig. 0.000) and intuition (-0.393, Sig. 0.002)

in decision making. On the other hand, the direct correlation between the inclination to poor context and knowledge importance in decision making (0.462, Sig. 0.000) was demonstrated as well. These data let us to believe that as more respondents are disposed to be guided by feelings and intuition in decision making, as more they would appreciate the rich context mode of e-offer. The majority of Russian respondents in this survey demonstrated their propensity to be guided by facts and knowledge (not feelings and intuition) on e-purchase, thus, poor context e-offers should be more prominent on Russian e-market. Moreover, in online purchase Russians are highly uncertainty avoidant and long-term oriented. The uncertainty avoidance directly correlates with knowledge and facts importance in decision making (0.385, Sig. 0.002). Like so, e-offers intended for Russian market should be very precise and detailed, providing more factual and trustworthy (possible to check) information about offered product (or service) and e-retailer itself, as Russians are inclined to spend additional time to find out more about potential e-business partner before e-purchase.

The resumptive means of considered cultural dimensions and psychological aspects of decision-making illustrated on fig. 4 demonstrate the dominant dimensions as well as similarities and differences between e-purchasers by countries of residence.

Logical is the observed link between roles of facts and feelings in decision-making: the more the respondents of one country rely on facts the less important feelings are for them during online purchasing. According to the survey results the respondents from Latvia, Lithuania and Russia are quite close in attitude to cultural dimensions, for example, they are indifferent to power distance or low-power distance minded, have aptitude for poor context and traditional gender roles perception.

Figure 4: Mean values of agreement with statements describing dimensions by countries



As concerns other dimensions e-purchasers from Latvia seem to be a bit different from Lithuania or Russia residents – it is coherent with separation of these countries in Lewis (2008) model. But still these differences are not drastic and the cultural attitudes of respondents from considered countries are not opposite between them, as it was expected after analysis of Hofstede indexes.

Aiming to identify what of observed differences between countries are statistically significant, the data were disposed to the Independent Samples t-test for equality of means with Levene's test. There was found statistically significant difference (on 0.05 level) between Lithuanian and Latvian e-customers in perception of Uncertainty avoidance (equal variances assumed: F 3.39, sig. 0.068; mean difference 0.416), Long-tem orientation (equal variances assumed: F 0.319, sig. 0.573; mean difference 0.592), Understanding of authority (equal variances not assumed; mean difference 0.535),

Relations in society (equal variances not assumed; mean difference 0.749), Feelings role in decision making (equal variances not assumed; mean difference -0.748), and Intuition role in decision making (equal variances not assumed; mean difference -1.095).

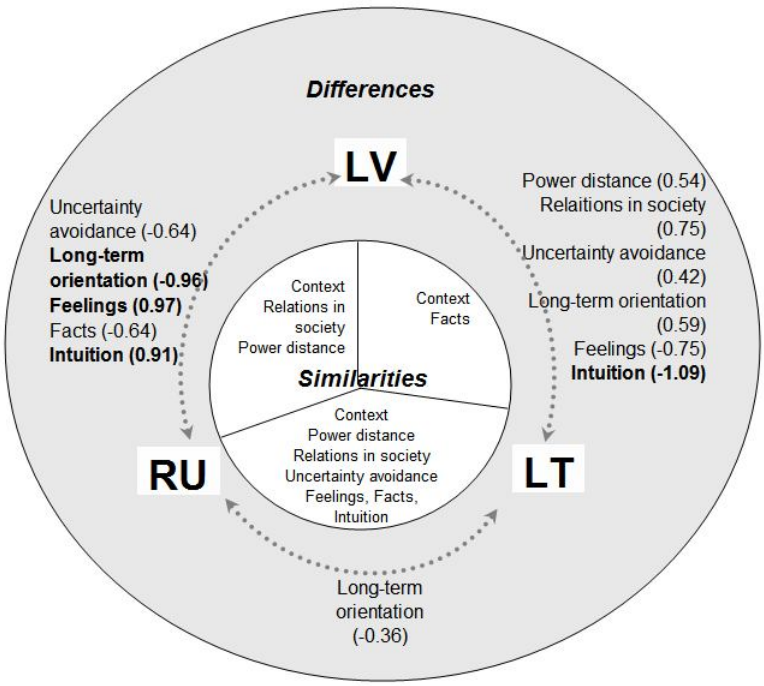
In case of comparison between Latvian and Russian respondents the statistically significant differences (on 0.05 level) were found for such dimensions and psychological aspects: Long-term orientation (equal variances assumed: F 0.211, sig. 0.647; mean difference -0.956), role of Feelings in decision making (equal variances assumed: F 3.643, sig. 0.059; mean difference 0.969), role of Facts in decision making (equal variances assumed: F 0.116, sig. 0.734; mean difference -0.637), role of Intuition in decision making (equal variances not assumed; mean difference 0.908), and Uncertainty avoidance (equal variances not assumed; mean difference -0.639).

As concerns comparison between Lithuania and Russia the difference on only one dimension was found statistically significant (on 0.05 level) – it is Long-term orientation (equal variances assumed: F 0.008, sig. 0.930; mean difference -0.365).

Thus, the conducted analysis discovered interesting situation: according to the number of dimensions, where statistically significant differences were found, two Baltic countries, neighbors and the only members of the same language family, in the online purchase are less similar between them than each of them are similar to Russia. However, the values of means differences between Latvia and Lithuania are smaller than between Latvia and Russia.

The fig. 5 is provided for complex analysis of identified differences and similarities between considered countries, the values of statistically significant differences are indicated in brackets.

Figure 5: Differences and similarities of cultural and psychological attitude in online purchase



Latvia has the largest amount of deviations with respect to the countries considered, while Russia has the majority of similarities. The difference in time perception was identified between all three countries – Latvian e-customers are less minded to keep long-term contacts and can be more oriented to quick-purchase mode than Lithuanian and Russian online customers, while Russia's

residents in online purchase are minded to make decisions according to earlier purchase experiences, relations with retailer and loyalty considerations. Like so, the loyalty and trust development strategy could be more efficient on the Russian market than on Latvian and Lithuanian ones, as e-customers from Baltic countries during the survey showed more flexibility about long-term orientation, they could easier than Russians change e-retailer and are not ready to spend long time for searching of particular long-term partner as Russians do.

Other discovered differences are pertinent to Latvia's case. Latvian online customers do not like uncertainties in the e-purchase, but they are more relaxed about it than their counterparts in Lithuania and Russia. Thus, the strategy of simplification of e-purchase process and maximization of the understandability of provided information about e-offer, which is indispensable for countries with high uncertainty avoidance, would be efficient in case of all three considered countries despite the identified difference between them.

The same situation can be observed for factual information's role in decision making – the providing of facts in e-offer is needed in all considered countries. However, Latvian e-customers are significantly more impacted by feelings and intuition when making decisions on online purchase – the role of these aspects is as important as role of facts, while Russians and Lithuanians trust more facts and are quite indifferent about emotional part of e-purchase. Like so, the e-offers oriented to the Latvian market should appeal to customers feelings and create basis for purchase of emotional origin.

Thus, the choice of Russian cultural model for online purchase would be rational, as (1) such a model would be suitable not only for Russian but for Lithuanian online customers as well, (2) at some extent it is acceptable for Latvian online customers, (3) Russia's market is big and promising, so the investments in the adaptation to Russia's online market should be the most rewarding.

4. Conclusions

The analysis of answers of Latvian, Lithuanian and Russian respondents showed the cultural dimensions important during online purchase in case of each country. The considered countries profiles described by Hofstede indexes and by Lewis cultural model differ from the attitude to the cultural dimensions expressed by e-purchasers from these countries. Thus, there is a need to correct the commonly accepted countries cultural profile to online area – as e-purchasers can present the part of society that in decision making differs significantly from general society. Basing on the survey's results it can be concluded that e-offer adapted to Russian e-purchasers could be successfully accepted by e-purchasers from Lithuania and Latvia – it would allow to keep expenses for localization on effective level.

However, the presented results of survey should be checked with bigger audiences and can deviate dependently on e-commerce sector, different age and incomes of target groups. Notwithstanding, the presented survey is believed to be useful on the start-stage of e-offers adaptation to the target markets as well as for further researches on the issue.

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The Role and Weight of Standards in Hotels

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Abstract

The article is dealing with standardization in hotels. Standards are used by international hotel chains regularly, but the importance of these standards is nearly never mentioned. This article is focusing on the role and weight of standards. Six interviews were organized with hotel managers. The interview structure was prepared according to existing hotel standard collections and managers had to evaluate the listed categories according to their importance, which gave the weights to the standards. The weights can help the authors to be able to order the standards according to their importance and after that in later research to evaluate other (not chain member) hotels by using mostly the important or not important standards. The paper is giving a chance to other authors, researchers and hoteliers to be able to decide which standards are more important to install and which are less important according to the list shown in the article.

Keywords

Standardization, weight, hotels

1. Introduction

At first it is essential to realize that standardization is not a favored topic either in the service management or in hotel management literature. The reason for this fact can be identified by the technocratic paradigm associated with standards. As services are mostly characterized by their individuality and their ability to be customized to meet the guests' needs better, standardization is kept back and hardly emphasized. However there is a tradition for standardization in the financial sector, which results some descriptions and analyses in this area. (Blind, 2006) Hotel sector can provide some good examples for creating standards, although these rules mostly exist in within hotel chains and hotel groups.

Firstly the article is going to introduce the definitions of standardization and the advantages and disadvantages of this concept. The second part of the paper is dealing with the standards focusing on hotels. Finally the paper continues with the results of the research which was carried out by the authors. The interviews can help researchers and hotel managers to identify the most important standards and emphasize them during the operation of the hotel.

2. Definitions for Standardization

In service as well as in literature of different sciences there are several definitions of standardization. In the followings some of the decisive ones which have their service connection and their difference in interpretation are going to be presented. According to the International Organization for Standardization (ISO) standards are documented agreements which contain technical specifications or other precise criteria. They are used consistently as rules, guidelines or definitions of characteristics, to make sure that materials, products, processes and services are fit for their purpose (Blind, 2006).

Berry et al. (1992) define standard as an essential tool for customer expectations and a meaningful asset for employees, they function as guideline for improving service quality. Imai (1997) identifies standard as a process that is the safest and easiest for the staff and it is the most cost-effective and productive way for the company to ensure quality for the customer. Droge, Jayaram, Vickery defined standardization as 'the use of standard procedures, materials, parts, and/or processes in designing and manufacturing a product' (Droge et al, 2004, p. 571). By Blind (2006) the major aims of standardization are fitness for purpose, compatibility, interchangeability (of products), variety control, safety, protection of the environment, and the product itself.

According to Hesser et al (2007) standardization is generally defined as the 'activity of establishing and recording a limited set of solutions to actual or potential problems directed at benefits for the party or parties involved, balancing their needs and intending and expecting that these solutions will be repeatedly or continuously used during a certain period by a substantial number of parties for whom they are meant.

Table 1: The definitions for standards and Standardization

	Standards
ISO	agreements, rules, guidelines, definition of characteristics, insurance of fitness with purposes
Berry et al. (1992)	guidelines for improving service quality according to customer expectations
MacDuffie (1995)	standard human resource guidelines, job specifications, set of standard activities
Imai (1997)	the safest and easiest method for workers and the most cost-effective and productive way for the company to ensure service quality
	Standardization
Droge et al (2004)	the use of standard procedures, materials, parts, and/or processes in designing and manufacturing a product
Blind (2006)	fitness for purpose, compatibility, interchangeability (of products), variety control, safety, protection of the environment, and the product itself
Hesser et al (2007)	establishing a limited set of solutions to problems of the parties, which are used repeatedly or continuously

According to Table 1 the definition of Standardization can be summarized by the following key words: *guidelines, rules, safety, consistency, productivity and quality*. In the service literature it always plays an important role to emphasize the fitness of standards to customer needs and ensure the constant quality for the customers.

3. The Reasons for Standardization

It is always an important issue for researchers and practical users to determine the reasons, the benefits and disadvantages of Standardization, if they are not used well. If standards are defined and work well they have a lot advantages such as: guiding and energizing employees; conveying a sense of priority; providing benchmarks against which employees can judge their own performance; allowing managers to judge employees' and the organization's performance; bringing a customer focus into employee's day-to-day reality of service delivery. (Berry et al., 1992) According to Imai (1997), standard procedures have the following features:

- represent the best, easiest, and safest way to do an activity, because workers on different shifts have to follow the same procedures which makes the system very cost-effective, efficient and safe;
- provide a method for managing knowledge through the preservation of "know how" and expertise because regardless of the comings and goings of individuals, the company can keep the know-how in the company;
- can be used as a reference to evaluate performance because with the using of standards job performance can be fairly measured;
- can show the relationship between cause and effect because if the company doesn't standards, it can cause abnormality, variability and waste (parachute folding) ;
- provide a basis for both maintenance and improvement activities because following standards is maintenance, improving standards is improvement, managers can't realize improvements without standards, so standards are the basis for both maintenance and improvement;
- able to provide objectives and indicate training goals because it is important for the standards to be understood either in a written form or by signs;
- provide a basis for training, because it is essential for the operators to be trained to use the standards;
- provide a basis for training, auditing, and diagnosis, because standards make it easier to control processes;

- provide a means for preventing recurrence of errors and minimizing variability, because quality control is one of the most important factor nowadays and by standards it is much easier for the management to control variability.

Like Standardization of materials, the Standardization of purchasing procedures could also be a potential point of cost savings for companies. However, the literature on Standardization of purchasing procedures is minimal. The use of standard purchasing procedures should reduce the possibility of errors and ease the tasks involved in identifying the root causes of a problem in the purchasing process. Once a problem has been fully identified, corrective action can be quickly implemented and the procedures may be rewritten to eliminate the problem.

According to the results of their article, it seems that Standardization of procedures, parts, and processes has a positive influence not only on being able to deliver on time but also on meeting customer needs effectively, which in turn is likely to have a positive effect on business performance.
Additional literature has shown that purchasing managers can save money by developing standard purchasing procedures that would enable them to spend more valuable time on "non-routine" activities, such as cost/value analysis, supplier development, and concurrent engineering (Sánchez-Rodríguez, 2006).

Table 2: The advantages of Standardization

	Advantages of Standardization
Berry (1992)	Guidance and energizing employees, clarification, help to sense priority, make easy measure employees' performance for themselves and the managers, bring customer focus
Imai (1997)	Best, easiest, safest way; keep know-how at the company, easy performance evaluation; good way to identify cause and effect; good for both maintenance and improvement; able to provide objectives; provide basis for training; easier to control processes; better quality control
Sánchez-Rodríguez (2006)	Cost saving, reduce the possibility of error, help identify the causes of problems, help satisfy customer needs (reliability), positive effect of business performance (have more time to non-routine activities)

In addition Berry et al. (1992) have found out what problems can be caused by using standards and Standardization improperly:

- *No service standards*: it means that the management doesn't believe in the importance of services
- *Too many service standards*: it causes that employees won't be aware of the most urgent service priorities
- *General service standards*: it is too little direction for employees but a limited basis for measuring their performance
- *Poorly communicated service standards*: it makes uncertainty among employees about standards
- *Service standards unconnected to the performance measurement, appraisal, and reward systems*: it means that service isn't a high priority for the management

According to the above shown literature and Table 2 the most important advantage of Standardization is the possibility for reducing costs. The second important is the quality assurance (by avoiding variance) and the measurement of the performance (of the employees and the organization). Standardization means guidelines and rules which make companies able to reduce costs, assure quality and help employees to do their work safe and effectively and help the organizations measure the work performance.

4. Hotel Standardization

Standardization is used in order to help the management to control, predict and minimize mistakes and deviation among employees. The primary aim with Standardization is the controlling of the output activity and service quality. It is a way to minimize risks, especially the ones dependent upon the human factor. Via standards and manuals the management keeps risks, connected to the production process, at a minimum. In order to make sure that we achieve a standard within our division, and to make sure that we achieve our mission statement in order to strive for a quality strategy, standardized policies are must. Everyone describes that there is a given set of standards that one has to adapt to. They say that it is good and it gives them security to know that they have a "bible" (as one of them described it) to relate to. Standards express what is expected in different service situations and manuals express how to accomplish it in practice. It can be observed that there is clear Standardization internally (in the sense that staff is expected to do the same) as well as externally (the hotels develop similar procedures) (Sandoff, 2005).

According to another research, hotel managers are increasingly facing a choice between a strategy of standardization and a strategy of individualization. A standardization strategy provides an accepted quality standard for all hotels within a given chain. Such a quality standard allows guests to form a clear understanding of the standard of services expected in all hotels in the chain worldwide. This strategy enables the hotels to improve global customer loyalty and generate positive word-of-mouth recommendations for all hotels in the chain. Big hotel chains often need to improve their productivity through Standardization of processes or outcomes to sustain their cost-based competitiveness.

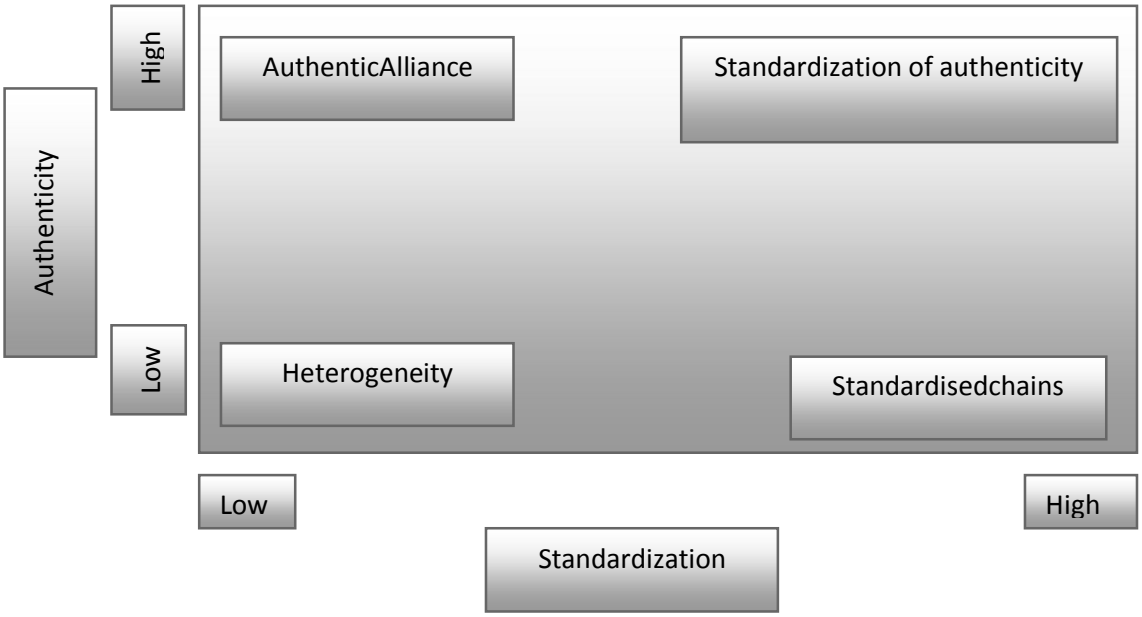
The difficulty (for customers) of perceiving the quality of services or processes in advance thus increases the imperative to introduce a system of quality standard signals to reduce uncertainties for the customer. Bouncken et al' (2005) study suggests that hotel managers who are following a Standardization strategy should promote communication and learning procedures among hotels. A standardized information system, handbooks, and meetings between management and staff (as well as informal contacts among employees) are all associated with this strategy. Hotels also have to consider implementing standardized processes in all functions (Bouncken et al, 2005).

5. The Relationship Between Standardization and Customization

There is no commonly accepted theory of the relationship of Standardization and customization. Researchers like Teboul (2005) states that Standardization and customization are two ends of a continuum, which means that if a hotel is highly standardized it cannot be highly customised. However, these concepts are called in other names in other authors' articles and books, they are dealt the same way as two independent dimensions (Shewhart, 1931; Sasser, 1990; Normann, 1991; Van Mesdag, 2000 and Tether et al, 2001).

Other researchers however like one of the current paper's authors see the problem in another way. Sundbo (1994, 2002) defines modulization as a solution to compare advantages of standardization and customization. MacDuffie (1995) and Droge (2004) mention flexible production plants as effective methods to mix Standardization and customization. Zeng et al (2012) also claims and illustrates the same independent dimensions (though using the name authenticity instead of customization) in the restaurant market in China.

Figure 1: The strategic position of companies analyzed by Zeng et al (2012)



However, Figure 1 shows a category which mixes the two dimensions called standardization of authenticity. Zeng et al (2012) use case studies to analyze the different methods of restaurant chains expansions. As the case for standardization of authenticity they chose Little Sheep Catering Chain Co. LtD, which successfully combines the standardized management systems and value co-creation, economy of scale and economy of scope. Another perspective was presented in a previous paper of one of the authors. Gyurácz-Németh, Clarke, (2011) state that Standardization and customization are both needed in the operation of a hotel.

Figure 2: Illustrating Accor brands according to the new theory

The theory uses the scale of Accor hotels to explain the relationship. In Sofitelit is obvious that the role of customization is higher than in Formula 1 hotels. The more significant role of customization is

understandable comparing to Formula 1 hotels. However Standardization is still necessary and the amount of Standardization should be higher as well because these luxury hotels have numerous types of services which should be standardized and mostly more demanding clientele who are requesting reliable quality. It is clear that in Formula 1 hotels customization is not important at all because of their budget hotel status but it is not at all accurate to state that a luxury hotel does not need to be standardized (Gyurácz-Németh, Clarke, 2011).

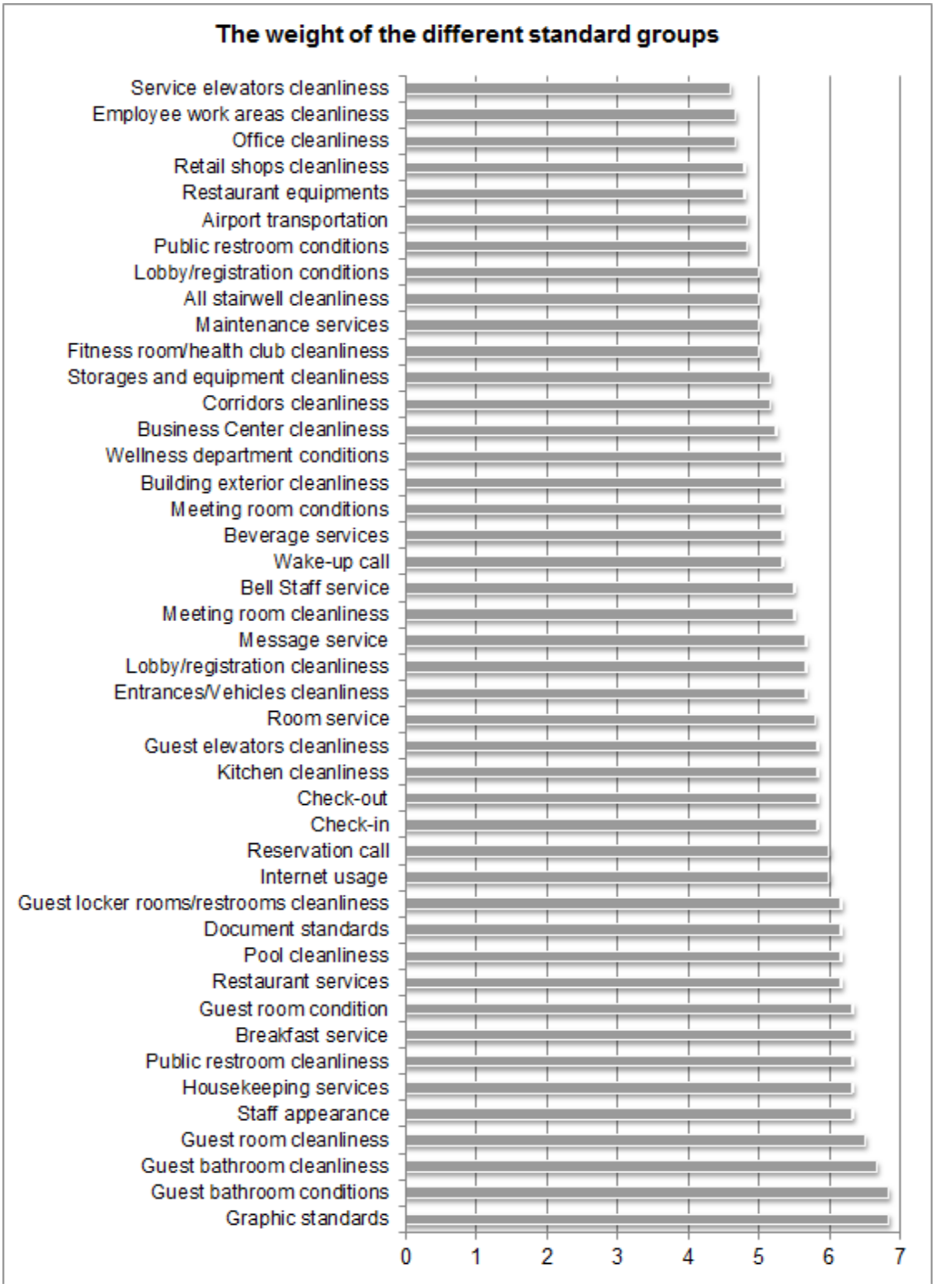
6. Research

The reason of the research was the fact that although there are several kinds of standards hotels apply in their everyday operations these standards are not equally important and appreciated by the staff and the managers. During the research six interviews were carried out with hotel general managers who are leading the operations of hotel chain members. In the selection of the hotel managers, gender and geography was not important, only their knowledge and experience with hotel standards.

The interview structure was set up with the help of hotel standard collections. These so-called ‘standard books’ contain all the rules the hotel staff have to apply to deal with guests or clean the rooms and public spaces besides staff offices. The standards are classified into different groups and the authors used these groups to reduce the number of standards, which would have been impossible to handle in other way. In the interview the general managers needed to mark the importance of the listed standard groups in a 1-7 scale, where 1 means low importance and 7 means high importance.

The Figure 3 shows the result of the research, the difference between the importance of standards.

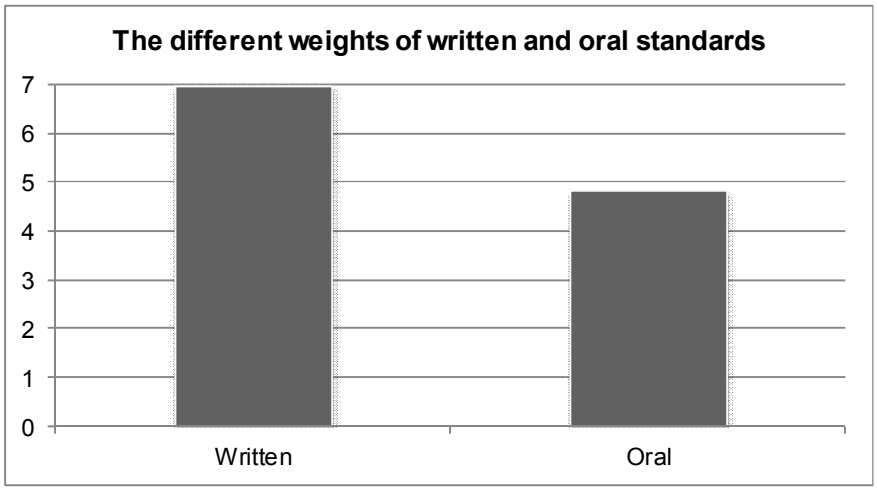
Figure 3: The different weight of standard groups



The first thing which is easy to recognize from Figure 3 is that the importance of services which involve the guests are more important than the employees. The most important standard groups include the guest bathroom condition and cleanliness but one of the less important is cleanliness of the employee work areas and the service elevators. The dominance of graphic standards (on the first place) may be a little bit surprising, but knowing the hotel chains' or the franchise owners' strict rules regarding the usage of the logo and slogan and its competitive advantage in the market, it is not a

surprising fact. The other important question of the research was to define the different significance of the written and oral standards.

Figure 4: The weight of written and oral standards



It was presumed by the authors that the significance of the written standards was going to be higher than the oral standards but regarding the further research the exact rate was important. As the results of the interviews (which can be seen on Figure 4), the difference was able to be defined, the weight of the written standards is the maximum weight (7), and the weight of oral standards got an average 4.83, so the difference is 2.17.

7. Conclusion

The aim of the paper was to emphasize the significance of Standardization in different fields of study and usage especially in the hotel business. Standardization is valued higher as customers are getting more quality conscious and expect the hotel to assure quality well. Beyond assuring quality standards can be easily used as guidelines and rules which make the company's operation more predictable and consistent. The reliable work and the existing guidelines increase the productivity of the hotel or other kind of service companies.

The paper analyzed the relationship between Standardization and customization, which can be dealt as two independent variables or (as one of the authors suggest) two factors which are in connection with each other.

As the importance of standards is obvious after the literature review, one question emerged to the authors: does each standard have the same importance? The definite answer was no, but another question how they should be differentiated remains. With the help of six hotel managers interviews resulted very significant facts. The research showed that graphic standards are the most important standards, which is followed by guest bathroom and room cleaning. The end of the list contains the cleanliness of hotel staff areas.

In the paper the question of strength of written and oral standards, guidelines emerged as well, and it was found that the strength difference between the two is 2.17.

According to the research the following recommendation can be formalized to the hotel managers, who are operating independent hotel without standards: Standardization and guidelines need to be emphasized but not for every kind of operations and in different significance. The hotel managers

have to concentrate on guest processes and graphic standards and do not have to force the Standardization of staff areas according to these results. In the further research these weights are going to be used to determine the level of Standardization of each independent hotels who join the research in Hungary.

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Corporate Governance and Price Momentum

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Extended Abstract

This paper explores the relationship between corporate governance and price momentum by using the degree of a firm's anti-takeover provision as a measurement for corporate governance. Our empirical results show that there exists a significant relationship between the degree of anti-takeover provision of a firm and a firm's price momentum profit. In specific, we find that firms with fewer anti-takeover provisions tend to exhibit higher price momentum pattern and thus generate higher price momentum profit. For a robustness check, we re-investigate our results by having the following three adjustments: (1) adjusting our portfolio returns for the Fama-French three factor model (Fama and French, 1993); (2) adjusting the industry factor (Moskowitz and Grinblatt, 1999; Grundy and Martin, 2001); and (3) adjusting by lagging one month period between the return formation period and the return holding period in order to mitigate the impacts to our portfolio returns from the bid-ask spread, price pressure and lagged reaction effects (Jegadeesh and Titman, 1993). After adjusting for all of the above factors, we still find significant higher price momentum profit from the firms with fewer anti-takeover provisions. This implies that our results cannot be explained by Fama-French's three factor model, the industry factor or the micro-structure factors such as bid-ask spread, price pressure and lagged reaction effects depicted by Jegadeesh and Titman (1993).

The potential explanation for our finding is that firms with fewer anti-takeover provisions tend to have higher degree of information asymmetry between management and shareholders (Cai, Liu and Qian, 2009). And because of the information asymmetry, the information of the corporation and management will not be dissimilated to the market as quickly and thus it will slow down theprocess of the new information incorporated into the market prices. Therefore, the price under-reaction to the information leads to the price momentum (See, e.g., Jegadeesh and Titman, 1993; Hong and Stein, 1999; Doukas and McKnight, 2003).

Table 1 verifies what has been found in the literature on the existence of the significant momentum profits but based on our sample period from 1990 to 2008. The difference between Panel A and Panel B is that Panel B represents the momentum results by lagging the return holding period for a month from the return formation period. The price momentum profits are shown in "P10-P1", the return difference between winner and loser portfolios. As evidenced from either Panel A or Panel B

that price momentum profits are significant in almost every one of the different return holding horizons from 3-month to 12-month periods.

Table 2 shows the main results regarding the higher price momentum for the companies that exhibit fewer anti-takeover provisions. As in Table 1, “P10-P1” represents the momentum profits. However, in Table 2 we add another dimension “G1-G10”, which represents the return difference between the “G1”, companies with fewer anti-takeover provisions (“democracy” companies) and the “G10”, companies with more anti-takeover provisions (“dictatorship” companies). The figures intersect the “P10-P1” columns and the “G1-G10” columns are the differences in price momentum between companies with fewer anti-takeover provisions and those with more anti-takeover provisions. Table 2 shows that in each of the different holding periods from 3-month to 12-month the price momentum for the companies with fewer anti-takeover provisions (“democracy” companies) is always significantly higher than that for the companies with more anti-takeover provisions (“dictatorship” companies).

For diagnosis and robustness checks, we also re-examine the above results: (1) by lagging one month between the return formation period and the return holding period, which is shown in Table 3; (2) by adjusting for the Fama-French three factor model, which is shown in Table 4; and (3) by adjusting for the industry effect, which is displayed in Table 5. All of the three tables demonstrate that after adjusting for the above three factors, the higher price momentum exhibited in the democracy companies still remains. That implies that the phenomenon found in Table 2 cannot be explained by any of the above factors. Thus, our above findings strongly suggest that the information asymmetry existing in the democracy companies, i.e., the companies with fewer anti-takeover provisions, causes the market under-reacts to the information and thus leads to a higher price momentum.

Table 1: Price Momentum

The figures in the table are the returns for each of the portfolios, P1, the loser portfolio, P10, the winner portfolio, and P5, the intermediate portfolio. The momentum profit is the difference between return of the winner portfolio and the loser portfolio, P10-P1. Our sample companies include those that have G Index during our sample period from 1990 to 2008. "J" and "K" indicate the different return formation periods and return holding periods, respectively, from 3-month to 12-month horizons. G Index is the corporate governance index, with smaller (larger) number represents fewer (more) anti-takeover provisions. In Panel A, there is no lag between return formation and return holding periods, while in Panel B there is one month lag between those two periods. Figures in the parentheses are the Newey-West t statistic. "*", "**" and "***" denote the 10%, 5% and 1% significance level, respectively.

J	Portfolio	G Index	Panel A				Panel B			
			K=3	K=6	K=9	K=12	K=3	K=6	K=9	K=12
3	P1	8.84	0.96	0.89	0.91	1.08	0.91	0.85	0.92	1.15
			(2.30)**	(2.92)***	(3.73)***	(5.20)***	(2.20)**	(2.83)***	(3.83)***	(5.59)***
	P5	9.42	1.02	1.07	1.12	1.18	1.05	1.10	1.14	1.20
			(4.13)***	(5.87)***	(7.37)***	(9.09)***	(4.22)***	(5.94)***	(7.63)***	(9.22)***
	P10	8.83	1.32	1.48	1.63	1.65	1.36	1.54	1.65	1.63
			(3.57)***	(5.10)***	(6.91)***	(7.59)***	(3.60)***	(5.31)***	(7.13)***	(7.27)***
	P10-P1		0.35	0.59	0.71	0.56	0.45	0.69	0.72	0.48
			(1.17)	(2.51)**	(4.11)***	(3.49)***	(1.50)	(3.10)***	(4.16)***	(2.88)***
6	P1	8.78	0.83	0.76	0.84	1.08	0.79	0.73	0.90	1.17
			(1.92)*	(2.46)**	(3.35)***	(4.93)***	(1.86)*	(2.38)**	(3.61)***	(5.23)***
	P5	9.41	1.05	1.09	1.13	1.21	1.09	1.10	1.15	1.21
			(4.36)***	(6.15)***	(7.67)***	(9.57)***	(4.53)***	(6.05)***	(7.87)***	(9.42)***
	P10	8.80	1.53	1.69	1.73	1.68	1.58	1.71	1.69	1.60
			(3.92)***	(5.80)***	(6.82)***	(7.30)***	(4.10)***	(6.04)***	(6.82)***	(6.99)***
	P10-P1		0.70	0.94	0.88	0.59	0.79	0.98	0.79	0.43
			(2.20)**	(4.31)***	(4.41)***	(3.13)***	(2.60)***	(4.66)***	(3.94)***	(2.21)**
9	P1	8.76	0.70	0.73	0.90	1.17	0.70	0.76	0.99	1.29
			(1.55)	(2.30)**	(3.45)***	(5.03)***	(1.58)	(2.40)***	(3.76)***	(5.48)***
	P5	9.43	1.04	1.06	1.12	1.17	1.06	1.08	1.12	1.18
			(4.38)***	(6.02)***	(7.62)***	(9.14)***	(4.46)***	(6.13)***	(7.78)***	(9.21)***
	P10	8.81	1.71	1.73	1.68	1.61	1.72	1.69	1.61	1.54
			(4.44)***	(5.69)***	(6.33)***	(6.80)***	(4.41)***	(5.52)***	(6.19)***	(6.63)***
	P10-P1		1.01	1.00	0.78	0.44	1.02	0.92	0.61	0.25
			(3.19)***	(3.91)***	(3.31)***	(2.13)**	(3.25)***	(3.49)***	(2.60)**	(1.19)
12	P1	8.74	0.69	0.81	1.02	1.26	0.77	0.90	1.14	1.35
			(1.53)	(2.46)**	(3.64)***	(5.19)***	(1.73)*	(2.71)***	(4.10)***	(5.56)***
	P5	9.44	0.99	1.05	1.10	1.17	1.05	1.08	1.13	1.18
			(4.18)***	(5.92)***	(7.50)***	(9.12)***	(4.28)***	(5.96)***	(7.70)***	(9.05)***
	P10	8.81	1.58	1.57	1.50	1.48	1.52	1.48	1.42	1.42
			(3.97)***	(5.07)***	(5.82)***	(6.50)***	(3.80)***	(4.85)***	(5.61)***	(6.31)***
	P10-P1		0.89	0.76	0.48	0.22	0.75	0.58	0.28	0.07
			(2.51)**	(2.64)***	(1.94)*	(1.03)	(2.13)**	(2.03)**	(1.16)	(0.30)

Table 2: Corporate Governance and Price Momentum

The figures in the table are the returns for each of the portfolios, P1, the loser portfolio, P10, the winner portfolio, and P5, the intermediate portfolio. The momentum profit is the difference between return of the winner portfolio and the loser portfolio, P10-P1. Our sample companies include those that have G Index during our sample period from 1990 to 2008. G1 represents companies with fewer anti-takeover provisions (with G Index ≦5), while G10 represents companies with more anti-takeover provisions (with G Index ≧14). "J" and "K" indicate the different return formation periods and return holding periods, respectively, from 3-month to 12-month horizons. G Index is the corporate governance index, with smaller (larger) number represents fewer (more) anti-takeover provisions. In Panel A, there is no lag between return formation and return holding periods, while in Panel B there is one month lag between those two periods. Figures in the parentheses are the Newey-West t statistic. "*", "**" and "***" denote the 10%, 5% and 1% significance level, respectively.

						J = 3						
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	0.88	1.38	-0.50	0.79	1.29	-0.49	0.77	1.34	-0.57	0.96	1.38	-0.42
	(1.81)*	(2.93)***	(-1.42)	(2.29)**	(3.42)***	(-1.71)*	(2.71)**	(4.50)***	(-2.27)**	(3.89)***	(5.55)***	(-1.86)*
P10	1.57	1.09	0.49	1.73	1.09	0.64	1.83	1.23	0.60	1.91	1.18	0.73
	(3.39)***	(2.31)**	(1.25)	(4.62)***	(3.70)***	(1.86)*	(5.78)***	(5.07)***	(2.17)**	(6.21)***	(5.21)***	(2.63)***
P10-P1	0.69	-0.29	0.98	0.94	-0.19	1.13	1.06	-0.11	1.17	0.95	-0.21	1.16
	(1.72)*	(-0.59)	(2.34)**	(3.10)***	(-0.59)	(3.14)***	(4.56)***	(-0.39)	(3.59)***	(4.04)***	(-0.83)	(3.62)***
						J = 6						
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	0.48	1.62	-1.14	0.38	1.49	-1.11	0.60	1.48	-0.88	0.78	1.48	-0.7
	(0.97)	(3.26)***	(-2.60)***	(1.12)	(3.78)***	(-3.35)***	(2.07)**	(4.51)***	(-3.16)***	(2.92)***	(5.34)***	(-2.56)**
P10	1.73	1.08	0.66	1.95	0.97	0.98	2.00	1.02	0.98	2.03	1.05	0.98
	(3.64)***	(2.52)**	(1.49)	(5.08)***	(3.22)***	(2.68)***	(5.75)***	(4.19)***	(2.92)***	(6.06)***	(4.66)***	(3.02)***
P10-P1	1.26	-0.54	1.80	1.57	-0.52	2.09	1.40	-0.46	1.86	1.24	-0.43	1.67
	(2.95)***	(-1.04)	(3.13)***	(5.67)***	(-1.25)	(4.54)***	(5.39)***	(-1.32)	(4.64)***	(4.28)***	(-1.51)	(4.51)***
						J = 9						
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	0.39	1.71	-1.32	0.50	1.62	-1.12	0.73	1.65	-0.92	0.92	1.71	-0.79
	(0.77)	(2.79)***	(-2.71)***	(1.39)	(3.51)***	(-3.15)***	(2.42)**	(4.30)***	(-2.70)***	(3.32)***	(4.88)***	(-2.36)**
P10	1.94	0.76	1.18	2.04	0.89	1.15	2.06	0.85	1.21	2.02	0.80	1.22
	(3.87)***	(1.84)*	(2.46)**	(4.96)***	(2.91)***	(3.06)***	(5.49)***	(3.52)***	(3.58)***	(6.05)***	(3.48)***	(3.86)***
P10-P1	1.55	-0.94	2.50	1.54	-0.73	2.27	1.33	-0.80	2.13	1.10	-0.91	2.01
	(3.65)***	(-1.53)	(3.87)***	(5.32)***	(-1.55)	(4.48)***	(4.53)***	(-2.1)**	(4.88)***	(3.73)***	(-2.81)***	(4.96)***
						J = 12						
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	0.49	1.77	-1.28	0.60	1.59	-0.98	0.73	1.54	-0.81	0.93	1.60	-0.67
	(0.92)	(2.65)***	(-2.21)**	(1.58)	(3.14)***	(-2.39)**	(2.17)**	(3.70)***	(-2.25)**	(3.10)***	(4.02)***	(-1.90)*
P10	1.47	0.67	0.80	1.65	0.87	0.78	1.62	0.79	0.83	1.70	0.77	0.93
	(2.99)***	(1.63)	(1.93)*	(4.12)***	(3.03)***	(2.27)**	(4.75)***	(3.33)***	(2.84)***	(5.02)***	(3.45)***	(3.05)***
P10-P1	0.98	-1.10	2.08	1.04	-0.72	1.76	0.89	-0.75	1.64	0.77	-0.83	1.60
	(2.45)**	(-1.67)*	(3.31)***	(3.03)***	(-1.51)	(3.64)***	(2.77)***	(-1.97)**	(4.08)***	(2.33)**	(-2.35)**	(4.10)***

Table 3: Corporate Governance and Price Momentum – Lagging Return Holding Period for One Month

This table presents the results for the corporate governance and price momentum by lagging one month for the return holding period. The figures in the table are the returns for each of the portfolios, P1, the loser portfolio, P10, the winner portfolio, and P5, the intermediate portfolio. The momentum profit is the difference between return of the winner portfolio and the loser portfolio, P10-P1. Our sample companies include those that have G Index during our sample period from 1990 to 2008. G1 represents companies with fewer anti-takeover provisions (with G Index ≦5), while G10 represents companies with more anti-takeover provisions (with G Index ≧14). "J" and "K" indicate the different return formation periods and return holding periods, respectively, from 3-month to 12-month horizons. G Index is the corporate governance index, with smaller (larger) number represents fewer (more) anti-takeover provisions. In Panel A, there is no lag between return formation and return holding periods, while in Panel B there is one month lag between those two periods. Figures in the parentheses are the Newey-West t statistic. "*", "**" and "***" denote the 10%, 5% and 1% significance level, respectively. For saving the space, only two return holding periods, 6-month (J=6) and 9-month (J=9), are reported in this table. The results are qualitatively the same for the 3-month and 12-month return holding periods.

J=6												
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	0.35 (0.71)	1.69 (3.29)***	-1.34 (-2.74)***	0.36 (1.01)	1.58 (3.93)***	-1.22 (-3.79)***	0.71 (2.37)**	1.48 (4.47)***	-0.77 (-2.64)***	0.84 (3.06)***	1.54 (5.43)***	-0.70 (-2.55)**
P10	1.96 (4.15)***	1.03 (2.50)**	0.93 (2.22)**	2.03 (5.25)***	1.03 (3.53)***	1.00 (2.81)***	2.03 (5.85)***	1.08 (4.55)***	0.94 (2.87)***	1.96 (5.97)***	1.14 (4.81)***	0.83 (2.82)***
P10-P1	1.61 (4.23)***	-0.65 (-1.21)	2.27 (3.88)***	1.67 (6.48)***	-0.54 (-1.29)	2.22 (5.00)***	1.32 (4.73)***	-0.40 (-1.18)	1.72 (4.49)***	1.13 (3.81)***	-0.40 (-1.39)	1.53 (4.32)***

J=9												
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	0.31 (0.61)	1.63 (2.65)***	-1.32 (-2.73)***	0.57 (1.58)	1.54 (3.36)***	-0.97 (-2.77)***	0.83 (2.66)***	1.68 (4.19)***	-0.86 (-2.41)**	0.99 (3.50)***	1.74 (4.71)***	-0.75 (-2.16)**
P10	2.02 (3.99)***	1.00 (2.44)**	1.02 (2.34)**	1.98 (4.82)***	0.95 (3.14)***	1.03 (2.94)***	1.91 (5.32)***	0.86 (3.55)***	1.05 (3.38)***	1.92 (5.77)***	0.85 (3.65)***	1.07 (3.30)***
P10-P1	1.71 (4.53)***	-0.63 (-1.08)	2.34 (3.85)***	1.42 (4.67)***	-0.59 (-1.30)	2.00 (4.25)***	1.08 (3.43)***	-0.83 (-2.25)**	1.91 (4.61)***	0.93 (2.94)***	-0.89 (-2.73)***	1.82 (4.50)***

Table 4: Corporate Governance and Price Momentum – Adjusted for the Fama-French Three Factor Model

This table presents the results for the corporate governance and price momentum by adjusting for the Fama-French three factor model. The figures in the table are the returns for each of the portfolios, P1, the loser portfolio, P10, the winner portfolio, and P5, the intermediate portfolio. The momentum profit is the difference between return of the winner portfolio and the loser portfolio, P10-P1. Our sample companies include those that have G Index during our sample period from 1990 to 2008. G1 represents companies with fewer anti-takeover provisions (with G Index ≦5), while G10 represents companies with more anti-takeover provisions (with G Index ≧14). "J" and "K" indicate the different return formation periods and return holding periods, respectively, from 3-month to 12-month horizons. G Index is the corporate governance index, with smaller (larger) number represents fewer (more) anti-takeover provisions. In Panel A, there is no lag between return formation and return holding periods, while in Panel B there is one month lag between those two periods. Figures in the parentheses are the Newey-West t statistic. "*", "**" and "***" denote the 10%, 5% and 1% significance level, respectively. For saving the space, only two return holding periods, 6-month (J=6) and 9-month (J=9), are reported in this table. The results are qualitatively the same for the 3-month and 12-month return holding periods.

	J=6											
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	-0.88	0.23	-1.11	-0.92	0.05	-0.97	-0.72	-0.06	-0.66	-0.70	-0.02	-0.68
	(-3.32)***	(0.61)	(-2.93)***	(-5.01)***	(0.16)	(-2.93)***	(-4.53)***	(-0.29)	(-2.40)**	(-4.24)***	(-0.11)	(-2.45)**
P10	0.77	0.01	0.77	0.86	-0.10	0.96	0.85	0.00	0.85	0.85	-0.08	0.94
	(2.88)***	(0.02)	(1.91)**	(3.75)***	(-0.44)	(2.87)***	(3.66)***	(-0.01)	(2.93)***	(3.90)***	(-0.56)	(3.56)***
P10-P1	1.65	-0.23	1.88	1.77	-0.15	1.92	1.56	0.06	1.50	1.55	-0.06	1.61
	(3.84)***	(-0.44)	(3.31)***	(6.04)***	(-0.35)	(3.89)***	(5.67)***	(0.19)	(3.84)***	(5.60)***	(-0.23)	(4.43)***

	J=9											
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	-0.96	0.27	-1.23	-0.81	0.17	-0.98	-0.56	0.19	-0.75	-0.55	0.08	-0.63
	(-3.61)***	(0.57)	(-2.66)***	(-4.67)***	(0.57)	(-2.89)***	(-3.63)***	(0.60)	(-2.05)**	(-3.38)***	(0.29)	(-1.74)*
P10	0.98	-0.31	1.30	0.94	-0.16	1.10	0.94	-0.14	1.08	0.87	-0.34	1.21
	(3.46)***	(-1.06)	(3.04)***	(4.15)***	(-0.68)	(3.23)***	(4.13)***	(-0.89)	(3.74)***	(4.20)***	(-2.27)**	(4.44)***
P10-P1	1.95	-0.58	2.53	1.75	-0.33	2.08	1.51	-0.33	1.83	1.42	-0.42	1.84
	(4.66)***	(-0.96)	(3.89)***	(5.94)***	(-0.75)	(4.20)***	(5.39)***	(-0.96)	(4.45)***	(5.36)***	(-1.50)	(4.56)***

Table 5: Corporate Governance and Price Momentum – Adjusted for the Industry Factor

This table presents the results for the corporate governance and price momentum by adjusting for the industry factor. The figures in the table are the returns for each of the portfolios, P1, the loser portfolio, P10, the winner portfolio, and P5, the intermediate portfolio. The momentum profit is the difference between return of the winner portfolio and the loser portfolio, P10-P1. Our sample companies include those that have G Index during our sample period from 1990 to 2008. G1 represents companies with fewer anti-takeover provisions (with G Index ≦5), while G10 represents companies with more anti-takeover provisions (with G Index ≧14). "J" and "K" indicate the different return formation periods and return holding periods, respectively, from 3-month to 12-month horizons. G Index is the corporate governance index, with smaller (larger) number represents fewer (more) anti-takeover provisions. In Panel A, there is no lag between return formation and return holding periods, while in Panel B there is one month lag between those two periods. Figures in the parentheses are the Newey-West t statistic. "*", "**" and "***" denote the 10%, 5% and 1% significance level, respectively. For saving the space, only two return holding periods, 6-month (J=6) and 9-month (J=9), are reported in this table. The results are qualitatively the same for the 3-month and 12-month return holding periods.

	J=6											
	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	-0.39	0.19	-0.58	-0.54	0.17	-0.72	-0.48	0.05	-0.52	-0.41	0.07	-0.48
	(-1.69)*	(0.48)	(-1.41)	(-3.43)***	(0.69)	(-2.52)**	(-3.39)***	(0.22)	(-2.53)**	(-3.45)***	(0.37)	(-2.38)**
P10	0.29	-0.19	0.49	0.32	-0.15	0.47	0.31	-0.27	0.58	0.24	-0.27	0.51
	(1.17)	(-0.53)	(1.24)	(1.85)**	(-0.54)	(1.44)	(1.93)**	(-1.27)	(2.15)**	(1.52)	(-1.51)	(2.21)**
P10-P1	0.69	-0.38	1.07	0.87	-0.32	1.19	0.79	-0.31	1.10	0.64	-0.34	0.99
	(2.04)**	(-0.73)	(1.95)*	(3.90)***	(-0.86)	(2.83)***	(3.69)***	(-1.04)	(3.55)***	(3.06)***	(-1.39)	(3.54)***

	K=3			K=6			K=9			K=12		
Portfolio	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10	G1	G10	G1-G10
P1	-0.69	0.15	-0.84	-0.50	0.16	-0.66	-0.37	0.16	-0.52	-0.37	0.21	-0.58
	(-2.66)***	(0.35)	(-1.95)*	(-2.81)***	(0.59)	(-2.23)**	(-2.50)**	(0.66)	(-2.30)**	(-3.29)***	(1.03)	(-2.83)***
P10	0.44	-0.30	0.74	0.35	-0.30	0.65	0.31	-0.36	0.67	0.22	-0.40	0.63
	(1.70)*	(-1.03)	(1.98)**	(1.84)*	(-1.41)	(2.29)**	(1.77)*	(-2.05)**	(2.97)***	(1.42)	(-2.44)**	(3.11)***
P10-P1	1.13	-0.45	1.58	0.84	-0.47	1.31	0.67	-0.52	1.19	0.59	-0.61	1.20
	(3.04)***	(-0.92)	(2.91)***	(3.30)***	(-1.36)	(3.44)***	(2.83)***	(-1.91)*	(4.58)***	(2.86)***	(-2.61)***	(5.04)***

Tagged to be Secure? Current Developments of Human Chip Implants and Implications for Companies and Employees

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Abstract

The future is wireless and human chip implants are no more mere science-fiction. "Technics" is becoming "embodied" (Ihde 2010). In the today's age of the 'Internet of Things' embedded, networked intelligent technical systems and equipment allows a development towards 'tagged' or 'chipped' humans. The basic technology is RFID (**R**adio **F**requency **ID**entification) as an automatic electromagnetic identification technology and data transaction system. During the last ten years, RFID seems to emerge as one of the most ubiquitous developments with diverse possible and already implemented applications and huge implications for business and individuals.

How does RFID technology work? A tag (device) or chip - on objects like products or a so-called human implant inside the body - needs a tag reader with an antenna and transceiver to gather the information stored on the chip and connects data to the company's computer system or host environment. Such RFID-technology as smart, ubiquitous, pervasive, ambient (mainly used terms), contactless and invisible communication between objects and objects or humans and objects, is used for manifold applications: for example from supply chain monitoring to toll collection and tail applications, wrist-bands for patient, tickets in parks, zoos or at events, rental car and driver tracking (drivability and kilometers travelled for individualized insurance rates), book tracking in libraries, ski lift access, and access control in companies for time tracking or security reasons. Most RDID-tags are passive devices, meaning that they have no power supply of their own. The minute electrical current induced in the antenna by the incoming radio-frequency scan provides enough power for the tag to send a response. Hence, these tags lie inactive until an RFID-reader transmits in their frequency range – the transmission provides enough juice to wake up the tag. RFID-tags, which possess their own power source, are larger in size and less common, have larger memories than passive tags, as well as they have the ability to store additional information sent by the transceiver, and can be read from much larger distances.

Human implants are miniaturized identification devices, with the potential to be used for security, identification, financial (as a kind of implanted credit card) or other reasons. An encapsulated chip has more or less the size of a grain of rice. Every chip contains a unique 16-digit identification number (ID). In October 2004, the United States Food & Drug Administration (FDA) approved human chip implants for medical purposes. Since then, prices for RFID chips have dropped; this is why tagging has become practical for businesses. Thus, besides the usage for patients, implants have also come to the forefront as a surveillance opportunity for companies: In 2006, CityWatcher.com (Cincinnati) has been the first publicly known company with implanted employees for security reasons. At nearly the same time, trendy nightclubs in Spain, the Netherlands, Scotland and the United States began to offer chip implants for its customers with special services like an entrance to the VIP-lounges, the payment of drinks via the implant by automatically charging the customer's credit card, etc. Simultaneously, another trend came up, namely chipping 'just for fun' for private

persons. In 2010, Albrecht (2010) estimated about 300 humans in the U.S. and about 2,000 worldwide who have been implanted (p. 346) for medical or security purposes. However, in the meantime, probably thousands are tagged worldwide. In addition, since the FDA-approval of human implants, in the US, several projects in hospitals with patients started, equally a national debate about mandatory chip implants for immigrants and guest workers.

Back to the question of human implants for employees: In their article "RFID inside", Foster and Jaeger (2007) bring an example of possible job advertisement in the future:

> WANTED: POWER SYSTEMS ENGINEER with experience in high-power (5-100-kW) motor-controller design. Must be U.S. citizen and have valid ISO1443-compatible access-control RFID implant. (pp. 27).

What about implications for companies and employees? The human body used as an information-processing device leads to crucial concerns, mainly in the field of *privacy* and personal rights protection, bodily *integrity*, personal *identity* and (information) *security*. In 2005, the European Group on Ethics in Science and New Technologies to the European Commission (EGE 2005) published an opinion on "Ethical aspects of ICT implants in the human body". Some of the aspects of human dignity, integrity, autonomy, privacy, surveillance, social aspects, risk predictability and special caution issues raised by the EGE seem to be still relevant:

> How far can such implants have irreversible impacts on the human [...]?
> […] How far can ICT implants become a threat to privacy?
> […] What are the potential invasions of privacy through ICT implants as sources and/or receivers of information in a network environment?
> […] How do we relate to persons with ICT implants that are connected online?
> […] How far are such possibilities dependent on such values as control or efficiency that may lead human beings to become even more dependent on market forces and even on the possibility of their (legal) use in the work place?
> How far do we transform our social and cultural environment through ICT implants?
> How far can they be used in order to track human beings and in which cases should this be legally allowed?
> To what extent does this technology allow manipulation by and for advertising?
> To what extent might this technology be misused by the military?
> How far can we predict today the benefits and threats of such ICT implants?
> (EGE 2005, pp. 24-26)

Unlike the (legal) situation in some states in the U.S., the EGE (2005) states a clear position concerning non-medical implants' applications and "[…] insists that such surveillance applications of ICT implants may only be permitted if the legislator considers that there is an urgent and justified necessity in a democratic society (Article 8 of the Human Rights Convention) and there are no less intrusive methods" (p. 34). To Rafael Capurro, member of the EGE, "[…] this recommendation is today even more crucial than it was in 2005" (Gasson et al. 2012, p. viii, foreword).

Regarding privacy, a forward-looking scenario may show the following situation (top manager in the field of ICT, interviewed at CeBIT, Hannover): "In the future, probably "[…] in about 10, 20 or 30 years, we will have two categories of persons: Firstly, persons who are prepared to lose their privacy - that will be mainstream trend and they will live without privacy. The second group will go down and exist on an aftermarket - they have to organize themselves, whatever way they are going to do it. That means, they will have to struggle for survival." Furthermore, beside privacy there exist also

other related aspects of implants in companies to consider: The permanently linkage of an implant to a person "[…] make them especially susceptible to privacy invasions and, in some cases, this persistent connection may even worsen the situation, exposing the RDID user to physical danger" (Kosta and Gasson Sep. 2008, p. 25). After some time and depending on the kind of implant, it is hardly possible to remove an implant (relating to bodily privacy). In cases of access control in companies (relating to location privacy), implants could be an advantage – nevertheless, tags can be cloned (p. 26) and may have other presently unknown implications. Mark Gasson, researcher at the University of Reading, had a tag inserted in his hand (version of ID chips used to tag pets) which was infected with a virus. Hence, depending on the quality of data stored on a chip of an employee in the future, this fact could also lead to security-related threats. All the same security and tracking issues of item level RFID-tagging are also relevant for implants - furthermore, a possible disabling ('killing') of tags as well as blocker tags for an avoidance of the functioning of a reader by broadcasting every possible RFID identification code are in use (Lockton and Rosenberg 2005, p. 225-229). Overall, security experts are warning of several risks connected with the use of human implants (e.g. Michael and Michael 2009). A further aspect relates to potential health impacts. Albrecht (2010) presents a review of studies (1990-2006) dealing with microchip-induced tumors in laboratory rodents and dogs and summarizes that implanted humans should be informed about the potential causal link between microchips and cancer (p. 346) (related to bodily privacy).

To summarize this proposal, when chips begin to be associated with individuals as a kind of bodily invasive surveillance, privacy, security and other risks for humans and organizations are threatened.—This article *(submission of full paper is planned)* tries to give an overview of the current state of development of human implants and effecting crucial issues for employees and companies in the future. In addition, surrounding organizational aspects like employees' working motivation, the role of leadership and others will be presented.

Keywords

Human implants, employee, organization, privacy, security

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Interdisciplinary Perspectives on Events Management

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Abstract

The paper aims to describe and to justify an innovative approach to events management. The discussion is based on (1) interdisciplinary, hermeneutical research within the two fields of sport and cultural sciences,(2) the re-evaluation of commonplace events management concepts as well as (3) in-depth interviews with managers of sports and cultural events. The systematical consideration of the connection between sport and cultural sciences can be seen as a desideratum: there are studies questioning the interfaces between the respective fields indeed. However the transfer of those findings into the field of events management hasn't been subject to discussion yet. The approach is meant to give a new impetus to a practically-oriented, interdisciplinary events research.

The analysis reveals various similarities between sports and cultural events with regard to their organizational principles and thus to the basic managerial competences needed. One important aspect in this regard is that both sports and cultural events are in many cases growing together, one only has to look at the various European Capitals of Culture with their numerous projects whose objective is to integrate sports and culture. Thus it seems to be of great importance to examine how themes from both fields may be combined in an integrative rather than additive sense. Furthermore both sports and cultural events represent specific cultural experiences, values and beliefs. Richard Sennett made clear that since the time of the Greek antiquity sports events were not only an act of entertainment or competitive shows (comp. Sennett 1995). The bodies of the athletes were representations of the values, ideas and self-concepts of the Greek polis. Culture was expressed through bodies which were presented in "contests" like the Olympic Games. Sport was, according to Sennett, not first of all an event in itself – it was symbolic representation of political, social and cultural ideas.

However events management in both fields also differs to an important extent, f.e. with regard to the understanding of the term "management", the use of basic managerial principles and, not least, the predictors and determinants of success. Therefore both event management in the fields of sport and culture can benefit to a great extent not only from a dialogue between science and practice but particularly from an interdisciplinary perspective integrating theories and approaches from the relevant disciplines. Before the background of the peculiarities mentioned simply transferring methods and approaches from common management and marketing theory is not appropriate to meet the various challenges (comp. Kaiser, Schütte & Keiner 2012; Kaiser & Schütte 2012; Kaiser & Wolfram 2012; Wolfram 2012).

Keywords

Events management, interdisciplinary approach, sports, culture

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Evolutionary Branches in Business Research: A Review of Converging Themes

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Abstract

It have become increasingly discussed in marketing, management and general business journals that 'Evolutionary', 'Darwinian', and associated labels represent dynamical and contextual-oriented ideas that have relevance in the future for both researchers and practitioners. While these theories come in assorted packages adopted to diverse audiences and inquiries, to bring order it is a warranted issue to address converging themes of relatedness and complementariness among research branchings under these labels. This paper reviews influential but divergent evolutionary branches to the study of organizational change, market dynamics, and industry and firm evolution. Building on this review, the paper address affinity and advocates that abstracted records of Darwinism demonstrate generic principles that could amalgamate the various branches of evolution-theoretic research upon a shared body of underlying commitments and principles. The concluding part considers relevance for future research in the light of standardization/adaptation problems in today's evolutionary branches of business research.

Keywords

Literature review, organizational change, market dynamics, Darwinism

1. Introduction

Many argue, with good reasons, that a trend of global convergence due to for example migration, supranational institutions and immediate access to information is ongoing (Hollensen, 2007). This convergence is acknowledged. In science, however, new discoveries are made and theories drafted that challenge incumbent axioms; often resulting in more variety and not less (Popper, 1975). Through time, theories and bodies of thoughts transmute to better fit our curiosity; and if the theories become accepted and spread we might call them 'adopted' or 'fit' as they profit, migrate and survive. But if they are considered misleading, erroneous, ill-formed or non-contributory in comparison with alternative ideas they will be endangered. When ideas are further specialized, the substrate of principles that instruct, enable and constraint theorizing of specific phenomena will vary from earlier forms. In the evolution of scientific knowledge ideas and principles descend with modification in order to populate and conquer unresearched niches and be better equipped to provide answers to curious inquires over time.

The downside of increased specialization and variability in a number of divergent directions might be lack of mutual understanding across a wider field of research. Yet, in a research community that reward specialization and new ideas, the noteworthy endeavor to find relatedness and complementariness that unites is often missing. This paper argues that cross-fertilizing of branches (and standardization in some underlying commitments and principles) within the same wider theoretical approaches have great potential for further theorizing, and to spur new insights. But to better enable relatedness and complementariness it is seemingly necessary to first review affinity and connection between various branches within a wider body of thoughts to converge nomenclature, and more explicit expose converging themes.

Consistent with the trend in science towards more variety and not less, scholars today distributed across a wide range of management, marketing and general business research are using diverse elements and concepts presented as 'Darwinian' or 'Evolutionary'. Such "alternative" perspectives are often used to account for more dynamic and contextual ideas (e.g. Nelson and Winter, 1982). Still, the accounts of Darwinism and evolutionary ideas in business research come in assorted packages adapted to diverse audiences and inquiries, and hence serve as an illustrative example of neighboring branches in social science that seemingly are decoupled. In this paper, first a generalized interpretation of Darwinism is mapped out as a frame of reference and benchmark to guide the subsequent review of various branches in search of converging themes. It have become increasingly warranted in management and general business journals that Darwinism may be carrying insights that has great relevance for the future for both researchers and practitioners in business, as it is portrayed to have unique explanatory potential for contextual and process-oriented phenomena (Brennan, 2006, Breslin, 2011, Stoelhorst, 2008d).

While we today know that equilibriums often are momentary and many empirical phenomena and theoretical axioms are in states of flux, Darwinian concepts might have bearing far beyond biology (Hodgson and Knudsen, 2010a). For management and business research, this potential would likely be better utilized if some common characteristics can be advanced to make better use of complementarities in the distant Darwinian body of socio-economic theorizing, as each of them independently expose both explanatory strengths and gaps that might be bridged if we unravel converging themes. Hence, to show possible affinity; the objective motivating this paper is to examine the converging themes among different research branchings in management and related literatures that uses 'evolutionary' and 'Darwinian' frameworks and concepts.

2. Generalized Darwinism

In this section, Darwinism as an approach to study socio-economic transmutation is discussed, and a generalized interpretation of Darwinism is outlined. However, I start this discussion by clarify the difference between evolution and Darwinism and comment briefly on some common misconceptions.

'Evolution' is sometimes used synonymous with Darwinism. The term, however, derived from Latin's *volvere*, 'to roll' (Hodgson and Knudsen, 2006), has been used for longitudinal processes in various disciplines before Darwin published his *magnum opus* in 1859. While no author can invoke exclusive rights to 'Evolution', Darwinism has a more precise meaning. Darwin held that his theory aimed at explaining how processes of selective nonrandom preservation of attributes in a population (together with generation of new variation, which he admitted that he knew nothing about) will form new varieties; and that this process of stepwise adaptation to local environments leads to increased specialization derived from a generalized common origin. This is, in order for varieties to colonize new niches to ease competition and thrive (Darwin, 1859)(cf. finding a monopoly-like situation). As a benchmark for the reviewed selection of evolutionary business literature, hence, this paper draws on a generic Darwinian account of evolution (and not as progression or change in the broadest sense of 'Evolution').

When it comes to offering a set of unison principles, this noteworthy project of abstracting the central themes of Darwinism is far from finished. Neither in philosophy of science (Godfrey-Smith, 2009) nor in economics and business sciences (Hodgson and Knudsen, 2006, Stoelhorst, 2008b), researchers are in complete agreement on how Darwin's principles should be generalized to both retain explanatory power and, at the same time, be sufficiently universal to be applied to all evolutionary processes. The unfinished project comprises in management and related literatures at least two issues. First, whether a generalized Darwinism, disconnected from biology, can be abstracted from Darwin's theory and adequately capture what is general about all evolutionary processes (argued by, e.g., Aldrich *et al.*, 2008, Hodgson and Knudsen, 2006, Stoelhorst, 2008b), or whether such cross-border endeavors to find common ground are futile if the exercise to apply Darwinism in social science analogously follows the biological model (argued by, e.g., Buenstorf, 2006, Nelson, 2007, Witt, 2004). We might therefore wonder whether it is the use of Darwinian principles *per se* or the examination of biological theory in social science that the antagonists are critical of. Biology in the wake of Darwin's work has been elaborated with auxiliaries for 150 years where the integration of Mendel's genetics (i.e. "the biological synthesis" integrated with Darwinian biology in the 1930s and 1940s) and Weissmanism (stating that only information carried in the germ cells can be inherited by the offspring) are prime examples. Darwin (1859) did know that variation and retention mechanisms somehow must exist, but he was unable to give detailed explanations of these mechanisms. No Darwinian trademark can, hence, be given to mutations and genes. Contrastingly, generalizing Darwinism means to carve a framework based of central principles elaborated by Charles Darwin that can apply to any evolutionary process or system. It does not mean to be an attempt to squeeze biological frameworks into social science.

The defenders of the generalization project, have shown how these critics often conflate generalized Darwinism with biology and therefore failed to distinguish between Darwinism as a meta-theoretic framework that always need auxiliary theories to elaborate detailed explanations and Darwinism as a universal full-fledged theory that elaborate full explanations alone (Hodgson and Knudsen, 2006). On the contrary, all prime advocates accentuate that generalized Darwinism is warranted but never enough (Aldrich *et al.*, 2008, Stoelhorst, 2008a). Moreover, no advocate contradict the critic expressed by Nelson (2007, pp., p. 91) who claims that the "the structures and mechanisms that are involved in the evolution of human culture need to be identified and studied in their own right."

Both sides in this debate seemingly agree perfectly with this statement. Thus, much of what is meant as a criticism apparently misses the target: it is criticism on squeezing biology into management, but not a serious critic on the generic Darwinian principles.

Despite some remaining ambiguity, Stoelhorst (2008b, 2008c), Beinhocker (2006) and Hodgson and Knudsen (2010a) has not just shown that it is possible to generalize Darwinism, but also how it might be achieved. Until further notice, I accept therefore that it is possible, and residing with the "how to generalize" issues: units of analysis (what is evolving), ontological commitments, *explananda* (what it explain) and *explanantia* (how it explains).

Unit of analysis -- Given the widespread acceptance it seems unproblematic to claim that Darwinism concerns systems denoted as 'open', 'adaptive' and 'complex' (Hodgson, 2002, Stoelhorst, 2008a). *Open* refers to its interdependency with the environment that the system needs to commandeer material and energy from for its maintenance of functional integrity, and *adoptive* that the systems composition will change as a result of interactions. They are *complex* in that these dynamic systems' consists of multiple elements; i.e. subsystems and sub-subsystems that, themselves, could be the unit of analysis in a Darwinian explanation (Stoelhorst, 2008b). By including the word 'population' to the conceptualization of Darwinian systems, it accentuates that a Darwinian understanding of evolution must embrace understanding of the range of similar but not identical varieties that are competing, i.e. population thinking (Mayr, 1982). Contemporary advocates of the generalized version believe that Darwinian theories can apply to social and natural systems at multiple levels (Beinhocker, 2011, Godfrey-Smith, 2009, Stoelhorst, 2008b). While on different levels, organizations, and colonies of organizations, markets and even nations, and other non-biological systems could be considered to be open, complex and adaptive systems.

Ontological commitments – From the widely accepted Continuity thesis defined and defended by Witt (2003, 2004), Hogdson's (2002) notion of 'ontological similarity' (that evolution for all qualified systems share some universal features), and the theory of interdependent multi-level selection (Maynard Smith and Szathmary, 1997, Sober and Wilson, 1998), some shared underlying commitments that are fundamental to Darwinism could be suggested (cf. Hodgson, 2004, Klaes, 2004):

Evolutionary systems change (cf. species are not fixed, Darwin, 1859).
Change is somehow caused. Although this commitment to causal explanations does not postulate predictability or regularity, there is a commitment to search for causal explanations.
The Continuity thesis proposes that the Darwinian explanations must explain how the outcome at time t is derived from state of things at time t-1. The consequence of this principle is a commitment to explain how today's systems are path-dependently molded from earlier stages (Stoelhorst, 2008a, 2008b).
Change takes place at multiple interrelated levels which postulate 'system thinking' (Stoelhorst, 2008a, Stoelhorst, 2008b) and an need for a 'layered ontology' (Dopfer and Potts, 2004), a term that refers to the assumption that interrelated processes of change going on at multiple levels. System thinking requires that the focal unit is analyzed not in isolation, but rather as member of a wider system where sets of competing similar but non-identical units exist.

Explananda -- Darwinism generically has the following explananda: to explain i) variety from common origins, ii) adaptive fit, and iii) accumulation of complexity (Dennett, 1995, Maynard Smith, 1993). The first explanandum relates to Darwin's notion that specialized varieties had descended from more general common ancestors, and was commonly accepted in the community of natural researchers shortly after publication. Darwin's second contribution is the uncovering of a generic causal logic that could explain how a system through an "algorithmic" problem-solving procedure

becomes more adapted to the environment, and how this cumulatively leads to accumulation of complexity/specialization (Dennett, 1995, Stoelhorst, 2008b); i.e. solutions customized for each environment. According to Stoelhorst (2008b) it is the second and third explananda that makes Darwinism uniquely useful in management studies. Especially adoptive fit is considered as the key explanandum (Maynard Smith, 1993), while accumulation of complexity and customization of specialist systems from the more generalist systems are seen as products of adoptive fit in order to profiting on fitness advantages and avoid direct competition (Stoelhorst, 2008b).

Explanantia -- What a Darwinian explanation involves is a subject for a substantial number of publications. In essence, central to explain adoptive fit is the algorithmic-style triune; variation, selection and preservation (Campbell, 1965): The system itself enhance the variety in its repertoire of design and acting instructions (i.e. variation), while the system's interaction with the environment reduces this variety (i.e. selection; at least partly as a function of fitness and success, and not only randomly), and as a result store instructions privileged by selection (i.e. preservation). While mating and occurrence of new generations fulfill both the variation creating mechanism and preservation of instructions for instincts and structures in biology, nothing a priori says that these two logically distinct mechanisms have to be united. In strict generic terms, the preservation mechanism has only one job; to store information over time to maintain variety (Stoelhorst, 2008b)

To comply with the logics of a functional explanation (Elster, 1983), the Darwinian explanation must separate 'unit of selection of' (i.e. the system's design and interactions with the environment) from 'unit of selection for' (i.e. the system's "memory" or "codex" where instructions are stored) to establish a positive connection between the ability to make acts that is beneficial for a system, and the probability to repeat those actions in the future (Sober, 1984). The selection and preservation mechanisms punish disliked acts; non-randomly preserving instructions that allow the system to perform the approved acts; thereby, change the composition of instructions being stored, and codes for, future interactions (Stoelhorst, 2008b), leading towards adaptive fit. Putting it differently; systems that are the least successful in interaction with the environment have a lower chance to secure subsistence, and therefore will also the sets of instructions that codes for these least beneficial designs and actions gradually become less frequent in a population of comparable systems (Hodgson and Knudsen, 2004).

Moreover, in order to explain the accumulation of higher complexity from simpler forms (third explananda), multi-level selection logic is required in the explanations (Maynard Smith and Szathmary, 1997). Supra-systems can evolve when, and only when, mutualism and collaboration such as through improved complementary allocation of resources, instead of hostile competition, appears to provide benefits for the parties in the between-group competition that in total helps each party to be more beneficial in competition between individual units of analysis (Stoelhorst, 2008c).

3. Contemporary Use of Evolutionary Ideas

In view of the generalized Darwinism outlined in the previous section, I will in the present section look at how various parts of the Darwinian framework has been interpreted and used in management and related studies. Literatures applying Darwinian analysis in management and related studies can be cataloged into "branches" in terms of aim, level of analysis, mechanism(s) stressed, and auxiliary literature used. Only research focusing levels of analysis exceeding the individuals (e.g. the firm and the market) is included in this paper, and the following branches are reviewed: Socio-economic evolutionists in the tradition of Nelson and Winter, Institutional-evolutionary school in the tradition of Veblen, routine-centric and capability-centric literature, and

Ecologist perspective(s). My intention is not to review all kinds of literatures that use Darwinian ideas within the management and organizational sciences, but rather to expose some prime examples.

A line of distinction separates those branches who study the evolution of firms from those who study evolution of sectors or markets (where firms are components). Known for its employment of computer-based simulation models, scholars in the Nelson-Winter's (NW) ***Evolutionary economic change*** tradition aim to explore from cases and simulations regularities in the processes of change by which markets and technologies change, and predict outcomes, based on some known and stochastic input variables (Dosi and Nelson, 1994, Nelson and Winter, 1982, 2002). NW-traditionalists tend to have a specific industry as their system of attention, conceptualizing an industry as a population of firms that compete based on R&D spending and technological gains. By means of biological analogy (rather than drawing on a shared Darwinian ontology) they assumes firm routines to have the "selection-for"-role to instruct behavior and store productive instructions. Moreover, at least in their 1982 thoughts, they were explicit in borrowing principles of 'natural selection', biology-like conceptualizations of variation and retention included, to explain industrial and technological transitions. In essence, it avoids a serious debate on the generalized Darwinism, and the preservation and variation mechanisms in the single firm, addressing that biology sometimes might be a good source of inspiration/starting-point where routines-as-genes (copied with some fidelity) is a heuristic; but other than that is the NW-framework not explicit Darwinian[1].

While the NW tradition sheds light on economic selection pressure on population-level dispositions, it downplay the social/institutional selection pressures, e.g. from peers, legitimacy seeking, and authorities. Still on the population level, the **Ecological perspectives** in organizational studies address this gap. In sum, this branch studies molding of organizational forms in course of time in different environments, including both economical and institutional pressures. Hannan and Freeman's (1977) conceptualization of organizational form evolution focuses, mainly, on the selection mechanism based on fit to environment within sets of similar but not-identical organizations – in a process logically equivalent to Darwin's conceptualization of selection. The ecological perspectives bring the importance of the changing environment in; and it assume that firm and market design gradually through selective preservation will be adapted to relevant externalities. While assuming that firms are, more or less, inert and historically tied to past and present investments, technologies and knowledge (i.e. cannot control its own variation endeavors), organizational ecologists have e.g. elaborated theories about how fluctuation in 'population density' (Ruef, 2000, Ruef, 2004) or how resource partitioning of a market is depend on market concentration (Carroll, 1985). Most ecologists assume that variations somehow are introduced in the population from new firms, but downplay the details of variation mechanisms. Widening the system of analysis further, Ruef (2000) introduced 'community ecology' into organizational science. It means studying how interrelated firm types (manufacturer, distributors, and etcetera) down the value chain operate under institutional pressure in molding of inter-organizational forms. Accentuating mutualism, commensalism, and parasitism as important terms, Ruef's group of scholars will for example explain emergence of new cooperative solutions that can profit from populating a niche less exposed to competition (cf. Darwin, 1859, on niches in complex ecological systems) in line with the need for multi-level selection thinking. Yet, critics may argue the ecologists stress unilaterally that the environments cause the organizational forms, instead of highlighting the co-evolution and suitable match between variation creation from within and selection pressure from the outside world.

[1] In recent articles Nelson is skeptical towards the use of biological metaphors and analogies in business studies (Nelson, 2007)

Fellow collective-level researchers in the **Veblenian-Institutional tradition** set also out to explain how institutions, social power and conventions control habits and mentalities of the people. Scholars in this tradition count Thorstein Veblen as an important intellectual ancestor. Veblen (1899) could be read as one long argument for the multi-level selection, and how seemingly irrational conducts might well nourish the individual in its group as it helps to promote the group in between-group struggling (cf. Maynard Smith and Szathmary, 1997). Concerning commitment to the Darwinian explanantia, the recent central authors in Veblenian-Institutional tradition have elaborated an explicit account of Darwinism stressing variation, selection and retention (see, e.g. Hodgson and Knudsen, 2010b). Yet, details of the micro-foundations of the single firm are often missing.

This gap, although, might be filled by branches that have elaborated auxiliary theories drawn on concepts from routines, learning and capability approaches to organizational change. A key aspect of this literature is to explore how routines and capabilities (conscious and subconscious to owner) contains instructions that constrain and foster operational acts, innovative acts, and design of procedures and structures, where the micro-foundations are scrutinized (see, e.g., Becker *et al.*, 2006, Jacobides, 2006, Jacobides *et al.*, 2006). Bridging to the above mentioned branch, it has been demonstrated why Veblen also could be recognized as an ancestor to the competence-based views on firm evolution (Foss, 1998), and that bounded rationality should be more firmly integrated as a key concept in the organizational capability literature (Foss, 2003). Not explicit Darwinian, this call to arms for more realistic assumptions about the human agent share with a general interpretation of Darwinism the assumption that systems must rely on some history-dependent substrate (e.g. capabilities, institutions or routines) that instruct (enable and constrain) the behavioral repertoire. Yet, there are varieties within the micro-focused branches as well.

The **Evolutionary capability tradition** highlight the dynamic aspects of problem-solving, decision-making and aggregated outcomes in course of time from Neo-Schumpeterian or Neo-Simonian attacking points, to explain how competitive advantage for organizations is being built (internally and by intention) and sustained by collective learning, absorption and exploitation of productive knowledge. While Schumpeter could not solve how novelty emerges in a routine-based system (firm), Winter (2006) built a framework to answer that problem, and acknowledged two major sources of novelty: the combinatorics of routines and the unreliability of routine imitation.

Figure 1: A summary of five evolutionary branches reviewed

	Evolutionary economic change ("the NW tradition")	***Ecological perspectives***	***Institutional (Veblenian) tradition***	***Evolutionary capability tradition***	***Organizational routine literature***
Aims	Positive (with some normative implication)	Positive (with some normative implication)	Positive	Positive and Normative	Positive (with some normative implication)
Level of analysis	Sector and industry-wide technologies	Sector [Population ecology], or industry [Community ecology]	Community (population level)	Firm	Firm
Key Darwinian mechanism(s) being stressed	Selection (and variation)	Selection (and new form emergence)	Retention and Selection	Variation and retention (adaptation as a choice)	Retention (and variation)
Central authors	Nelson, Winter, Dosi	Hannan, Freeman, Ruef, Carroll	Veblen, Hodgson, Knudsen, (Foss)	Teece, Jacobides, Aldrich, (Winter), (Foss)	Becker, (Foss), (Knudsen)
Auxiliary theories (most used)	Schumpeterian theory, economy, (biology)	Sociology, ecology, (institutional theory)	Institutional theory, theory on routines	RBV, Penrosean, Schumpeterian, and cognitive theory	Organizational behavior theory, psychology, learning theory
Substrate coding for system's procedures and designs	"Routines-as-gene" is an heuristic	not present (or Implicit)	Organizational routines (as genotypical dispositions)	Capabilities and knowledge	Routines-as-rules, Routines-as-actions, "best practice"
Darwinian traits	Mostly analogous to evolutionary biology	Mostly ontological, and implicit or explicit	Ontological and explicit	Various; seldom explicit use of Darwinism	Mostly implicit

In contrast, the focus in **organizational routine literature** is less normative and management focused, while it draws more on related concepts from psychology and behavioral aspects to explain organizational modifications (see, e.g., Becker and Zerpoli, 2008), and on the puzzling of understanding variation mechanisms (Becker et al., 2006); in Darwinian words how variation is replenished. However, these issues are closely related to some of Hodgson's and Knudsen's work (2010b), which underline the problem of separate these research branches as they sometimes overlap, reuse theories and also investigate similar phenomena. Yet, the shared converging themes are not explicit, as the unifying Darwinism is not present or implicit.

4. Discussion

Each branch that studies socio-economic and organizational evolution that draws on, or borrows ideas from, Darwin's theory has distinguishing ambitions, which (although sometimes overlapping and cross-fertilizing) embrace a variety of specific economic phenomena at different levels of attention. However, as the review expose, many of them materialize aspects of abstracted records of Darwinism. Some researchers are explicit in the use of the full triune, while other merely focuses one out of three the mechanisms to explain empirical phenomena. These may explain selection, but not evolution. As shown above, merely selection is not enough to comply with the logics of a functional explanation to which Darwinism is devoted. For evolution not to come to a halt --

variation, selection and retention must be explained (e.g. selection without variation creation leads to an empty set).

Concerning then the distinction between the system's interactions (and designs) and the instructions that code for them, is somewhat accentuated, at least in the firm-centric approaches (cf. Feldman and Pentland, 2003, while not being explicit 'Darwinian' it uses a similar logic making distinction between regulative/instructive aspects of routines and the actions performed).

Moreover, being committed to system thinking, a full Darwinian story needs an examination of interrelated processes of change going on at multiple levels, relating the evolution of the focal system to the evolution of the wider environment (supra-system) that the system inhabits. Combining frameworks from both population-level and firm-level branches, we might come up with multi-leveled co-evolutionary explanations. It is, hence, possible, and fair, to argue that these distant explanations will be stronger if they are cross-fertilized with findings and assumptions stressing complementary mechanisms and co-evolutionism. A full Darwinian story of firm evolution might, as I see it, be examined if we combine details from these various branches and incorporate these upon one converging framework. This converging framework must surely be very close to "Generalized Darwinism" as it is described above.

I think that the potential to unite is good, as the branches reviewed share the focus on creating positive theory; to inquire "what is", "how did it happen" and similar kinds of positive questions. Few of these questions contain indication of approval or disapproval (normative questions). Darwinists attempt to explain what happened, although some scholars use their results to outline normative guides and implications. It must be noted that Darwinism *per se* is a set of positive theories, where the outcome of selection has no teleology and no divine power in any particular direction (Browne, 2006); and it is neither "moral" nor "just" (Hodgson and Knudsen, 2010a).

To sum up: Seemingly, today's assorted evolutionary branches are related upon the older and more general records of Darwinism. But through time each one of them has been fertilized by auxiliary explanations specific to each question, and thence evolved in different directions. An interesting question for further research is whether also the theories of Schumpeter, Penrose, and Simon (three authors often cited in the selected publications reviewed) should be considered as descendants of Darwinian principles, or considered as compatible auxiliary theories to the reviewed branches. For example, some interpreters stress that Schumpeter is not only compatible with Darwinism, but share and express the generalized Darwinian ontological commitments and explanantia as new innovations (variation) in a system's instructions forces some of the existing and competing alternatives to lose positions and struggle for their existence (Fagerberg, 2003, Kelm, 1997).

5. Better Bearing Through Amalgamation?

The paper has addressed affinity and advocates that generalized records of Darwinism demonstrate a framework that could amalgamate some, broadly defined 'Evolutionary' branches of management (and related) research upon a shared body of commitments and generic explananda and explanantia. This result shed lights not only on the possibility to unite divergent research directions, but on the relevance for future research in the light of better communication and cross-fertilization. Breslin (2011) argue that a major obstacle to extend the use of evolutionary ideas in our domains is the lack of conceptual consensus leading to miscommunication and mislead critic. Hence, in trying to standardize the use of concepts upon a shared generic framework perhaps the greatest benefit is to facilitate cross-fertilizing and spread of ideas across the whole body of evolutionary thoughts in

management and related domains in order to more firmly explain the multi-leveled evolution of procedures and structure in firms and markets.

Although such amalgamation based on affinity is impelled, it does not seem uncomplicated to convince the skeptical by writing more conceptual papers on how we might generalize Darwinism. Such a crusade has been ongoing during the last decade without given rise to much wider acceptance. Instead, I will argue that for the future it might be more warranted to combine from various evolutionary branches to better explain specific empirical phenomena within the domain of management. This is needed to examine how a body of evolutionary thoughts converging upon generalized Darwinism can provides answers to real empirical questions about nature, evolution and origin of organizational procedures and designs which previously have been left unanswered or ignored. Indeed, only when we have combined the various theories and tried them together we will actually know if it provides a relevant theory to explain real phenomena.

In essence, Darwinian principles literally may provide the framework that combine, bridge and organize the various evolutionary theories in order to lift the entire domain to higher levels of knowledge-building in a way similar to that Popper (1975) and Campbell (1974) postulated -- that scientific knowledge itself adopt fit and accumulates complexity by means of new variation and selective retention. Hence, using converging themes to standardize the generic theoretical and conceptual frameworks may paradoxically contribute to foster new insights and further adopt and customize the 'Evolutionary' and 'Darwinian' theories in management and related business studies to better fit our curiosity.

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Local or Global Packaging Design?

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Abstract

One integral part of the packaged product is its' packaging. In addition to serving a number of functional means, it is an essential mean to attract consumers' brand attention at the point of purchase. In the literature brand packaging is referred to as an extrinsic product cue (e.g., Mendez*et al.*, 2011), i.e. a cuenot influencing product performance in contrast to the intrinsic product cues. Yet, research shows that consumers' choices are not only based on the product itself, but also oncues that can be changed without changing the product (Miyazaki *et al.*, 2005).Indeed this is a challenge for the brand marketer as 70% of decisions are found to be made in store and 90% of the decisions are based on visual examination of the package (e.g. Clement, 2007; Inman *et al*., 2009).

The aim of the current study was to explore the impact of packaging cues on consumers' product preferences. In the study packaging is referred to as a media that influences choices through its various extrinsic cues, i.e. verbal (e.g. COO, manufacturer), numerical (e.g. price), and cues that stimulates consumers' senses such as touch (e.g. material, shape) and sight (e.g. color, shape, letter font). The varying impact of verbal and numerical cues is acknowledged in cross-country studies (e.g. Pecotich and Ward, 2007), whereas the impact of cues influencing senses has received less scholarly attention (*Swahn* et al., 2012).

The current study contributes to the field by focusing on the impact of packaging's sense-cues in a cross-country context, i.e. color, shape and letter font. A sample of 98 Finnish, 30 American, 30 Ghanaian, 52 Mongolian, 103 South-African respondents ranked 16 experimental packages in two product groups. The results of the two conjoint studies show similarities and dissimilarities in consumers' preferences across the two product types and across the five countries. The results suggest that some cues are local, whereas others are global, i.e. some cues benefit from being designed from local perspectives, while others can be standardized. Indeed global brand owners benefit from paying attention to the local impact of the various cues on packaging. One of the most essential sense-cue was color, and the study particularly stress the need to understand the impact of color and the multi-functions color play on brand packaging at the point of purchase.

Keywords

Aesthetics, attention, color, communication, packaging

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Standardized CSR

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Abstract

To identify, monitor and control CSR activities in business relations, a certain level of standardization must be available. Thus targets can be set, results compared and indirectly the sensitivity of vendors towards environmental and social issues increased.

Keywords

Corporate Social Responsibility, standards, standardized supply chain sustainability, CSR audit

Corporate Social Responsibility

The new CSR policy of the European Commission states that to fully meet their social responsibility, enterprises "should have in place a process to integrate social, environmental, ethical and human rights concerns into their business operations and core strategy in close collaboration with their stakeholders".[1]

Today when information is spreading fast and is easily accessible, manufacturers are expected to fully disclose where they source their products, or they will face a PR backlash. No customer wants to support child labor or environmental pollution. In some cases it might be enough to damage the company's image if CSR activities are neglected. People generally react suspiciously if a market player remains silent. To become transparent several initiatives go towards standards.

Standardization Initiatives within CSR

GRI's Sustainability Reporting Framework for instance enables all companies and organizations to measure and report their sustainability performance. By reporting transparently and with accountability, organizations can increase the trust that stakeholders have in them, and in the global economy.[2]

The standard ISO26000 offers guidance on socially responsible behavior and possible actions. As a guidance document the standard is just an offer, voluntary in use. It encourages organizations to discuss their social responsibility issues and possible actions with relevant stakeholders.[3]

AA1000 Series of Standards released by the organization AccountAbility is helping organizations become more accountable, responsible and sustainable.[4] They are open source frameworks developed through a multi-stakeholder consultation and review process.

Maybe the most comprehensive guidance though is provided by UNGC the United Nations Global Compact. The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labor, environment and anti-corruption.[5]

Global Compact has shaped an initiative that provides collaborative solutions to the most fundamental challenges facing both business and society. It deals both with global and local issues from private and public sector. Participation is voluntary though it has benefits:

- provides a policy framework for the development, implementation, and disclosure of environmental, social, and governance policies and practices;
- shares best practices to manage common challenges,
- involves a wide range of stakeholders including UN agencies, governments, civil society, labor, and other non-business interests;
- establishes a collaborating global network of business units and subsidiaries across the value chain
- makes an extensive database accessible on sustainability and development issues and
- provides standardized management tools and resources to act effectively in the environmental, social and governance realms.

Standardized Supply Chain Sustainability

Supply chain sustainability is increasingly recognized as a key component of corporate responsibility, and customers and investors are beginning to set expectations for enterprises. These additional expectations may be found in contract terms with suppliers or implicit in supply relationships. Effective management of the social, environmental and economic impacts of supply chains makes good business sense, but the challenge to comply with existing and emerging regulations, meet stakeholder expectations and reach internal sustainability goals. Supply chain sustainability is the management of environmental, social and economic impacts, and the encouragement of good governance practices, throughout the lifecycles of goods and services. The objective of supply chain sustainability is to create, protect and grow long-term value for all stakeholders involved in bringing products and services to market.[5]

Generally to maintain the sustainability a company's supply chain, the following steps need to be considered:

1. Commit – understanding the external landscape
2. Access – map the entire supply chain a company has
3. Define – the key elements of the codes of conducts
4. Implement – make resources and management support available
5. Measure – set clear goals, distribute responsibilities and follow up the fulfillment
6. Communicate – the progress and do regular reporting

Picture 1: Supply Chain Sustainability Cycle - United Nations Global Compact

Source: www.unglobalcompact.org/docs/issues (June 8, 2012)

Based on a case study of UN Global Compact[6], incorporating environmental, social and governance considerations into supply chain management can probably deliver business benefits like:

Better risk management, reduced operational risks; "social" license to operate within communities, reduced costs and enhanced efficiency and productivity; improved working conditions can reduce turnover and improve quality and reliability; environmental responsibility improves efficiency and profitability; corporate brand and values, and customer and consumer confidence and loyalty are

protected and enhanced; process and product innovation; empowered suppliers uncover opportunities for developing sustainable products and services; good supply chain management can increase shareholder value. Corporate buying practices can impact suppliers' ability to improve their business conduct. Downward pressure on cost and efficiency can force suppliers to contravene some of their own ESG standards in order to meet their buyers' commercial requirements. At the opposite end of the scale, companies can use their purchasing power to help instill good ESG practices in small and medium-sized companies across the developing world.

Today, successful supply chain managers must increasingly think beyond short-term financial considerations to building relationships that can deliver long-term value along the entire supply chain. This includes incorporating sustainability issues into the company's sourcing and purchasing practices. In fact, companies that do engage with their suppliers around these issues constitute one of the most important drivers for spreading corporate citizenship principles around the world.

One standardized toolkit provided by UNGC for sustainable cooperation along the supply chain is considering the scope of engagement. The standard approach describes 4 levels of supplier engagement on sustainability:

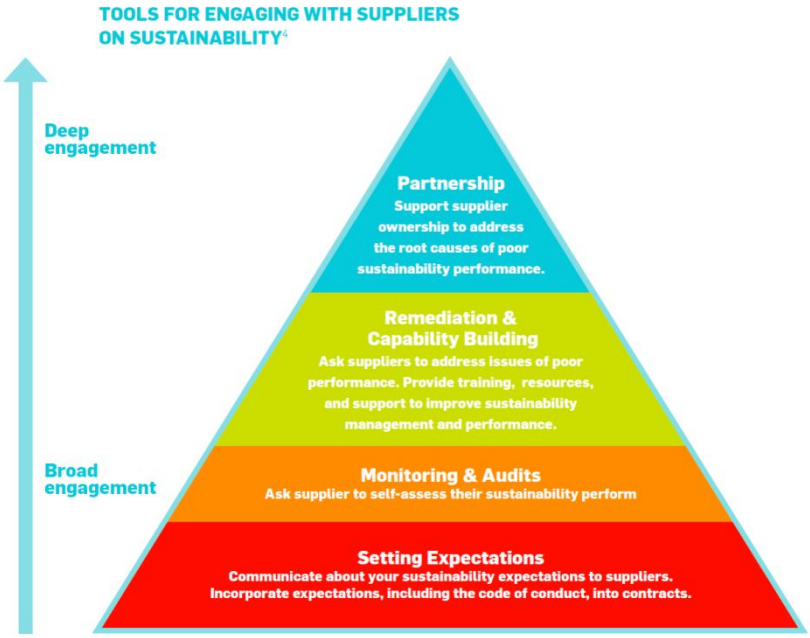
Level 1: set expectations - communicate about your sustainability expectations to suppliers; incorporate expectations, including the code of conduct into contracts

Level 2: monitoring and auditing - ask supplier to self-assess their sustainability perform

Level 3: remediation and capability building - ask suppliers to address issues of poor performance; provide training, resources, and support to improve sustainability management and performance

Level 4: partnership - support supplier ownership to address the root causes of poor

Picture 2: Overview of Tools for Engaging With Suppliers on Sustainability - United Nations



Source: www.unglobalcompact.org/docs/issues (June 8, 2012)

The different players in the supply chain are at different tiers in the production process, and each has different capabilities and incentives to implement a given CSR program, making management of the

supply chain increasingly intricate. Management aside, the issue becomes complex due to the pressure from multiple stakeholders requiring the corporation to be more responsible through the lifecycle of the product. The pressure from some quarters is to ensure a sustainable product lifecycle, from environmental and social impacts arising from material extraction and manufacturing, to product use and disposal. This is a challenging task that requires additional company investment. Monitoring suppliers from around the world requires significant financial and human resources. Partly as a response to CSR pressures, but partly also for competitiveness reasons, the overall trend is to collapse the supply chain and develop longer-term relations with a smaller number of suppliers.

Where cost control of CSR initiatives is a priority, on-site monitoring by external independent firms can reduce costs by streamlining the travel and maintenance of large internal departments of company auditors[7]. Industrial cooperation with standardized management tools can also help to share costs and risks.

Implementation of good social and environmental practices though will not survive in the long term if owners, managers, and supervisors along the supply chain are not convinced of the benefits of CSR.

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CSR Standards

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Abstract

CSR is a business model which promotes business contributions to sustainable development i.e, it creates a balance between economic interests, environmental needs and social expectations by integrating emphasis on environmental and social interrelationships, stakeholder approach, ethical behavior and volunteering into a business strategy.

Due to its positive effects CSR has become a global conception applied by many companies around the world. There is a need to measure, control and verify CSR activities of the companies, and to report the results to internal and external stakeholders. CSR standards are special methods of this process. The article summarizes the features of the common applied CSR standards and presents examples from the business life.

Keywords

Business ethics, corporate ethics, corporate social responsibility, CSR standards, ethics standards

Content of CSR

The Corporate Social Responsibility is not a new phenomenon. Since the root in the 1960s, the meaning and definition of CSR has changed essentially. Today it is not only a widely discussed issue in the academic sphere but an actual challenge in the practical business life as well.

Corporate Social Responsibility has not a generally accepted definition: ''corporate social responsibility means something, but not always the same thing to everybody. To some it conveys the idea of legal responsibility or liability; to others, it means socially responsible behavior in the ethical sense; to still others, the meaning transmitted is that of 'responsible for' in a causal mode; many simply equate it with a charitable contribution; some take it to mean socially conscious; many of those who embrace it most fervently see it as a mere synonym for legitimacy in the context of belonging or being proper or valid; a few see a sort of fiduciary duty imposing higher standards of behavior on businessmen than on citizens at large'' (Votaw, 1972, pp. 25).

The concept of Corporate Social Responsibility (CSR) has been a topic of a number of publications. Based on several publications Garriga and Mele (2004) summarized the main CSR theories and approaches in four groups: instrumental theories, political theories, integrative theories and ethical theories. Within instrumental theories CSR is only an instrument of the company for wealth creation, and the company tries to achieve only economic results with its social activities. Political theories deal with the responsible use of power of corporations in society. In integrative theories the corporation is focused on the satisfaction of social demands and the basis of ethical theories is the ethical responsibility of corporations to society.

After summarizing the definitions, it can be concluded that "CSR is a business model which promotes business contributions to sustainable development i.e, it creates a balance between economic interests, environmental needs and social expectations by integrating the following components into a business strategy:

- **Emphasis on environmental and social interrelationships** – corporations operate in the environment and society in an integrated form. They take into account the impact their operations have on the environment and society and they want to exert a favorable effect on evolution. Some publications and corporations lay more emphasis on this component and prefer using the term Good Corporate Citizenship.
- **Stakeholder approach** – during their operations companies make efforts to take into account the interests of shareholders and stakeholders. As all the participants concerned have an interest in the responsible behavior of companies, the term Corporate Responsibility (CR) has been in use instead of Corporate Social Responsibility (CSR) recently because it reflects a broader approach.
- **Ethical behavior** – the concept of CSR does not only take into account the impact of corporate operations on the communities concerned, but it also stresses the need for ethical behavior which respects the interests and values of these communities. Some papers consider CSR and business ethics as synonyms. Several experts think CSR is the expression of the business ethics in corporate practice (Institute of Business Ethics, 2012).
- **Volunteering** – having acknowledged their responsibilities, companies then decide to assume them on a voluntary basis. Volunteering reflects their commitments and provides them and the communities involved with opportunities to apply the most favorable instruments. Taking into account practical elements, a system giving rise to CSR or controlling it does not exist. However, this does not mean that CSR cannot be motivated by government regulations or community expectations." (Szegedi, 2010:1)

In the last decades CSR showed a huge development in theory, research and practice as well. Mühle (2010:17) emphasizes that CSR has become from a limited local idea a global conception used by many actors from politics, civil society and also from business. According to Carroll and Buchholtz (2003) "CSR is increasingly becoming a global concern, the differences in societal expectations around the world can be expected to lessen in the coming years." Principles of CSR are increasingly being applied by many companies around the world. "CSR has moved from ideology to reality" (Du-Swaen-Lindgreen-Sen, 2012:1). According to the mentioned authors the reason of the widespread CSR efforts are not only the ideological thinking but the positive effects of CSR engagement.

According to the literature, the advantages that corporate social responsibility may have are as follows (Szegedi, 2010, pp. 70):

- improving image, multiplying PR and advertising opportunities
- reducing social and environmental risks, prevention of scandals, decreasing criticism from civil organizations and others concerned enhancing corporate reputation
- becoming a more attractive company for a well qualified and trained labor force
- improving morale and conditions at work, resulting in a more committed, productive, innovative, loyal and content work force
- increasing transparency for customers by means of responsible trade
- upgrading corporate brands
- attracting loyal customers
- developing mutually beneficial partnership collaborations based on trust and common scales of values, resulting in new business opportunities, new markets and an increase in innovation productivity
- promoting greater transparency of corporate processes, resulting in an increase in the feelings of satisfaction of stakeholders and investors, and also resulting in greater interest in the company
- developing good relationships with government
- regulators, authorities, the public and, especially, with the media
- contributing to the development of a more stable global market
- creating corporate values arousing trust, as a result of which the national and international competitiveness of major corporations will increase

Assessment of Corporate Social Responsibility

Since the 1990s the literature has begin to deal intensively with the conception of Corporate Social Performance. „Assessing a company's social performance, the researcher would examine the degree to which principles of social responsibility motivate actions taken on behalf of the company, the degree to which the firm makes use of socially responsible processes, the existence and nature of policies and programs designed to manage the firm's societal relationships, and the social impacts (i.e. observable outcomes) of the firm's actions, programs, and policies" (Wood, 1991:693).

Within a social/ethical audit process companies would like to measure, control and verify their CSR activities, and to report the results to internal and external stakeholders (Agle-Kelley, 2001). Regarding the connection between CSR and CSP several authors emphasizes that „CSR deals with activities and CSP deals with outcomes, but the main problem, that there is no agreement regarding what and how Corporate Social Performance should be measured. In addition organizations often report activities and not outcomes using different methods (Salazar- Husted– Biehl, 2012:176).

There are several organizations which assess the CSR performance of the companies. For example oekom research is one of the leading independent rating agencies worldwide in the field of CSR,

which has over 18 years experience. Its corporate ratings are based on a scientifically developed list of criteria and have acquired an outstanding reputation among experts. The fourth, annual review of global corporate responsibility gives detailed results of the corporate responsibility rating of the around 3,100 companies. Table 1 contains the best companies in selected sectors (oekom , 2012).

Table 1: The best companies in selected sectors as at 31.12.2011; basis: oekom Universe

Sector	Best company 2011	Country	Rank 2010	Best company 2010	Country
Auto Components	Johnson Controls	US	2	Denso	JP
Automobile	Renault	FR	1	Renault	FR
Chemicals	BASF	DE	1	BASF	DE
Commercial Banks	HVB Group	DE	1	HVB Group	DE
Construction	Berkeley Group	GB	1	Berkeley Group	GB
Consumer Electronics	Sony	JP	3	Electrolux	SE
Food & Beverages	Coca Cola Hellenic Bottling	GR	1	Coca Cola Hellenic Bottling	GR
Household Products	Henkel	DE	1	Henkel	DE
Insurance	Standard Life	GB	1	Standard Life	GB
Internet & Software	IBM	US	1	IBM	US
Machinery	Volvo	SE	2	Atlas Copco	SE
Media	Reed Elsevier	GB	1	Reed Elsevier	GB
Metals & Mining	Norsk Hydro	NO	1	Norsk Hydro	NO
Oil & Gas	OMV	AT	1	OMV	AT
Paper & Forest	Stora Enso	FI	3	Svenska Cellulosa	SE
Pharmaceuticals	GlaxoSmithKline	GB	1	GlaxoSmithKline	GB
Real Estate	British Land	GB	1	British Land	GB
Retail	Coop Genossenschaft	CH	new	Migros Genossenschaft	CH
Telecommunications	BT Group	GB	2	Vodafone	GB
Utilities	Terna Rete Elettrica Nazionale	IT	1	Terna Rete Elettrica Nazionale	IT

Source: oekom, 2012, pp. 27.

Main CSR Standards

CSR standards provide special possibility to evaluate and report corporate social performance. A variety of voluntary social and environmental and CSR standards have appeared during the past decades. This chapter introduces the most common CSR standards. Table 2 contains the main features of them.

AA1000 Framework

A principle based standards of an independent, global, non-profit organization working in a multi-stakeholder network, for helping market players to become more accountable, responsible and sustainable.

Indicators, targets and reporting systems are generated as a result of stakeholder engagement, this way assuring the effectiveness of this approach. In this accountability framework no targets are set, just potential revealed. Tension between stakeholders is not solved, but engagement to find a basis for effective cooperation is generated. The principles assuring the quality of the process: social accountability; inclusivity in addressing all stakeholders, letting them hear their voice without consequences; completeness, materiality and responsiveness.

Introducing this standard, open a dialogue about sustainability between stakeholders and improves business performance. Extending to the supply chain it creates value-oriented partnerships between market players. Exemplarily some companies benefiting from the use of this standard: Timberland, McDonalds, Pfizer (Accountability, 2012).

GRI Guidelines

GRI is a globally applicable sustainability reporting guidelines, voluntary accounting framework for corporations for creating indicators of a company's economic, social and environmental influence. Covers all main stakeholder groups, but also addresses general issues as human rights. Reporting process and content is defined, no target values are set. Systematic indicators link the companies' performance from micro- to macro-level, cross-cutting indicators connect different sustainability elements.

Its indicators combine economic, social and environmental criteria, serve as a management tools, set clear direction for the operative level and translates the desired trends of stakeholders into KPIs. Exemplarily some companies benefiting from the use of this standard: The Coca-Cola Company (Coca-Cola, 2012) and HEAG Südhessische Energie AG (Ad Hoc News, 2010).

Table 2: Main characteristic features of the CSR standards

Types of standards and issues covered	ILO Conventions	UN Declaration of Human Rights	OECD Guidelines for Multinationals	Ethical Trading Initiative Base Code	GoodCorporation	UN Global Compact	GRI Guidelines	AA1000 Framework	SA8000	ISO 26000
Year of release	1920-2001	1948	1976	1998	2000	2000	2000	2008	2008	2010
Type of Standard										
Auditable Standard or Framework				x	x		x	x	x	
Membership based, signatory standards				x		x				x
International Conventions	x	x	x							
Features										
Applicable to all organisations	Where ratified	x	x		SME's		x	x		x
Covers all business functions	Labour	x	x	Supply	x		x	x	Labour	x
Internationally Recognised	x	x	OECD Countries			x	x	x	x	x
Compliance Based	x	x	x	x	x		x	x	x	
Requirement for Reporting / Disclosure						Partial	x	x		
Requirement for Stakeholder Engagement			x		Partial		x	x		x
Requirement for Performance Measurement			x				x	x		
Requirement for Governance / Management			x	x	x	x	x	x	x	x
Requirement for Embedded Values								x		x
Specific Issues Covered										
Stakeholder Dialogue / Engagement								x		x
Environmental Reference			x		x	x	x	x		x
Bribery and Corruption			x		x					x
Political Donations			x				x			x
Workplace / Employment	x	x	x	x	x	x	x	x	x	x
Health & Safety	x	x	x	x	x	x	x	x	x	x
Supply Chain			Limited ref	x	x		x	x	x	x
Employee Involvement	x				x		x	x		x
Training and People Development	x		x		x		x	x	x	x
Human Rights	x	x	x	x		x	x		x	x
Grievance/ Whistle Blowing			x	x					x	x
Marketing/ Advertising Practices			x		x					
Trading/Business Practices			x	x	x		x			x
Community Involvement					x		x	x		x
Restructuring			x							
Security		x	x				x			x
Sustainable development			x		x		x	x		x

Source: Smith, 2002 and the web pages of the standards

SA8000

A standard created by Social Accountability International (New York) about employment and working conditions. Stakeholders are employees and suppliers; the standard though also contains references about trade unions, NGOs, consumers and investors. Certification is voluntary, though - beyond compliance with local laws and codes - it presents the adaptation of ILO conventions about employment, of Universal Declaration of Human Rights and of The United Nations Convention on the Rights of the Child.

Incorporates the issues: Forced Labour, Child Labour, Freedom of Association, Collective Bargaining, Health and Safety, Minimum Wage, Living Wage, Discrimination Practices, Disciplinary Practices, Working Hours, Training.

During audit the auditee must prove SA800 standards are part of the management system, are regularly reviewed and subject to continuous improvement. After certification the products sold can wear the certification mark SA8000. Manufacturing facilities, suppliers or retailers may benefit from better acceptance by NGOs, trade unions and governments, have a positive image on the labor market, and have a marketing advantage at products sold under the label. Exemplarily some companies benefiting from the use of this standard: OMV Group (2012), TNT N.V. (2009) Perfetti Van Melle (2012).

The GoodCorporation

The GoodCorporation Standard is a regularly updated Standard developed by the Institute of Business Ethics. Principles in it define a framework for responsible management. The assessment focuses on four core issues: existence of fair policy, availability of a system for its implementation, evidence about its proper practice and a positive feedback of stakeholders, that the system is working and it is fair. Any organization can undergo an assessment and those that demonstrate working policies and practices in every area set out in the Standard will attain GoodCorporation Accreditation.

The GoodCorporation Standard covers 62 areas of management practice, broken down into six sections, each focusing on a stakeholder group: employees, customers, suppliers and subcontractors, community and environment, shareholders or other providers of finance, management commitment (IBE, 2010).

Exemplarily some companies benefiting from the use of this standard: L'Oréal Group, DHL Express – Deutsche Post, Telefónica, S.A., Nestlé S.A., Total S.A., O2- Telefonica Europe, AXA S.A., The British Land Company plc (Goodcorporatio, 2012).

Ethical Trading Initiative Base Code

Similarly to SA8000 it focuses on employment and working conditions, is based on ILO and UN standards, is a multi-constituency partnership companies, unions and NGOs.

Adaptation is verbatim of via incorporation into own code. Beyond compliance with national labor low the greatest protection to workers must be ensured. Key provisions of the law:

1. Employment is freely chosen.
2. Freedom of association and the right to collective bargaining is respected.
3. Working conditions are safe and hygienic.
4. Child labor shall not be used.
5. Living wages are paid.
6. Working hours are not excessive.
7. No discrimination is practiced.
8. Regular employment is provided.
9. No harsh or inhumane treatment is allowed.

Improvements are based on shared best practices, their adaptation is promoted via trainings, management procedures pricing and similar incentives. Verification is done a regular basis by 3rd party. Exemplarily some companies benefiting from the use of this standard: Marks&Spencer, Sainsbury's; Tesco; Tschibo GmbH; WH Smith (Ethicaltrade, 2012)

OECD Guidelines for Multinational Enterprises

This approach is a collection of recommendations from governments to Multinational Enterprises about responsible business conduct. It addresses general business practices, consistent with applicable laws though voluntary to follow. Stakeholders are the employees and consumers. OECD Guidelines cover most sustainability issues thus servers as basis for several other standards. Principles described here on employment, human rights, environment, information disclosure, combating bribery, consumer interests, science and technology competition and taxation show many similarities with UN Global Compact issues (OECD, 2012)

Global Compact

The UN Global Compact is the world's largest CSR initiative, which involves all relevant social actors: companies, governments, labor, civil society organizations. It has more than 8,000 participants, including over 6000 businesses in 135 countries around the world. The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labor, environment and anti-corruption.

The Ten Principles of the Global Compact (Global Compact, 2011):

Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights;
Principle 2: Make sure that they are not complicit in human rights abuses.
Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;

Principle 4: the elimination of all forms of forced and compulsory labor;
Principle 5: the effective abolition of child labor; and
Principle 6: the elimination of discrimination in respect of employment and occupation.
Principle 7: Businesses should support a precautionary approach to environmental challenges;
Principle 8: undertake initiatives to promote greater environmental responsibility; and
Principle 9: encourage the development and diffusion of environmentally friendly technologies.
Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.

ISO 26000

ISO 26000 serves as a guidance on socially responsible behavior and possible actions; it does not contain requirements, therefore -in contrast to ISO management system standards-, is not certifiable. The practical value of ISO 26000 might be considered as limited as it only provides a common understanding of social responsibility, it does not facilitate management routines and practices leading to social responsibility. The standard is offer, voluntary in use (ISO 26000, 2010).

Pros and Cons

AA1000 Framework
Strength: it is non-prescriptive.
Weakness: is at a relatively early stage of its development, not yet fully proven.

GRI Guidelines
Strength: implements sustainability reporting into management systems, combines economic, social and environmental aspects.
Weakness: increases pressure on CSR reporting, organizations may lose other key performance indicators from the focus.

SA8000
Strength: comprehensive approach of labor and employment issues also in developing countries.
Weakness: the accuracy of audit results a questionable, gives no space for labor organizations and trade unions for discussion about standards.

The GoodCorporation
Strength: a practical assessment approach against as GoodCorporation Standard or against a company's own statement of business principles.
Weakness: no open forum for best practice approaches .

Ethical Trading Initiative Base Code
Strength: embraced ILO and UN standards; clear implementation process, greater credibility.
Weakness: increased focus on processes for development and improvement.

OECD Guidelines for Multinational Enterprises
Strength: covers many sustainability issues, serves as a proved basis for further standards.
Weakness: issued by OECD countries, might not have legitimacy beyond.

Global Compact
Strength: main driver for standardization in sustainability issues.
Weakness: -

ISO26000
Strength: comprehensive overview of CSR issues.
Weakness: not certifiable.

In order to use appropriate standard companies should determine how effectively the company is dealing with corporate social responsibility issues, and how it knows its level of effectiveness, decide how an external standard will contribute to business goals (Smith, 2002). Global reporting standards are broader in scope but sometimes provide less guidance in how to implement them and operate at a level where legal support is very uneven. Difficulties in measuring of Corporate social Performance that social accounting standards are in constant revision for refinement and improvement The general advantage of standards is assurance by an independent judge and added value/improvement of process. (Greenwood-Kamoche, 2012).

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Standardization of Logistics Jobs in European Union – Freight Forwarder

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Abstract

Standardization of jobs results advantages of employers, employees and trainers as well: clear, unequivocal requirements and expectations, promotes the mobility, increased flexibility of labor market.

A project - called CENTRAL - was created in European Union in the frame of Leonardo da Vinci Program. CENTRAL aimed at to work out qualification reference and training modules for logistics jobs. Two jobs were selected: warehouse operator and freight forwarder.

This paper presents the results of the project in the case of freight forwarder. Researchers found that there are many differences in the existing qualification and exam requirements in European countries. The training modules they have worked out will be tested in the participating countries. These modules are accessible for the training institutes in other countries.

Keywords

CENTRAL Project, competences, freight forwarder, logistics, qualification

1. Introduction

As the size of European Union is extending, trade and logistics become more and more important. Fortunately activities in logistics – storage, transport – are more standardized worldwide than activities like production. Linked procedures such as order process, INCOTERM clauses are also standardized. Looking at these it is surprising, that requirements in training systems are different by countries. Table 1 shows some characteristics of freight forwarders in different countries.

Table 1: Characteristics of freight forwarder qualification in different countries

Country	Job title	Level of certificate	Duration of training
FR	Technicien(ne) Supérieur(e) en Transport Logistique option Transitaire Aérien et Maritime	FQR Level 3	2 years, 854 h
HU	Szállítmányozási ügyintéző	EQF: 4, ISCED: 4	Built in other qualification
IT	Spedizioniere	Level 5	600 h, 420 training in center (practical and theoretical), 180 internship
DE	Speditionskaufmann	Approx. Level 5	3-year dual training course
BE	Organisateur de Transport	not yet defined	n/a

The duration of training differs widely between the countries.

2. The Central Project

Competence research is carried out in most countries. (Veres et al, 1990; Helan-Le Roy et al, 1999; Sandberg, 2000; Sanghi, 2004;Pató, Kovács, 2006). There are efforts in European Union to work out common frameworks for jobs. (Kovács, Pató Lasseree, 2009, 2011; Kovács, Pató, 2010, 2011).

Advantages for employers:

- Easier to hire people from international labor market.
- International companies can use same job descriptions, requirements.
- In-house training can be the same in different countries.

Advantages for employees:

- Easier to find job in abroad.
- Sometimes higher qualification than just in the case of local requirements.

Trainers:

- Internationally recognized output.
- Chance for international participants

Central Project aimed at working out European level qualification reference for logistics jobs. It project can be seen as a kind of continuation of a previous project called NOVALOG. During NOVALOG we defined and described jobs in logistics, collected cases for innovations in logistics training and set up international training database (Kovács, Pató, 2010). CENTRAL is also based on wide European cooperation. It is true not only for the countries but the nature of participants. Consulting firms, research institutes, trainers, universities participate.

The changes occurring in logistics and transport sector give rise to increased demand for new skills. The existing certifications and training programs do not always provide a satisfactory response to the needs of employers and training bodies. Under AFT's (France) coordination we wishes to respond to

these issues within the framework of the CENTRAL project, in co-operation with European and multi-actor partners: ITL in Italy, DEKRA in Germany, the University of Pannonia in Hungary, FOREM in Belgium, Economic High School Ion Ghica in Romania, and Skills for Logistics in the UK.

Overall objectives:

- Draw up an inventory of logistics and transport jobs in Europe
- Prepare common job definitions
- Extend the NOVALOG approach, the result of a previous LEONARDO project, to all transport and logistics
- Better define the skills required for the most representative jobs
- Set up a European certification reference for the selected jobs
- Develop a training course design based on the above skills certification process which is linked to the ECVET system

Operational objectives:

1. Update the existing NOVALOG nomenclature for the representative logistics jobs
2. Extend the nomenclature to the representative transport jobs
3. Convert the nomenclature into an online database
4. Certify skills for a series of jobs by trying out the ECVET system and thereby provide a better response to the needs of employees and employers
5. Develop European training modules to increase skills in key jobs where the existing training offer has gaps. (One key job is freight forwarder.)
6. Transfer these innovations to the whole of the transport and logistics sector and to new countries

Results of the project:

- NOVALOG nomenclature to be perfected, extended to transport jobs, and converted into an online database
- A European certification reference, testing the ECVET system
- European training modules using transferrable credit points

Expected impacts:

- Structuring of logistics and transport jobs in Europe
- Establishing the correspondences between jobs in the various countries
- Harmonizing the definitions of trades in Europe
- Improving the training offer in our sector
- Cooperation, sharing of experiences and best practice between professionals Europe-wide
- Thanks to the harmonization of definitions of jobs and skills and European certification, the transnational mobility of professionals can be facilitated

The project will hold its closing conference in December 2012, which is open for the public. More information about the project can be found at -http://www.logisticsqualifications.eu/.

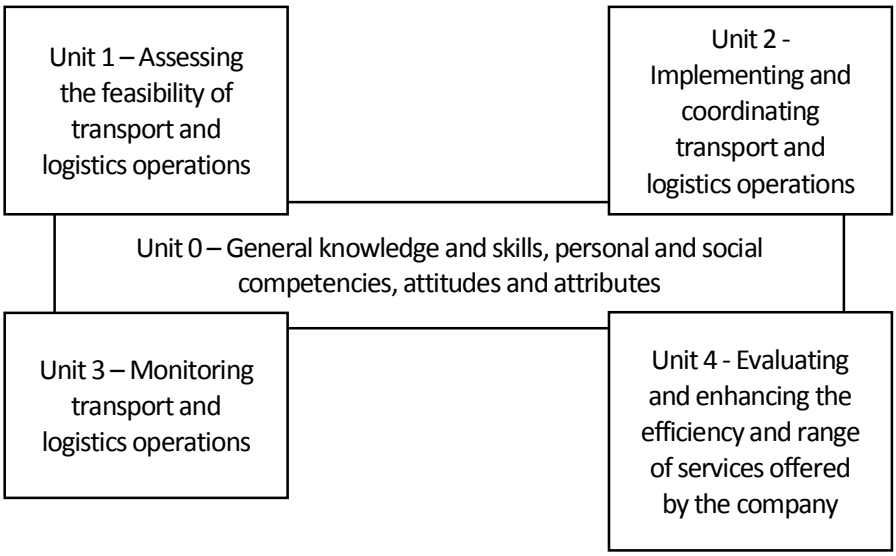
3. Qualification Reference

The bases for qualification reference are:

- Tasks
- Competences.

Widely accepted approach of competences is the KSA (knowledge, skills, abilities) model. (Veres, Locklear & Sims, 1990). Also there are studies related to competence requirements, competence profiles. (Bergenhenegouwen et al. 1997; Kovács, Pató, Elbert , 2011) CENTRAL classification of freight forwarders' job can be seen in Figure 1.

Figure 1: Tasks of warehouse operator (CENTRAL)



The basic nature of freight forwarders' job is the control of processes. They work autonomously and use the wide variety of resources in order to fulfill customers' need. They have responsibility for the quality of their own work and the others involved in the logistical chain. The competence profile worked out by CENTRAL researchers can be seen in Table 2.

Table 2: CENTRAL competence analysis of freight forwarder

Knowledge	Skills	Competence
He / she knows:	He / she is able to:	He / she is competent to:
Unit 0 – General knowledge and skills, personal and social competencies, attitudes and attributes		
• cost-calculation • the logistics market: transport modes, services and actors • contracts and main aspects of related regulation • INCOTERMS • quality assurance • goods, packaging, warehousing technology, logistics controlling • English language • relevant documentation • the range of services offered by their company and its structure and business specific areas of • traffic geography • supply-chain management and logistics • international trade • legal aspects of business transactions • finance (bank-related operations)	• use the company's ICT systems, standard software and workplace-specific software • assist in implementation of QA methods • correspond and communicate with business partners in English, process English language documents • consider cost- and time-effectiveness when planning and organizing his/her work • apply research methods •	• make well-informed decisions swiftly • organize his / her work and the work of others in an efficient and effective way • communicate effectively with customers and other departments • coordinate work with the rest of the team and other departments • act as an "entrepreneur" when conceiving new business plans and networking outside the company
Unit 1 – Assessing the feasibility of transport and logistics operations		
• regulations for the transport of goods (national and international) • regulations relating to customs, social practices, health and safety • environmental regulations • transport requirements • protocols and rules to comply with • customs procedures • research methods •	• identify customer requirements and provide support and advice to customers • calculate prices, including calculating and verifying elements that constitute the cost of a complex logistics service • develop offers • assist in creating networks to consolidate, dispatch and deliver goods • assist in the development of logistics concepts • apply research methods • collaborate in the calculation of costs and returns and in commercial control procedures • negotiate prices •	• consider economic aspects in his / her work (making use of opportunities to consolidate consignments into larger loading units) • take into account environmental aspects • conceive and implement transport solutions according to the needs of their company and its business partners • propose alternative solutions •
Unit 2 - Implementing and coordinating transport and logistics operations		
• fundamental principles of supply chain management • modes of transport • transport / logistics service contracts • sub-contracting and its regulations • Relevant documentation (national and international) • scheduling and planning methods • goods, packaging, warehousing technology, logistical control • traffic geography • the company's controlling and	• create, develop and close the file for shipments • organize shipping of goods to final destination by air, sea and land taking into account legal, environmental and economic concerns • design, direct and coordinate all operations needed to organize international freight transport • prepare documentation for goods transported • draw up contracts and supervise their implementation, with assistance of legal experts, if needed	• consider economic aspects in his / her work (making use of opportunities to consolidate consignments into larger loading units) • take into account environmental aspects • apply his / her communication and organizational skills in the coordination of people involved in the logistics chain • conceive and implement transport solutions according to customers' needs • act on behalf of the client when dealing with customs and / or other organizations •

documentation procedures • finance (bank-related operations)	• procure insurances for services rendered • take into account customs legislation and regulations governing cross-border trade • issue and check invoices and receipts • carry-out payment and dunning procedures • perform administrative tasks • identify and select potential sub-contractors	
Unit 3 – Monitoring transport and logistics operations		
• customs documentation • company-internal documentation procedures • insurance • traceability and its tools • management of incidents and unforeseen problems, procedures for crisis management	• document and verify goods' movements • implement appropriate safety and security procedures • control and monitor the cooperation of persons and institutions involved in the logistics chain • coordinate and control all services provided	• make well-informed decisions swiftly • apply his / her communication and organizational skills in the coordination of people involved in the logistics chain • respond adequately and appropriately to unforeseen problems
Unit 4 - Evaluating and enhancing the efficiency and range of services offered by the company		
• appropriate research and analysis methodologies • innovation in the transport and logistics market • general and company specific KPIs	• develop offers • identify and evaluate service offers on the transport and logistics market • monitor the market and play an active role in enhancing the range of services offered by their company • assist in creating networks to consolidate, dispatch and deliver goods • assist in the development of logistics concepts • optimize time and cost of transport • analyze and evaluate previous processes and costs, using KPIs	• self-organize and take initiative • network within and outside the company

4. Conclusion

Freight forwarder is one of the most complex job in logistics. (It is especially true in the case of traditional logistics concept, recently supply chain managers and administrators have a larger scope.) They arrange transport, storage, custom process of cargos on behalf of shippers. They provide a full range of services including: tracking inland transportation, preparation of shipping and export documents, warehousing, booking cargo space, negotiating freight charges, freight consolidation, cargo insurance, and filing of insurance claims. Freight forwarders usually ship under their own bills.

According this their job definition is complex, they are supposed to have wide variety of competences.
Standardization of this job is vital in European Union for the smooth domestic and international businesses. Results from CENTRAL Project will contribute to achieve this objective.

Acknowledgment

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Innovation Management for Small and Medium Enterprises - A Pleasant Tool to Get New Ideas for Product and Services

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Abstract

The most barriers to get new ideas for SME are: no time, no resources and the daily business – no chance for thinking out of the box. The 9-view screen is an easy tool to analyze my product/service, to know my customer and to get new ideas for new products/services to reach a safe future for my enterprise.

The first step is formulating my doing, my mean goal/target. What is the basic function of my product/service? The next two steps are to zoom in and to zoom out (thinking in space). Zoom in: what are my components? What are my resources I can use? The next step is to thin in time: what is the customer doing before using my product/service und what is he doing after using?

The same process must be worked out with my processes and my resources. The tool works efficient because the analyses and generation of new ideas goes parallel. You`ll get a new knowledge of your customer and your doing and by the way you will generate lots of ideas of new products and service. You become aware customer needs without a questionnaire.

In the contribution I will show a lot of practical examples how it works and reached benefits in several class of business.

Keywords

9-view-thinking, customer´s needs, thinking in space and time, analyzing, lot`s of ideas

The Impact of Brand Equity and Perceived Product Quality on Customer Loyalty

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Abstract

As a result of advanced technology and increasing interaction among people living in different countries, the world has become a global village. Marketers are eager to explore the opportunities in the global market. At the same time, risks in developing a new market are of concern to marketers. Among all the factors that would affect the acceptance of a brand in a new market, a brand with well-established reputation might have some advantages in its efforts to expand to a new market.

Branding has been recognized by both practitioners and researchers as one of the most important assets to a company and become a top management priority in the last decade (Keller & Lehmann, 2006; Raggio & Leone, 2007). In a competitive market, building long term relationships with customers has been a critical management issue that strategies are designed to reinforce customer satisfaction and loyalty. For consumers, satisfaction with the product and service will have a positive impact on whether to establish long-term relationships with the manufacturers, in which perceived product quality would contribute to this post-purchase evaluation. In addition, trust is viewed as the keystone and one of the most desired traits (Khan, Shahid & Akhtarf, 2009) that can foster the relationship bonding between the customer and the brand and/or the organization. Accordingly, the purpose of this study is to examine the effect of brand equity and perceived product quality on developing long term relationships with customers as indicated by their brand trust, satisfaction, and loyalty.

Eight hypotheses were developed based on literature review. Brand trust is argued to be a multidimensional construct which includes benevolence, integrity and competence, trustworthiness, credibility and, honesty of a brand (Li, et al., 2008). Since brand equity, a precursor of relationship building with the customer (Lundstrom & Dixit, 2008), is the cumulative experiences with a brand, it should help to form positive belief of reliability, safety, and honesty of the brand, which, in turn, enhance the trust toward the brand. Thus, a positive impact of brand equity on brand trust is hypothesized (H1).

Brand equity may be the source of favorably biased attribute perception (Park & Srinivasan, 1994). High brand equity can offset the negative effects when there are performance failures (Sloot, Verhoef, & Franses, 2005). H2 states that brand equity has a positive impact on customer satisfaction. Satisfaction can lead to trust when the brand consistently deliver its promises and take into account the customers' welfare (Selnes, 1998). Thus, customer satisfaction has a positive impact on brand trust (H3).

Researchers (Bloemer & Kasper, 1995) identified satisfaction as a primary influencer of customer loyalty. However, Delgado-Ballester and Munuera-Alemán (2001) argued that trust played a mediating role of the relationship between satisfaction and loyalty. They found that trust had a more

significant impact on loyalty than satisfaction did. The relationship between trust and loyalty is based on reciprocity, which means that the more a company wins consumers' trust, the more consumers will show loyalty to the company (Sirdeshmukh, Singh, & Sabol, 2002). Thus, brand trust has a positive impact on customer loyalty (H4).

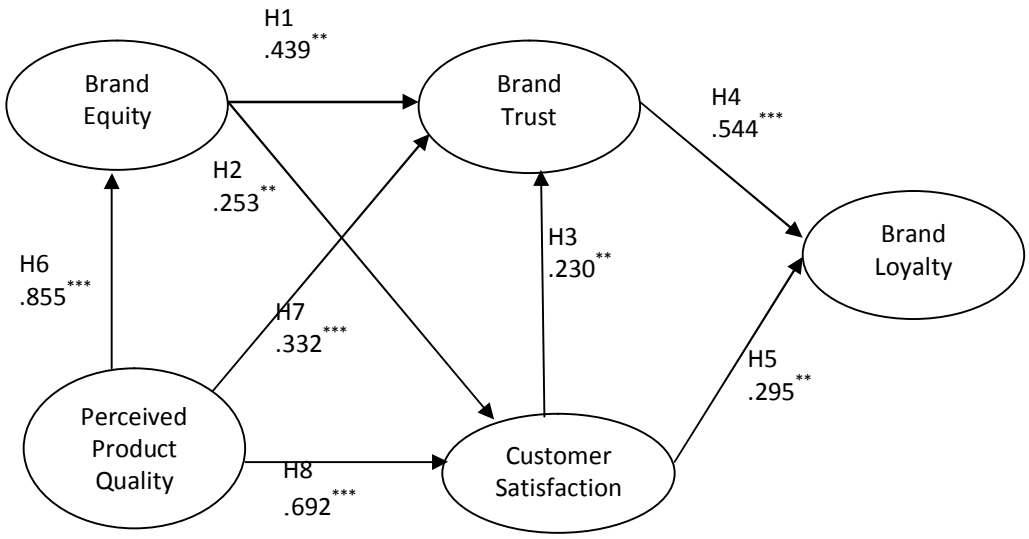
Loyalty is the cumulative satisfactory experience with the product or service. Through direct and pleasant interaction experience the customer could truly developed a positive effect on their loyalty toward the brand (Biedenbach & Marell, 2009). The higher the customer satisfaction is, the stronger the loyal relationship is between customers and companies, since customers would be much more willing to engage in repurchase intention, positive word-of-mouth communication and cross-purchases (Gounaris, Tzempelikos, & Chatzipanagiotou, 2007) and vice versa (Athanassopoulos, Gounaris & Stathakopoulos, 2001) (H5).

Consumers' product quality perceptions of brands influence their brand choice decision (Steenkamp, 1990) and future commitment (Porter, 1980). Accordingly, perceived product quality should have a positive impact on brand equity (H6) and a positive impact on brand trust (H7). Study showed that high perceived product quality will increase customer repurchase intention by maintaining high customer satisfaction (Kotler & Keller, 2006). H8 states that perceived product quality has a positive impact on customer satisfaction.

The independent variables were brand equity and perceived product quality. The dependent variables were customer satisfaction, brand trust, perceived product quality, and customer loyalty. A total of thirty-seven 7-point Likert scale items measuring these research variables were adopted from relevant literature (i.e., Yoo et al., 2000; Netemeyer et al., 2004; Li, et al., 2008; Raghunathan & Irwin, 2001). Cell phone and laptop were chosen to be the research products. A convenience sampling was applied to collect data by online questionnaire. Respondents were randomly assigned to one of the two experimental products and asked to fill out the questionnaire as instructed.

With the 366 valid responses, all hypotheses were tested with structural equation models and the results (see Figure 1 for the standardized coefficient of each hypothesized path) showed that hypotheses were all supported.

Figure 1: The results of SEM



χ^2= 232.808, *df*= 47, p=.000 , RMR=.059, GFI= .907, AGFI=0.846, **:p<.01, ***:p<.001

The results of this study are consistent with previous research (e.g., Athanassopoulos, Gounaris &

Stathakopoulos, 2001; Biedenbach & Marell, 2009; Delgado-Ballester & Munuera-Alemán, 2001; Ha & Perks, 2005; Lundstrom & Dixit, 2008; Doney & Cannon, 1997; Sirdeshmukh, Singh, & Sabol, 2002) that brand equity and perceived product quality are important influencers for brand trust and customer satisfaction, which, in turn, contribute to customer loyalty. In other words, quality product can contribute to brand value. In a global market, a well-established brand not only provides products that satisfy consumers' needs but also offers the image and symbolic meanings of social value, especially for highly socially visible products (Barwise & Robertson, 1992). The enduring efforts of marketers in building brand equity and quality product can create value for customers that generate long term relationships with customers.

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Business Ethics and How to Implement

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Abstract

Observing the relationship between business and ethics can be extended to the way of work, to the use of economic and natural resources, business management, ownership relations, relations with employees, work quality, attitude towards the local community, religion, country, the natural environment. There is also a dilemma as to whether business ethics is a matter of personal conscience of directors, managers, officers, or as a result of a joint and collective morality of a group, community, environment, society. In these times, marked as an era of globalization, the two confronted positions about the relationships between business and ethics are gaining in importance and require more complete response will be enriched with versatile multi-disciplinary research. It seems that, today, this question be actualized, and it becomes unavoidable, as in the developing and transitional countries, and in those most developed economies and socio-economic areas.

Keywords

Ethics, business, code, society, globalization

1. Introduction

In order to clarify doubts and to provide vocabulary that will be followed throughout the text of this work, we highlight some of the main definitions and descriptions of terms (Crane, D. Matten, 2007):

- ***Responsibility*** - the company effort to meet the demands and needs of the primary subjects of interest;
- ***Corporate citizen*** - Society-oriented company actions designed to demonstrate their role as a constructive social member;
- ***Corporate sustainability*** - Business operations that can be performed over longer periods of time without destruction of environment.

In common usage the terms "ethics" and "morality" they are often used in the same sense. In most cases, it is probably fair to say because this method does not use these terms highlights some major problems in communication and understanding things about business ethics. However, in order to clarify some of the arguments, many academic authors have pointed out the differences between these two notions. Therefore, the delimitation of the meaning of the concepts of ethics and morals certainly has a lot of comparisons and following what we feel is the best way to separate them.

Moral concerns norms, values, and beliefs embedded in social processes that define good and bad for the individual or society. The term ethics is linked to learning and morals and for a set of reasons that explain the specific rules and principles that define good and bad for the situation. These rules and principles are called ethical theories.

Ethics involves the assessment and application of moral values that society or culture accepts as its standard. To suggest that individuals define their own standards of behavior means to strive for moral anarchy. Certain satisfaction can be derived from compliance with a personal code of conduct, a violation of that code, but not necessarily open to serious ethical questions. (Dej; 2008; pp. 20)

Ethical behavior is largely based on good character. Although a good education can provide some sort of moral compass that can help individuals identify the right direction, and then follow the way the decision to do the right thing, then this is not the only factor that determines ethical behavior. Educational programs of business ethics can give shape and development of ethical values and behavior of young people.

The complexity of today's society requires that individuals need additional guidance. They need help to recognize the ethical dilemmas that will likely arise in their work, as well as rules, laws and norms that apply in this context. That way they can adopt strategies and use them to reach the best decisions.

With the growing globalization of business through travel and the use of the Internet around the world, a growing number of managers is in the worldwide environment full of ethical challenges. If the conduct of business activities with the challenge of ethical behavior in one's own culture, imagine how many difficulties requires management of the business environment in the culture and language. Individuals need to learn about the behavior of business in different cultures, as well as the broader organizational issues, whether and how to do business in foreign nations, and how to lead employees in a global business environment.

We live in a time of unprecedented change. In the business challenges we face and opportunities that are much more critical and more complex than ever - where the consequences of failure unthinkable, a noticeable impact of our decisions around the globe. Fragile economy and the climate out of control, poverty, over half the planet and the lack of natural resources, species extinction and population explosion, the ethical dilemmas at every turn and a low level of trust in business are the

symptoms of a changing world. It seems that the only constant is change and change is all around us. Help is required at the end of the industrial age, the change of power development, from large to small, but the fact that we can only keep our lives with new thinking, new behaviors and new balance. We struggle to balance our priorities and ambitions - a quest for personal and business success, as well as search the world a better place. Is it possible to achieve both?

Social and environmental issues are more important than ever. For businesses, they represent some of the greatest possibilities for finding new markets for profitable growth, even persistent and engaging sources of competitive advantage and effective ways to reduce cost and risk.

"What we miss most in life, is someone who would force us to do what we can." Ralph Waldo Emerson, 1803 - 1882, American philosopher

When business people talk about business ethics, the issue most often, start from the following assumptions: personal values and beliefs of wider social values, the current political and legal frameworks and codes of ethics in the concrete business practices (Njegovan, 2008, pp. 60).

The job is a complex network of human relationships - the relationship between producers and consumers, employers and employees, managers and shareholders, members of the corporation and members of the communities in which these corporations operate. These are the economic relations, which creates the exchange of goods and services, and moral relations. Questions related to profit, development, technological advances, include an ethical dimension, and include the effects of pollution and depletion of natural resources, quality and character of the work environment and consumer safety (Krkač, Dedeljak, 2007, pp. 201).

Personal values and beliefs of owners and management to a large extent determine the level of ethics in the organization. Lower-level managers and workers often follow the ethical standards adopted by their superiors. Business behavior, however, is full of challenges and it happens to individuals, despite the high personal ethical standards, do not believe in the importance of morality in economics. In addition, ethical procedures come from the profession. An ethical approach to the profession, also derives from personal beliefs, but are mainly applied on the basis of accepted standards, ie. professional codes of ethics.

Another determining factor of business ethics can be determined by ***social factors***. These are the values, customs and traditions of a society that govern the ethical behavior of citizens and business people in a given society. The Company, therefore, says the business community to follow ethical standards. The concept states that "ethics is a clear aspect of making or so called normative aspect, and as such belongs to a group of institutions that include practical religion, laws, behavior." (Njegovan, 2008, pp. 60) Thus, it is acceptable or unacceptable ethical behavior depends on the culture of a given society.

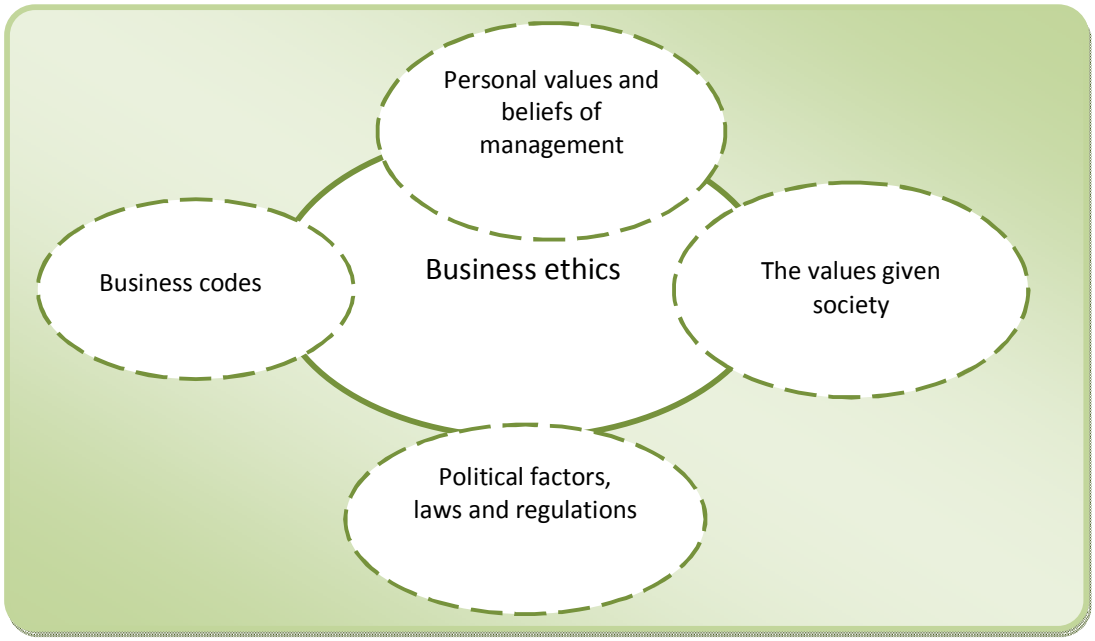
In the third group is the determining factor of business ethics are ***political factors***. The current government, political parties and leading politicians achieve significant impact on business behavior. Legal measures and enforcement measures taken by the authorities set standards and ethical business.

Fourth determinant of business ethics are codes of ethics defining ethical standards prescribed norms of ethical behavior and associated with the activities of the organization. The Code defines the application and consequences in daily practice. For example, many organizations manage to formulate a code of professional managers, but also for all other employees. Edson describes the establishment of ethical codes in three steps: the identification, description and achieving ethical objectives (Gary, 2003, pp. 64).

Business Ethics includes all activities carried out in an organization in order to ensure correct, fair and responsible behavior of the organization. This particular business ethics goes beyond positive legislative and regulatory framework and a comprehensive and superior to the concept of business conduct.

Ethical standards (ethical norms, principles) are usually defined as a system of values that an organization supports and promotes the conditions of their own actions (operations), not only to unilateral codes of ethical conduct, nor only because of external legal and regulatory requirements. For example, expression of values such as "how to behave in society as a public institution," according to ethical standards.

Picture 1: Domains of Business ethics



Source: Njegovan (2008), pp. 61

Ethical-legal compliance within the organization includes all the inner workings of the organization to comply with laws and regulations overall, which is applicable to a given type of work, the goods and services which the organization deals. Ethical-legal compliance or conformity is defined as compliance with applicable laws and regulations and all the internal activities that make up the purpose of applying ethical standards and that the data organization established in its orientation.

Ethical Policy (Ethical and legal policy compliance) includes the goals that an organization is established to review the content of their work. It assumes that organizations create and implement their own ethical standards consistent with the applicable laws and regulations, depending on the nature of the organization.

Codes of ethics (Behavior management ethics policy guidelines) are the standards of conduct established by the organization to its ethical policies applied in practice. For this purpose, it creates, if necessary, a manual for compliance with the law (a manual for compliance with ethics). Specific manual is based on the content of codes and guidelines to be applicable to specific jobs and occupations.

Internal regulation rules of internal functions, and introduced them to the organization to ensure proper functioning of the ethical-legal compliance management system. This includes specifying the superimposition of a service and responsibility for ethical-legal compliance.

Planning (Annual) is defined ethical policy changes. That would make the overall plan that includes such content, such as weather maps, time and participants of educational programs, jobs that require specific intensive training, curricula reform steps, defining the system of information, consultation and communication aimed at raising awareness on ethics. The shareholders (individuals or groups who are directly or indirectly under usticajem ethical practices as they take the organization[1]) are obliged to respect the code of ethics. It includes: consumers, employees, shareholders, trading partners, organizations that are in a relationship with a given company, the members of society and government services.[2]

2. What is the Management of Business Ethics?

"Management means doing things right, leadership means doing the right things." Peter Drucker, Economist, management guru, author (1909-2005)

A key issue is employee morale in the degree of their integration into the working environment. If a safe and flexible work environment, if members of the organization it can achieve its own goals to moderate success the company, then proportionally, and the appropriate level and morale. Therefore, the principle of integration requires that the same respect and need organization and individual needs. This requires an honest effort from employees and from management. Otherwise, the organization and every individual in it will suffer because of failed integration.

Psychologists have found that the integration of employees in the company does not suffer from disturbances in the relationship management - employee, that the degree of integration (internal and external) in direct relationship with the basic dynamic-acting factors, especially in an unfavorable environment. Integration of law, requires management to adopt such a strategy in integration processes and the nature of the human factor when it controlled. This means that workers do not make the amorphous personality but to recognize their specific individual values and incorporate them into an integrated body of the organization.

Management has the task of leading the company in a way that ensures respect for the environment, the economic success and behavior in accordance with the ethical standards: ***the prescribed standards (law) and moral norms (unwritten rules of behavior).*** Successful and ethical management are synonymous.

There are several useful suggestions what companies can do to implement ethical conduct, including:

- ***Behave ethically,***
- ***Know the people you employ,***
- ***Develop an ethical code, which makes sense,***
- ***Manage ethical training,***
- ***Encourage ethical behavior,***
- ***Create places, units and other structural mechanism dealing with ethics.***

[1] Organizations are defined as corporations, educational institutions, medical institutions, public bodies, religious organizations, government agencies, marketing groups and more.
[2] The organization's operations are included inside and outside agents – stakeholders.

Behave ethically - This is the first and most important influence on ethical behavior in the organization. The institutionalization of high ethical standards in the organization grew from the character of people who occupy important places in it. Managers cannot expect that employees behave ethically if they themselves do not behave so. They are the most important model in the organization and they have major social impact on employees at lower levels. To become a model manager for the employees it needs to show consistency between their ethical philosophy and ethical behavior. Managers who want to influence the ethical behavior of employees without the support from the top is likely to have to do so by making their own individual action to confront unethical behavior in the organization.

Make sure you know the people you hire - As individuals during most of life meets with ethical issues, there is no doubt that, when filing an application for employment, prospective employees already possess a substantial history of ethical decision making. There are several ways to check the people you need to hire: an exploration of origin, which may include acts of simple verification of information from job applications, telephone checks with the recommendations of former employers, the request for a copy of the official document, the engagement of companies involved in this type of research.

Develop a code of ethics that makes sense - Ethical codes are a sign of ethical philosophy of the company. To be ethical rules make sense in it must be clearly defined basic principles and expectations, he has to deal with potential ethical dilemmas faced by employees and must be applied. Must accept and approve employees who need to apply it. This means that managers must consider not only the content of regulations, but also the process of determining its content. To be more efficient code, it needs to develop and expand in the open, participatory environment, including the possible higher number of employees. However, many ethical rules exist only in words and deal primarily with issues of profit ignoring other important issues.

Manage ethical training - Employees should have an experiential awareness of the types of ethical dilemmas they face and to know what action to take when this happens. One way of raising awareness is the ethical training management. It should encourage employees to participate in these meetings as well as other forms of training that can be confronted. After the training is usually used fictitious scenarios that simulate situations in which employees can be found while doing their jobs. Using scenarios in which the topic of illegal gifts or bribes, employees have the opportunity to make decisions based on the specific situation and that of those decisions openly with their colleagues, bosses... However, there are many constraints (eg. bounded rationality) of this type of training that may reduce the employee's ability to convey intellectual understanding into practice.

Encourage ethical behavior - Ethical behavior must be supported through the company's incentive system. Employees should be rewarded for ethical behavior and punished for unethical behavior. This involves developing a clear understanding of how the company defines ethical behavior, development of measurement and reporting of ethical behavior, and system development and performance assessment, which includes ethical behavior. An effective incentive entails the commitment to make difficult decisions when it comes to unethical behavior. Those who are in a position to make ethical decisions often play a central role in the organization or organizations representing professional force. The successful implementation of ethical behavior requires management willingness to severely punish unethical behavior.

Create places, units and other structural mechanisms that deal with ethics - As mentioned previously, no cooperative effort from the organization to influence the ethical behavior will fail if not supported and accountable structures to support the culture of the organization. One way to operationalize this support is to create a structural mechanism for the implementation of ethics.

There are many mechanisms that an organization can apply, which are designed so that management is informed about ethics as well as monitoring the ethical behavior of employees, transfer of information regarding the ethics policy, ombudsman for the ethical issues and reporting of ethical violations...

It is emphasized that ethical behavior in business organizations is a complex problem with distinct individual and situational dimensions. Implementation of ethical behavior in business organizations is possible, but this is not an easy task.

2.1. Components of implementing business ethics

Typical components of the implementation of business ethics are (Crane, Matten; 2007; ppp. 171):

- ***Mission and values***
- ***Code of ethics,***
- ***Informational channels,***
- ***Risk analysis,***
- ***Manager acting in accordance with the ethical code,***
- ***Consultants,***
- ***Education and training in ethics,***
- ***Reporting.***

Moral has three components: ***a moral norm, moral judgment and moral sanction***.

The moral norm arises from the complex society and social relations of society and contains a requirement for individuals to behave in one way or another. Moral standards vary based on moral principles, and they allow each member of the community in particular moral action. They are the unwritten rules governing their relations within the community. Significantly to the moral norm is that in everyday human behavior divides the human, inhuman, good, bad, positive and negative. Any ethical norm presupposes a possible discrepancy between actual human behavior and what kind it should be. Moral standards do not regulate only the current state, but express request to be better. Moral norms presuppose the existence of moral consciousness, which is formed on the basis that such a distinction is made. Moral standards do not create states but are built like an unwritten social rules.

Moral judgment is an inseparable relationship with moral norms. Moral judgment is expressed in society's attitude towards the behavior of individuals and whole social groups in relation to the moral norm and can be positive or negative. Moral judgment is closely related to moral norms and attitudes. Moral judgment is the attitude of society towards a given moral-specific behavior that can be good or bad, valid-invalid, positive-negative.

Moral sanctions entail moral judgment. Moral sanctions are unfavorable consequences for the entity who has violated a moral norm. There are two kinds of moral sanctions: internal, personal, remorse, and external, social, deprivation of certain goods. Moral sanctions are measures that the company takes appropriate for a particular moral behavior.

Institutionalization of business ethics are the methods that impose ethical behavior and conduct of his control. Can be implemented by introducing codes of ethics, ethics committees, programs for the implementation of ethical education, enforcement and other social control. Many organizations are choosing to make a code of ethics governing the ethical and unethical behavior in their business. In

order to successfully implement an ethical code of conduct in the organization it is essential that managers regularly exercise control of his respect.

Ethical codes are made to organizations define acceptable behavior of their employees and also impose high standards of business. From the point competition ethical codes allow companies to compare their business to business competitors and best practices of international and national organizations. Business ethics studies the application of personal norms on the activities and goals of commercial enterprise and as such does not represent any particular moral standard, but a study of how a business context poses its own unique problems of the moral person who acts as a representative of the system.

1.2. The evolution of business ethics management

The corporation is an association that has legal personality and shall be established to protect the rights of owners and to represent their interests. In the Middle Ages they were the organization of craftsmen and traders who are in the business and enjoyed various privileges and monopoly rights so it is mostly because the bourgeois revolution and canceled. The corporate system is a social and economic structure of individual states, organized as a community in which many corporations connect and align the interests of different classes, classes and various other layers. The originators of the concept of corporate appeared in the theory of interest groups that developed under the auspices of functionalism. Corporations are created to order the division of labor and to risk sharing. Today's corporations are so many financial empire that the individual loses touch with their workplace. So easily dismisses his employee morale because there is no close contact with your company and the workers in it.

Managing business ethics can bring significant benefits to the company. Ethics programs help to maintain morality in turbulent times, strengthen team spirit, motivate employees and help to promote a positive business image to the public. Ethics examines the moral, human and explores the value-critical attitude towards the actions of other people and himself from the standpoint of good and evil.

Business Ethics explores the foundations, sources and origin of moral values, criteria and instruments for the evaluation and moral judgment in the business world in order to shed light on the meaning and find a solution of moral dilemmas and conflicts produced by human activity in the corporation which manufactures and corporations in their relations with other business entities.

However, business ethics is a broad term and covers and covers many aspects of everyday life:

a) Under the business ethics of the means and the organizational and corporate culture that refers to the rules of ethical conduct, the basic value systems, ethical principles and specific rules of ethics that the company seeks to apply;
b) The business ethics to include the principles and rules of behavior based on general and business culture, principles and rules that dominate the interpersonal communication;
c) Under the business ethics of the means of communication and business arising from the relationship of business culture and ethics in business;
d) The business ethics and the mean value of moral behavior and ethical standards of conduct embodied in codes of professional or business conduct, or business etiquette.

2. Setting Standards of Ethical Conduct

Most companies begin the process of formation of organizational ethics by developing codes of conduct, which is a formal statement that describes what the organization expects from its employees. Such statements can have three different forms: ***a code of ethics, code of conduct and statement of values.***

Ethics is the most comprehensive and consists of general statements, sometimes altruistic and inspiring, which serve as the basis for the principles and rules of conduct. Code of Ethics generally defines the methods for reporting violations, disciplinary action for violations, as well as the structure of the process. Code of Conduct is a written document which may contain some inspiring statements, but usually referred to acceptable or unacceptable behaviors. When behavior is more similar set of regulatory rules and, as such, tends to cause less discussion of concrete actions.

Some of the key reasons that codes of ethics fail to (Ferrell, Fraedrich, Ferrell; 2010; pp. 224):

- When code is not presented to the employee,
- When not readily available,
- The code is written too complicated and therefore not understandable by the average employee,
- Code is not written clearly, and it is not directly positioned,
- Top managers is never applicable "in the spirit" code.

The benefits of ethical codes:

- Employment start to think about ethical issues before they meet them in real business situations;
- Gives a chance to the employees to refuse to perform unethical activities;
- Define the boundaries of acceptable and unacceptable behavior;
- Helps in introduction of employees in ethical behavior.

Codes of ethics are statements about the norms and beliefs companies, express expectations about the behavior of managers and employees thinking. Their purpose is to stimulate thinking and models of relationships that will lead to the desired behavior. Code of Ethics should refer to general moral principles and to help build the moral atmosphere within the company.

Code of Ethics is a statement of ethical principles and rules of conduct. He must be a component of the overall company culture. It is a way of life, deeply ingrained in the collective body of the company that carried out the procedures, rules and instructions to the values contained in the Code are respected by all employees and associates. Code of Ethics must be a tradition, a way of behavior that is passed from generation to generation.

Manager, the broker is required in their work, and life in general, defended the honor, dignity and reputation of their profession through the codes of conduct. The behavior of employees is no less important than the knowledge and ability, and this is particularly noticeable in service organizations.

2.1. Code of ethical conduct

Code of Ethics establishes principles and rules of business ethics and is designed for businesses, all persons employed and persons engaged under the contract in any sector of the economy.

Do we respect the codes of ethics and principles depends on many conditions: the kind of social milieu encouraged, such as a legacy of what the existing social conditions, the system of values we have, we hold it to high moral principles. The key moment, the line between ethical and unethical business usually shoot in crisis situations, whether it is a crisis of government that we had in the late 20th century, or about any of the standard bureaucratic crisis faced by every entrepreneur designate meets every day (Vučićević, 2011; pp. 7).

Knowledge of the Code allows an individual to confidently deal with difficult situations at work and that his real abilities come into play. If the code is unknown or if it does not comply will be much harder to be successful.

The basic principle of good business manners was very careful consideration the interests and feelings of others. In other words, what you do and say you have to show that the person with whom contact take care as much about themselves. Their behavior should demonstrate the possession of real human value which is the basis of the behavior of others, which are present in all. So, if you need to resolve a contentious situation, the supervisor or punish someone is released, should not only act fairly and consistently, but also demonstrate an understanding of personal problems. Very often, it takes a strong will to curb the natural instinct to take advantage of someone who is at a lower position. However, in this way not only to gain the respect of others, but it increases their own sovereignty and respect for themselves.

Respect for the principles and rules of business ethics includes the following principles:

1) Professional conduct of business;
2) Scrupulously and fully download and fulfillment of obligations and responsibilities;
3) Conducting business in a way that does not jeopardize the professional reputation;
4) Using the allowed resources to achieve business goals;
5) Compliance of incompatible activities;
6) Confidentiality;
7) Avoiding conflicts of interest between personal and business entities;
8) Conducting business activities in a manner not harmful to existing shareholders, members or co-owners;
9) Commercial activities that increase the capital value of the company;
10) Abstaining from the use of political influence or pressure to achieve business goals;
11) Business cooperation with other undertakings "bona fide"[3];
12) Resolving disputes with business partners through negotiation or mediation, and efforts to continue good business relations;
13) Respect for intellectual property rights;
14) Conducting business activities in accordance with the regulations on the protection and enhancement of the environment;
15) Respect for standards of business ethics and contribution to the further promotion of morality in business relations.

The aim of the Code:

1) To contribute to the execution of business activities in the spirit of business ethics, good business practices and principles of good faith;
2) To provide transparency of companies and institutions.

[3] In philosophy the term bona fide refers to good hope, faith.

3. Business Ethics and Leadership

The way the leaders in an organization using the power and influence others is reflected in all aspects of work, especially on organizational culture, productivity, commitment, optimism, identity, satisfaction and a positive work behavior.

Several criteria are considered in the evaluation of individual quality of leadership when it comes to ethics in the first place: a personal set of values, the level of moral development, conscious intention, freedom of choice, the use of ethical and unethical behavior and other types of impact.

It is known already that the personal integrity of leaders is an important element of effective leadership, and is also the cornerstone of ethical leadership.

The simplest definition of integrity, honesty and emphasizes consistency in the expression of personal values and behaviors. For the practice of ethical leadership, however, is not enough just to act in accordance with their beliefs, but to be your moral values and ethical behavior. You have a leader who believes he is manipulating others to achieve better results the company is correct and that the practice is implemented consistently.

Leadership to be effective, it must be ethical. There is no doubt that they are somewhat more stringent ethical standards in relation to the legal norms of behavior.

Ethical Leadership is defined as the demonstration of normal behavior through appropriate personal actions and interpersonal relationships and promote such behavior by followers through two-way communication, reinforcement, and decision making.

The ethical leader is trustworthy because it keeps the word and practices what he was saying. Moral leadership is committed leaders to do things that were promised. Ethical values are linked to national and organizational culture.

Models of business ethics assume that the value of organizations and individuals influence the strategic decisions of companies. Business ethics is applied ethics because it concerns the application of one specific type of activity.

3.1. Moral Leadership

"To lead people, walk beside them!" Lao-tsu, Chinese philosopher (4-6 century BC)

The causal chain of an activity in a large organization often involves a lot of people who are connected to each other hierarchically. They feel at the end of the chain are forced to the schedule of certain actions - have received orders and options open to them are limited. You have not created the plan and its implementation, just followed the instructions. Therefore feel that the responsibility for their actions falls on those above them.

On the other hand, the management company does not see the specific outcomes that the commands issued since the distance from its actual execution. It is believed that the employees directly lower organizational charts should be given powers to make decisions, and to them, as long as they work well, you should check. Thus, at both ends of the chain of people involved in the business believe that these are actions that you are not morally responsible.

However, the structures and laws that are immoral are encouraging people to act immorally, and moral structures and laws encourage people to moral action. Well, in terms of morality, society or organization or company they're good because of its good structures and good for people who make them. Moral people are needed to create and maintain the moral structure. One supports the other. If the structure supporting immoral or unethical activity and reward, it is clear that they can change only the people who recognize them as poor and who have the power, ability and willingness to change them. In this sense, ethical people are necessary for the existence of ethical companies, and corporations.

Hobes solution is the legal form of the idea called "***social contract***". He believes the only way to moral evil, but rational people avoid conflict. If there was no society, people would live in a "state of nature" where life was "solitary, poor, painful, brutal and short".

4. Conclusion

We've looked at approaches to business ethics, and we've seen that all have limitations. If we hope to find an approach to business ethics that is free from conceptual problems, we will not likely find any. Ethics is a complex subject and its history is filled with diverse theories that are systematically refuted by rival theories. So, we should expect to find controversies when applying ethics to the specific practices of business. However, following any of the above three approaches to business ethics will bring us closer to acceptable moral behavior than we might otherwise be. Close attention to one's profit motive and the moral interests of consumers might in fact generate some morally responsible business decisions. We can indeed find additional moral guidance by looking at the laws that apply specifically to businesses. In gray areas of moral controversy that are not adequately addressed profit motives and the law, we can turn for guidance to a variety of general and specific moral principles.

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Culture-Personality of France and Hungary Scale Development and Results

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Abstract

The main objective of our research was to develop a Culture Personality (CP) scale that enables us to measure how consumers describe the cultures of certain countries as personalities. Our main research question is, on the one hand, whether perceived culture-personalities influence the evaluation of countries as ideal tourist or business destinations, on the other hand, whether some aspects of the perceived personalities of consumers correlate with the above ones.

For scale development, based on our qualitative results, a 51-item semantic differential scale was generated to measure France's and Hungary's culture-personality traits of France and Hungary among students of the two nationalities. In this article, after a short theoretical and methodological overview, the initial results will be introduced about these two culture-personalities and the differences perceived by these two groups. Correlations were found between more than half of the personality scale items and ideal tourist and business destination evaluations.

Keywords

Culture, personality, scale development, self-congruency

1. Introduction

The concept of personality gained attention among researchers in marketing when very similar products resulting from mass production started to be positioned on the bases of brand personalities, associations or abstract traits (McEnally and De Chernatony 1999); especially because in most cases this kind of differentiation required less investment than product development (Azoulay and Kapferer, 2003).

Nowadays, the concept of country image, country branding and destination marketing have recently gained more attention in the international academic research in marketing relying its methodology partly on the achievements of brand personality theories.

We believe that the personality of a country is strongly connected to the country's culture. The main objective of the research presented in this article was to develop a Culture Personality (CP) scale, which can be used to measure how consumers perceive the cultures of different countries as personalities. In this paper, a short overview of concepts and related theories of culture and personality will be given followed by the discussion of the partial results of scale development. The article finally investigates the impact of culture personality on the evaluation of countries as ideal touristic and business destinations.

2. Theoretical Background

2.1 The role of personality in marketing

A considerable amount of research has examined the relationship between self-concept and customer behavior. Based on the findings two motives have been identified that can induce mental or behavioral reactions - *self-esteem* and *self-consistency* (Epstein, 1980). According to Sirgy (1982, 287.) the previous one *"refers to the tendency to seek experiences that enhance self-concept*". Self-consistency, on the other hand, *"denotes the tendency for an individual to behave consistently with her view of herself"*. To explore the psychological mechanisms and determine valid associations researchers differentiated several types or components of self-concept that can play different roles in brand decisions. Based on the literature we can distinguish the *actual self* which reflects the image perceived about oneself and the *ideal self* that refers to the image of oneself that is desired to be perceived by others. Another dimension of self-concept reflects the beliefs that others hold about the individual. The *social self* for instance denotes the image that is believed to be perceived by others and the *ideal social self* is what we would like others to hold about us (Sirgy, 1980; Prónay, 2011). In the social psychology literature further components can be found, e.g. the *expected self* (Higgins, Klein and Strauman, 1985) or the *possible self*, which has an idealistic dimension and an opposite one we are afraid of becoming (Markus and Nurius, 1986). Based on time, self-concept can refer to past, present and future (Markus and Wurf, 1987) and it can be dynamic, that is, some of its constituents are relatively stable, although other components can change very easily depending on the social context.

In marketing the main focus of researchers has been concentrated to the link between various types of self-concept and brand image but the results were contradictory in some cases. After his literature review Sirgy (1982) found that although the effects of congruity between the four basic types of self-image discussed above and brand image are mostly supported, some studies were not consistent with these findings. Regarding destination marketing there seems to be a difference between the consequences of the actual and the ideal self-image. The former plays role when consumers make decisions about returning to a destination. On the other hand, if they have to recommend a destination, they consider options that are consistent with their ideal self-image (Usakli and Baloglu, 2011).

2.2 Defining the concept of personality

Personality, the core concept of our research, has been conceptualized in many different ways. Diverse approaches have been emerged in the literature depending on assumed antecedents of the concept that can presumably be biological, psychoanalytical, or evolutionary etc. One of the most popular directions of various research streams is the trait theory that emphasizes the stable and inherited characteristics of a person and focuses primarily on the measurement of these traits. The pioneering researcher of this theory was Allport, who collected 49 definitions of personality between the two World Wars to analyze and classify them. Based on this work he developed his own definition as *„personality is the dynamic organization within the individual of those psychophysical systems that determine his unique adjustments to the environment"* (1937, p. 48.). This description reveals the nature of the concept that can be hardly captured in a precise manner and by necessity researchers define it at a general level. Despite some weaknesses of the theoretical background, the trait theory evolved into the most dominant approach of investigating personality. This can be attributed to the strong measurement orientation and the attention paid to the development of applicable scales. Allport and Odbett (1936), for instance, following Bumgarten's work, based on a lexical method collected almost 18 000 phrases that are found to describe the differences of the behavior of individuals. This became the origin of the most recognized measure of personality, the Big Five (John and Srivastava, 1999). The Big Five model of personality assumes a hierarchical structure of traits and five broad dimensions at the highest level. Although both the lexical method and the Big Five model are heavily criticized stating that it ignores deeper theoretical approach and explanations (McAdams, 1992), the five factor framework is accepted as a universal empirical tool to measure personality. It is important to emphasize that trait psychologists albeit admit that personality can also be determined by other factors than genes, they mitigate the relevance of the environment (Mirnics, 2006). As a consequence, personality is considered as a sum of relative constant characteristics of an individual (Azoulay and Kapferer, 2003) and as such, it is easy to measure.

As mentioned before, trait psychology regards the personality concept as a hierarchical structure of traits but beside the widely accepted five factor model, different numbers of dimensions can be found in the literature, such as the 6-factor model of Ashton and Lee, and the 3-factor model of Eysink (Linden et al., 2010). Researchers have recently investigated the possibility of more common dimensions or a single universal one called the General Factor of Personality (GFP; Linden et al., 2010).

2.3. The relationship between culture and personality

Culture has also been defined in various ways. Kuper (1999, p. 227.) provides a short definition as *„a matter of ideas and values, a collective cast of mind*". Hofstede interpreted the concept alike to some extent, given the definition as *„the collective programming of the mind that distinguishes one group or category of people from another* (…) *interactive aggregate of personal characteristics that influence a human group's response to its environment*" (Hostede 2001, p. 9.). As Allport's conceptualization of personality, Hofstede's culture concept also manifests in the reaction to the external environment. Also a similarity between these two concepts that they are the source of uniqueness/differentiation, but in case of culture the distinction is made on group level instead of the individual one. The main difference is, on the other hand, that in case of culture, inherited components are excluded.

The origin of the conceptual connection between culture and personality stem from the phrase of national character, a concept that has been in interest in history. Inkeles and Levinson (1969, p. 428.) defined it as a *„relatively enduring personality characteristics and patterns that are modal among the adult members of the society*". This definition induces the question whether the character or personality of a country, nation or culture is the sum or average of the attributes of all members, or it reflects the characteristics of a typical member or the group has other, distinct characteristics. For the owner of a dog, his/her favorite pet can be described with several positive attributes. We can say that it is especially a friendly. However, if she/he meets next day a flock of one thousand similar dogs, the crowd will remind her/him the phase "frightful" despite the fact that none of the members alone can be marked with this trait.

In the country image model of Heslop et al. (1993) the image of the country and the one of the people living there are handled as two different – but strongly correlated – concepts. People image is not considered as part of the country image, it can be interpreted in other dimensions.

Hofstede and McCrae (2004) empirically tested the relationship between the factors of culture and personality and they tried to explain the uncovered associations from the theoretical point of view, assuming opposite causality. According to Hofstede, there can be three reasons behind the significant differences between the traits of cultures: a) the inherited traits have systematically different distributions in nations; b) in the socialization process the dominance of the common characteristics of individuals increases; c) response bias since the individuals of cultures are differently affected by social expectations while answering the personality test. However, McCrae in the same article emphasized the inherited, biological nature of personality. Culture can influence only the way of manifestations of personality in different situation but it cannot be changed at trait level. McCrae refers to the research of Bouchard and Loehlin (2001) that concludes that common environment has only minor impact on personality and to the longitudinal studies that revealed that personality traits are stable despite different life experiences (McCrae and Costa, 2003). McCrae explains the explored connection between cultural and personality factors with two theories. *Selective migration* supposes that an individual whose personal characteristics do not fit to a culture will leave it and *reverse causation* assumes that a culture and its institutions and value systems are determined by the distribution of personal traits in it.

3. Research Methodology

Results presented in this paper are partial outcomes of the culture-personality (CP) scale construction procedure. For generating the scale items, qualitative data were collected during each semester between 2004 and 2012 among foreign exchange students, answering the following question: „Culture is often thought of as the personality of the society. If your culture was a person, how would you describe its personality traits?". Altogether 520 culture-personality descriptions (about 42 different cultures) were generated this way and based on the most often used adjectives, a list of personality traits was prepared.

In 2012, two control methods for these scale items were used. 48 personal interviews with MBA students were conducted then 70 international business majors were asked to discuss cultural descriptions in small groups after lectures of the intercultural communication course on theories of cultural models. Utilizing the results of these above mentioned three methods, a 51-item bipolar scale was developed.

Opposite adjectives of the semantic differential scale were examined and content validity was checked. Before translating the scale items to English and French, interviews with linguistic experts were conducted. Then real content of the adjectives were discussed with bilingual translators. This

way – besides resembling the different versions of parallel translations – interpretation of the Hungarian adjectives were double-checked. To finalize the scale items, we employed 5 topic-experts, 3 native speaking translators and 2 bilingual proof readers.

An online survey was conducted among a convenience sample of 216 Hungarian and 47 French university students. Both groups were asked to rate the personal traits of the French and the Hungarian cultures , on a 7-point semantic differential scale (see Gyulavári et al 2012), with the following introduction: "Please rate the French and the Hungarian culture as a person, using the following scales". Both groups filled in the questionnaire first regarding their own culture and then regarding the other culture.
Further phases of the scale development and the finalized scale will be presented in later publications.

4. Results and Discussion

4.1. Personality traits of the Hungarian and the French cultures

In the followings, we present the first 10 scale items that respondents evaluated with the highest means on a 7-point scale. Regarding these variables with the 10 highest means, we found similarities for five personality traits of the French culture (proud, ambitious, dynamic, wasteful and open-minded) and for 4 traits of the Hungarian culture (pessimistic, traditional, conservative and inflexible) among French and Hungarian respondents. On the whole, Hungarian participants evaluated French culture more positively than Hungarian culture, while French students associated more positive characteristics with their own culture than those of Hungary's.

Interestingly, both groups found their own culture humorous, on the French respondents' list of adjectives this is the first adjective in rank with the highest mean, for Hungarians it is the second. Besides, both nations perceive their own culture's personality as proud (third rank on the Hungarians' list, and second on the French'.) In the following table (Table 1) Hungary's most characteristic personality traits perceived by Hungarian and French respondents are listed.

Table 1: The most characteristic personality traits of the **Hungarian culture** among Hungarian and French respondents

Hungarian respondents; n = 216				French respondents; n = 47			
Personality traits of the Hungarian culture		Mean (1-7)	St. Dev.	Personality traits of the Hungarian culture		Mean (1-7)	St. Dev.
1.	**pessimistic**	6,01	1,141	1.	**conservative**	5,76	1,091
2.	humorous	5,04	1,189	2.	**traditional**	5,34	1,261
3.	proud	5,36	1,423	3.	sad	5,24	1,504
4.	**traditional**	5,13	1,142	4.	insensitive	5,21	1,590
5.	**conservative**	4,96	1,212	5.	rough	4,97	1,322
6.	past-oriented	4,93	1,195	6.	**pessimistic**	4,90	1,589
7.	unstable	4,88	1,150	7.	**inflexible**	4,83	1,338
8.	**inflexible**	4,87	1,226	8-10.	impolite	4,76	2,012
9.	disorganised	4,71	1,243	8-10.	brave	4,76	1,272
10.	anxious	4,70	1,124	8-10.	calm	4,76	1,806

While 91 per cent of the Hungarians perceive the Hungarian culture pessimistic, only 52% of French think so (giving 5, 6 or 7 for the optimistic-pessimistic bipolar item on a 7-point semantic differential scale). 42% of the Hungarians while only 24% of the French evaluated this item with "7".
French respondents perceive the Hungarians more conservative than Hungarians see themselves. (82% vs. 72% gave 5, 6 or 7 on this trait). Both groups similarly reckon the Hungarian culture-personality traditional and inflexible. Besides, the French believe that Hungary's culture personality is

rough, insensitive, impolite, sad, calm and brave, the Hungarians perceive it as past-oriented, unstable, disorganised and anxious. The most characteristic culture-personality traits of France are demonstrated in Table 2.

Table 2: The most characteristic personality traits of the **French culture** among Hungarian and French respondents

Hungarian respondents; n = 216				French respondents; n = 47			
Personality traits of the French culture		Mean (1-7)	St. Dev.	Personality traits of the French culture		Mean (1-7)	St. Dev.
1.	**proud**	6,05	1,08	1.	humorous	5,90	1,40
2.	dreamer	5,02	1,34	2.	**proud**	5,83	1,28
3.	self-reliant	4,99	1,36	3.	**ambitious**	5,45	1,35
4.	**ambitious**	4,96	1,51	4.	friendly	5,28	1,51
5.	**wasteful**	4,94	1,07	5-6.	sophisticated	5,03	1,21
6.	**dynamic**	4,83	1,21	5-6.	**dynamic**	5,03	1,45
7.	sad	4,81	1,14	7.	**wasteful**	4,93	1,39
8.	feminine	4,80	1,47	8.	modern	4,90	1,29
9.	**open-minded**	4,73	1,52	9-10.	sexy	4,83	1,58
10-11.	colourful	4,63	1,19	9-10.	**open-minded**	4,83	1,69
10-11.	educated	4,63	1,28				

According to 42% of Hungarian and 38% of French respondents France's personality is expressly proud (gave "7" on a 7-point scale). The level of agreement is the same on French being open-minded and ambitious. Although the means are not different for being wasteful (4,93 and 4,94), it is obvious that Hungarians typified it more wasteful with scores "5" and "6", while one third of French respondents gave "4" on the wasteful-thrifty bipolar scale. The same frequencies can be found on the adjective "dynamic" (only 13% of the Hungarians and 31% of the French gave the middle value, "4".)

Whilst the French described the Hungarian culture as rough, impolite and insensitive, they perceive themselves friendly and sophisticated. Interestingly, the Hungarians believe that the French culture-personality is sad, at the same time the French have the same belief about the Hungarian culture.

In the followings, we elaborate on those personality traits that show significant differences in means among French and Hungarian respondents ($p \leq 0,05$). Figure 1 presents remarkable differences of the Hungarian culture's evaluations regarding quite a lot of attribute-pairs: out of 51 pairs 24 significant differences were found.

Besides the above mentioned differences, the French see the Hungarian culture as colder, more rational, less intelligent, more average, thrifty, industrious, realistic, strict, careless, more future-oriented, grey, feminine, self-dependent and selfless than Hungarians see themselves.

Figure 1: Significant differences of evaluation of Hungarian culture-personality traits in frame of the means given by Hungarian and French respondents (in parenthesis the opposite trait of the semantic differential scale is shown, meaning the negative pole of the scale: 1 on 1-7).

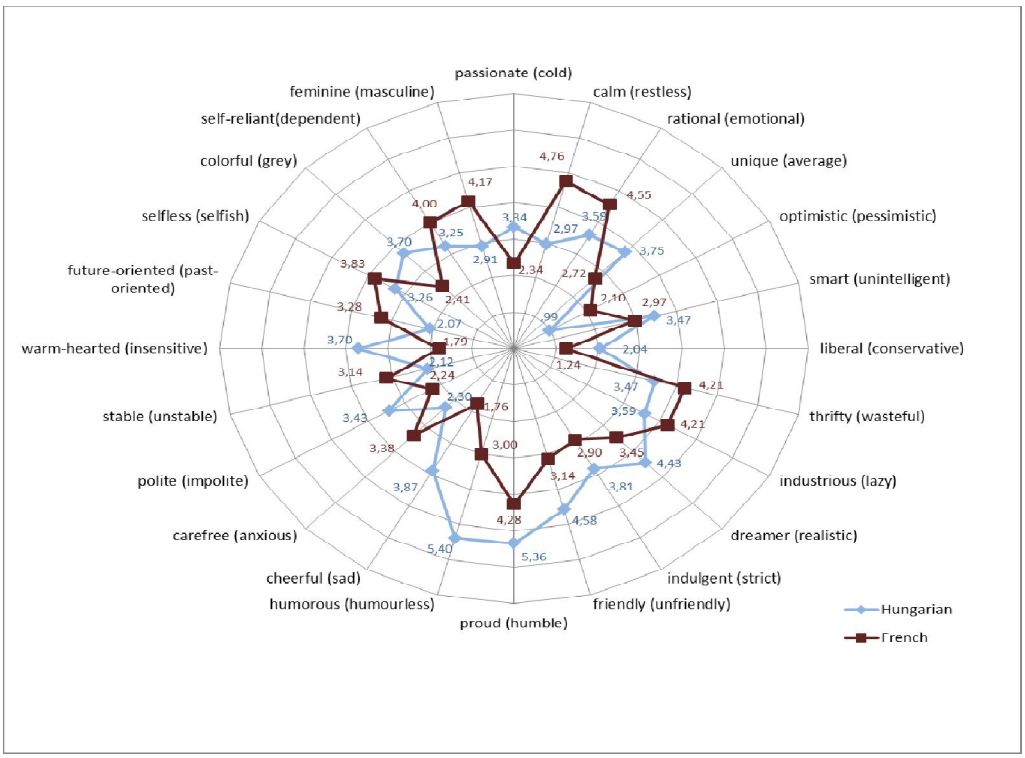
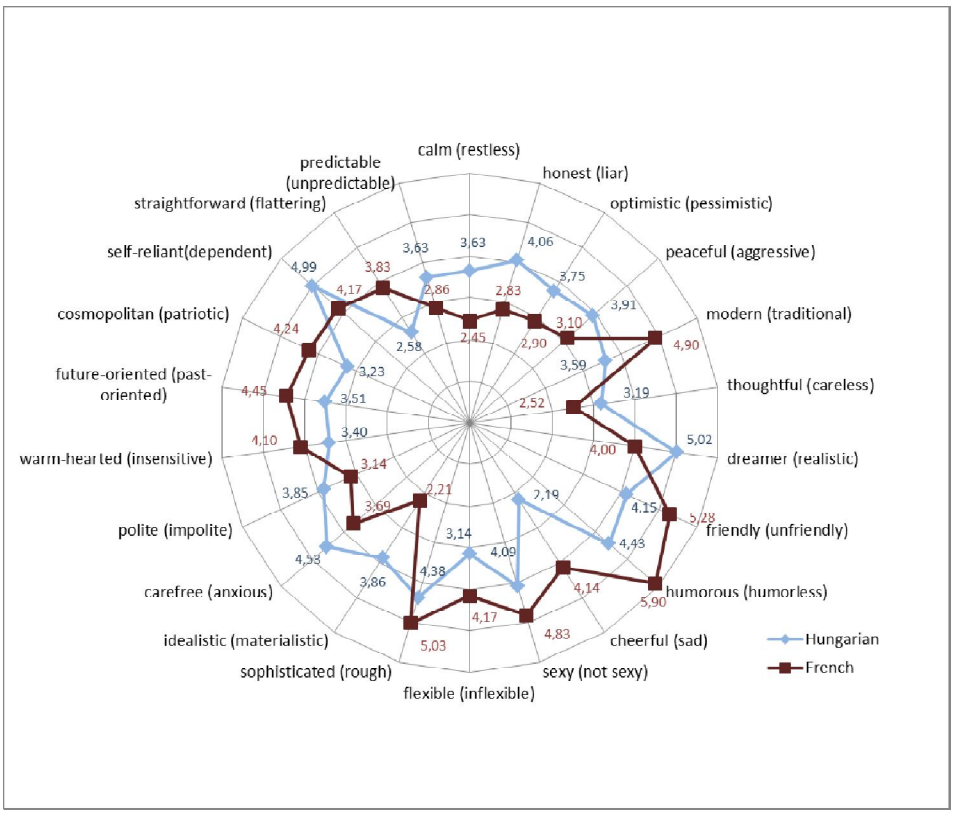


Figure 2 represents personality traits of France that were perceived significantly different by the French and the Hungarians, we found 22 significant differences (p≤0,05). Hungarians see the French more honest, calm, more optimistic, peaceful, traditional, thoughtful and realistic than French themselves. Also, the Hungarians perceive the French culture-personality more sad, less friendly, less humorous, less sexy, more inflexible and less sophisticated than the French. They describe it more idealistic, carefree, polite, insensitive, more past-oriented, self-reliant, flattering, stable and patriotic.

Figure 2: Significant differences of the evaluation of French culture-personality traits in frame of the means given by Hungarian and French respondents (in parenthesis the opposite trait of the semantic differential scale is shown, meaning the negative pole of the scale: 1 on 1-7).



4.2. The effect of culture-personality on the evaluation of the country as a tourist and business destination

One of the research questions in the focus of our study is which personality traits influence whether the country is considered ideal tourist/business destination or not. Correlation was found between France being ideal business and being ideal tourist destination for the Hungarians (Pearson correlation: 0,482, p<0,0001). France is considered quite an ideal destination from the touristic point of view (mean is 5,00), and a little less ideal business destination (4,25), measured on a 7 point scale. For the French, Hungary is also an ideal tourist destination (5,04), but less ideal as a business partner (3,11). (Important note: the French respondents have spent 3,5 months in Hungary as exchange students so have some experience regarding the country).

Correlations can be found in Table 3. As the sample size of French respondents is quite small, we discuss only results for France, i.e. which personality traits correlate with the evaluation of France as an ideal destination for Hungarians. We found correlations with 24 variables in case of tourist destination, and with 18 variables regarding business destinations. Among these, 13 scale items are positively correlating with both. Honesty is the most important culture-personality trait, it has the highest correlation coefficients with both the tourist and the business destinations.

Table 3: France as an ideal tourist and business destination in frame of its culture-personality traits

Correlation **either** with ideal tourist **or** business destination			Correlation with **both** ideal tourist and business destination		
Culture-personality traits	ideal **tourist** destination	ideal **business** destination	Culture-personality traits	ideal **tourist** destination	ideal **business** destination
warm-hearted	,301		**honest**	**,371**	**,346**
passionate	,287		friendly	,370	,163
carefree	,254		sexy	,352	,286
tolerant	,243		smart	,330	,291
polite	,226		humorous	,312	,210
selfless	,205		brave	,308	,221
dynamic	,202		educated	,282	,221
optimistic	,176		unique	,272	,236
generous	,171		colourful	,229	,133
individualistic	,150		peaceful	,198	,172
idealistic	,137		straightforward	,160	,207
well-organized		,202	perfectionist	,143	,226
stable		,195	industrious	,140	,263
self-reliant		,179			
proud		,154			
ambitious		,135			

Pearson correlation coefficients ($p \leq 0.05$)

5. Summary

The article summarizes the first and initial attempts at developing a valid instrument for measuring people's images on culture personalities. Initial results show that not only different culture personalities are perceived differently, but some of the traits of the same culture are also judged differently by diverse groups (in our case, the French and the Hungarian respondents). One of the most important results is that out of 51 scale items, 29 correlated with the evaluation of a given country as an ideal tourist and/or business destination.

Our research has limitations due to the nature and size of the sample and the initial stage of the scale development. Further research is needed to test the appropriateness of the CP scale across different countries, to validate the scale and reduce the scale items, and to verify the coherence with the relevant self-congruity theories.

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Standardization as a Key Issue in Shared Service Organization

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Abstract

The aim of a shared service model is improving processes and ensuring more cost-efficient operation. In this paper I focus the role of standardization in shared service organizations. In my research I analyzed some case studies to disclose the main benefits of process standardization. I determined the advantages and disadvantages of it and the connection with shared service model. I analyzed how companies should embark on process standardization, how they should utilize standardization for improving of shared service model. I treated the global-local dilemma related with service organizations and the risk of standardization from an aspect.

Keywords

Standardization, shared service organizations, center of excellence, SSC, BPM

1. Purpose of Manuscript

To provide an overall picture about shared service organizations and the tools and methods used within them. Among these I focused mainly on the standardization. I would like to answer some practical questions connected with shared service model: what process standardization means, what it is used for, what could companies reached by standardization, is there any disadvantages using standardization or only advantages.

In complex global environment the main question for organizations how to adopt their organizational structure to the emerging challenges and how to find the right balance between standardized global and tailored local processes.

2. Design/Methodology/Approach

This research is mostly based on literature review. A lot of articles deal with shared service centers and other shared service organizations (SSO) but there is no one that comprises the role of standardization. I collected some international case studies (Infosys, Oracle, about shared service centers to examine the practical benefits of it.

3. Findings

The rising complexity on the field of structures, processes and communications is making global organizations more difficult to manage. The original target of using shared service model was cost-cutting but nowadays its judgment had been changed greatly. They are considered such strategic business units those aim to reach service and operational excellence. In line with it the service portfolio of shared service centers (SSC) were also extended. These days centers include more complex and knowledge-based processes like R&D, sales or marketing which are closer to traditional core business. There are a lot of drivers for establishing of shared service center but the most important are the followings:

- improved services, reduced costs;
- standardized services and processes;
- diminished administration costs;
- supporting corporate strategy;
- grouping similar tasks and demolishing redundant processes;
- favoring progress;
- facilitating introduction of new technologies;
- improving working capital.

So standardization is a key issue for each shared service centers because this is one of those elements that could be possible the cost-benefits of service delivering. But let's see what standardization is anyway.

4. Standardization

Standardization means a framework of agreements to which all relevant parties in an industry or organization must adhere to ensure that all processes associated with the creation of a good or performance of a service are performed within set guidelines. This is done to ensure the end product has consistent quality, and that any conclusions made are comparable with all other equivalent items in the same class. The main criteria for standardization are:

- improved ICT,
- transfer of technology,
- uniform terminology,
- sized and dimensions are coordinated and adapted,
- process variety are reduced,
- function requirements and characteristics are specified.

Business standardization means establishing uniform business processes across various organizational units or locations. It helps to decompose a large problem into smaller parts that can be individually solved. The expected results of it are processes that consistently meet their cost and performance objectives using a well-defined practice. Standardization also reduces the risk of failure. Through standardization, individual business units can share expenses, and will benefit from a company-wide business process management (BPM). BPM is a structured approach employing methods, policies, metrics, management practices and software tools to manage and continuously optimize an organization's activities and processes. In the context of BPM, I understand process standardization as the unification of business processes and the underlying actions within an organization in order to "facilitate communications about how the business operates, to enable handoffs across process boundaries in terms of information, and to improve collaboration and develop comparative measures of process performance. Corporate-wide development of business processes lowers the total expenses, using economics of scale. (Ricken et al., 2005)

To standardize effectively requires a good understanding of the differences between divisions' management teams, their inputs, their products and customers, and the constraints under which they work. it is crucial to divide between 'standard processes' and 'standardized processes'. A standard process exhibits predetermined input, produces an ex-ante specified output, and is repeated identically. Standard processes are predestined for being exactly defined and standardized. However, they only offer this potential and may not be standardized, yet. Standard processes are simple: events and outcomes are well-understood; the process can be designed to accept a specified type of input, and to produce an ex-ante specified type of output, and process control is realizable by following established standard procedures and process descriptions.

5. Process Standardization

Process is a logical sequence of tasks performed to achieve an objective. Process may be standardized across an organization, agreed upon within a smaller group or unarticulated sets of common assumptions. These unarticulated processes can include accepted ways of acting in a group meeting or asking for help and are considered components of culture. (Lamb et al., 2007)

Process standardization means the unification of variants of a given business process by aligning the variants against an archetype process that results in transparent and uniform process activities specified in standard operating procedures which are obligatory to all actors in an organization in order to create a time-, cost-, and quality-optimal way of achieving the business process' goal.

Standardization of corporate processes intends to develop performance and to give executives more control over operational performance. The most known performance measurement is the cost of executing the process. Although it is no less important, the quality of the results is less often considered. Finally, the impact on other business processes needs to be considered, such as the ability to apply the standard performance measures and, thus, compare a unit's performance with others. Advantages of process standardization:

- direct cost and quality improvements;
- simplified and better decision making;

- the process becomes more reliable;
- reducing variability and ambiguity;
- develop process maps;
- provide individuals and teams with an understanding of their role in the overall whole;
- variations in quality shrink;
- less expenses in development of innovative new practices, and less expenses in the administration of processes;
- comparing the performance between different units of an organization becomes easier;
- process standardization is an important prerequisite for the standardization of IT systems;
- simplifying the coordination and control between subsidiaries and business functions.

Disadvantages of process standardization:

- coordination cost;
- loss of motivation and morale because of not invention;
- rigid processes reduce overall flexibility;
- less locally oriented approach.

To avoid proliferating of disadvantages it is important to streamline processes without standardizing more than it is necessary.

6. Standardization at SSC

Standardization is a key benefit experienced in the private sector. Standardization reduces cost for training, support and upgrading software. This is usually the second stages of evolution in shared service model. After the consolidation stage where the focus is on the bringing same processes and systems under one roof and located it near to the corporate or major customer, the second stage focus on the standardization. Private sector companies can benefit from best practices. They adjust their processes to achieve greater efficiency. But it is not so easy in the public sector. Adjusting processes to achieve greater efficiency or standardization often requires changes to the law. Privacy, agency independence, de-centralization and other problems can make standardization exercises difficult. Shared services initiatives begin with analysis of the current situation. There can be significant commonality among government organizations.

Standardization could offer an opportunity to codify best practices and facilitate effective coordination among individuals and groups working on a complex problem. (Lamb et al., 2007)

Big companies attempt to rationalize operational costs by standardization and deliver services over country's borders as well. Depending on the expected assets at the end of the process, either a captive center is created or an outsourcing provider will get the delivery. The key lies in the reorganization of processes. If the function moves to an offshore location then this will mean further cost reduction. Shared service organizations (SSO) could be a good tool for these aims.

There will be a lot of advantages of using shared service organizations. The first and the most evident is combination of benefits in centralization and decentralization without disadvantages of them. Standardization established by function reduction facilitates to exploit benefits of economics of scale that was unexploited till then. Over and above in decentralized organizational units the redundant processes and resources are eliminated. This releases important capacity.

Standardization and consolidating of services in a central, newly established unit also has an effect that goes beyond the mere cost-benefit factor. The standardized and more transparent processes

also make a more focused control and allocation of services within a group possible. Improvement in internal processes can also have positive external effects, such as a better product or service quality.

Operating shared service centers with transfer pricing create near-market situation inside of company that could ensure efficiency of shared service center and compel quality services delivery. After all shared service center (SSC) bears comparison with external service providers and service level agreements that mutually elaborated with customers should adjust to prices and performance of external providers. Delivered service depends on volume is uniform for each organizational units and it is a huge step for smaller organizational units.

Another benefit of these organizational solutions is that cooperation between service centers and customers influences the whole company. It creates such management framework that contributes to better operation of the company with increasing organizational transparency, making aims and demands precise and measuring performance. This management framework could be the business process management (BPM) that is one of the most frequent business themes in the process-based organizations. BPM is a management practice that provides for governance of a business's process environment toward the goal of improving agility and operational performance. BPM is a structured approach employing methods, policies, metrics, management practices and software tools to manage and continuously optimize an organization's activities and processes.

7. Bundling processes into an SSC

To move functions into a shared service center is a complex process. It could be succeeded only with experienced executives and motivated employees. There are some questions that should be answered before company embarks on it (Hach et al., 2012):

1. Which functions can be moved?

It is essential that functions that are bundled into a shared service center should be as simple as it possible to get economies of scale and a profitable transfer of knowledge among employees. Operational functions should be bundled as fully as possible in the SSC.

2. To what extent should functions standardized?

Complex functions usually require complex and costly processes. To solve this problem and simplifying them it should be broken services into standardized components.

3. Which processes can be automated and how?

An automated process could ensure faster processing, better service quality and lower operational costs.

8. Next generation of SSC

In today's rapidly changing business environment, executives are now aligning their shared services goals with overall long-term corporate goals and the shared service organization’s vision is expanding to a broader strategic role in sourcing actions. With demands and opportunities of globalization, new sourcing models are being developed by companies with a focus on more value-added processes.

Shared service organizations are moving to the next generation step by implementing standardize and re-engineer approach. Many sourcing initiatives started out with business processes being just centralized, with few process improvements. This approach had mixed returns. To move to the next generation, shared services must assess the maturity level of their processes and determine the best path to achieve standardization and process re-engineering. This makes or buy decision is leading

many SSCs to include outsourcing as an enabler of standardization and process reengineering and to drive an ongoing continuous improvement strategy across all functions and geographies.

9. Balancing Among Global, Regional and Local

In every global service organization there is the dilemma about the level of global or local processes. Organizations are looking for the opportunity to realize benefits from economies of scale by organizing their similar tasks into a shared service centers but in parallel with it to support high-growing regions tailoring to local markets any tasks that are different from country to country. The former one is help companies to assess the essential elements of processes to keep and eliminate the redundant elements and too much duplication in effort. The later one could help to refine operations and elaborate customized services that can exploit regional growth.

The regional effort can evolve regional center of excellence (CoE) that often are very cost effective. Center of excellence is an organizational unit that during doing its own work – as a secondary task – improves its knowledge and experience. It fosters the work of other units and contributes to the progress of the whole organization. Center of excellence consists of functional or cross-functional teams that endeavor to gain new knowledge or experience inside or outside of the company. Teams could be physically or virtual but they exist mainly permanent rather like project. Knowledge-management is a significant characteristic for center of excellence. Term of CoE does not mean that the work of other organizational units is not important or maybe less valuable. These units also have to fulfill the prescribed service level but there is no plus task of developing. Over doing own work CoE has to elaborate good practice and disseminate it among the other units of organization.

McKinsey's survey illustrates (Gibbs et al., 2012) that corporate executives should regularly evaluate which process be global or local. But it is quite hard if companies have too many processes and executives do not know how many processes they have or what those processes are. Additionally only few could differentiate the standard processes that create value from those that do not and identify which are these value drivers. Unfortunately in many companies this is the case.

So it is important that companies do not standardize processes more than it is necessary. Business units should choose their locally relevant key performance indicators (KPI) that are fit to global KPIs and contribute to annual targets. Technology development could help standardization but it is only meaningful if companies are sure in realizing the expected returns. Standard processes are not enough to reach all potential benefits of global operating. Companies have to listen to all stakeholders that influence and execute processes to capture more benefits of it.

10. Risk of Standardization

In quickly changing environments rigid processes inhibit organization's ability to improvise and capitalize upon new situations. Standardization could make processes inflexible so there is risk in standardization as well. According to John Seddon, who elaborated the Vanguard Method1, most of the shared service centers are only attempt to reach economies of volume but relatively few could justify the success it. He claims that most of SSCs cost more than lesser because services moved into service centers are fractionized and changed that cause flawed, repaired, duplicated and time-

[1] The Vanguard Method: this model used for service organizations and could help in change from „command and control" organization to be „system thinking" organization. In practice it means translating Lean and TPS for service organizations.

lengthened services and additionally generate failure demand as well2). According to Seddon services are not appropriate for total industrialization, depersonalization that service centers do. In these shared service centers if a demand comes from a customer it is broken down elements, sent them for specialists who will make it in prescribed time. The performance of human resource is measured as producing resources, managed by indicators, service standards and cycle time of services. There is significant difference between producing and service delivering. Customer demand stands beyond services has more variability than producing so not everything is suitable for standardization. This problem is boosted by division between front and back office functions. Because if the customer negotiates with the front office staff but the work is done by back office contributors then front office should explain the problem for back office and it always could not be succeeded entirely. And it also could be happened that front office does not know how back office could do the work. (Seddon, 2010) Seddon claims that trust in low transactional cost is fad of shared service centers and it comes from the industrial mass production thinking. The execution is based on the pattern of call centers and shared service centers where the assistance of information technology is suitable for controlling and reporting. This form concentrates on the standardized work and the staff in the hope it will reduce the costs. But according to Seddon the cost-driven industrial implementation will lead to huge failure demand because the exaggerated integration and reducing of variability that increase the cost rather decrease them. (Mellors et al., 2011)

If company discloses the real customer demand then it could be succeeded to plan delivering at transactional points and it makes unnecessarily the back office work. And if there is no back office then there is no need for large work-process management systems and task monitoring, etc.

According to Seddon if a company thinks about establishing shared service model, before starting, it should be consider the following aspects: (Mellors et al., 2011)

- examine where are the concerned services in the organization and improve them on their own place. Do not change their place only if they are redundant and able to eliminate or outsource.
- After it, company should examine the possibility for economical improvement by reduced using of common resources.
- Finally it should be examined if there is enough IT solution that improve process efficiency.

On the results of these steps companies could reach significant improvement without failure demand and sending less money for IT meanwhile creating bigger value.

11. Conclusion

Structures and processes are interrelated. If company gets the right balance among global, local, regional and local processes then it is easy to avoid duplication in organizational structure. Clear structures and not too many standardized processes could also clarify roles, help to focus internal communications.

Standardization could greatly improve process performance, lower the costs for process maintenance and be able to control better the operations. Standardization always needs senior management support because they could ensure that focus remains on the overall performance improvement.

[2] Failure demand: demand because of service failure. When demand for a former existing service is increasing because the renewed service could not deliver that customer and executives want. For example in a call center it could be generated increased phone calls if the customer could not get answer or help for its problem firstly.

There is some criticism of exaggerated standardization in shared service centers, so companies have to find the right balance in using it.

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Is Standardization Appropriate for Companies´ Front Ends? Towards Customer Centricity at the Example of Smartphone Apps for Retail Banking

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Abstract

Increased competition forces long-established companies to permanently rethink their strategies. Typically, they have to fight back low cost providers intruding into their ancestral markets. To be successful, standardization at the front end might not be a promising avenue. Instead, establishing a strong relationship with the customers and pursuing rigorous customer centricity appears to be a more viable option. First, this paper explores the concept of customer processes as an approach for companies to differentiate from their competitors. Thus, we follow a management perspective. Second, the paper presents a proposal how new technology, such as smartphone apps, can serve to build up a customer-centric business model. For this purpose, the conceptualization of a smartphone app to support customer processes is demonstrated. Third, the potential success of such an application is elaborated from a theoretical perspective of attitude formation theory. The paper is based on the example of retail banking to impart the idea as transparent as possible.

Keywords

App, customer centricity, customer process, retail banking, smartphone

1. Introduction

At the example of retail banking it becomes apparent how digitalization tore down former entry barriers and allowed new financial service providers to enter the market. Karakostas et al. (2005, p. 855) emphasize this fact as "customers are just a mouse-click away from competitors". Relinquishing brick-and-mortar branches these competitors are able to offer products at lower prices and more favorable interest rates. The entrants offer a much smaller range of products. Mostly, the products are highly standardized and automated. What can be the answer of old-established companies to hold off the intruders? Standardization at the front end does not appear to be promising for traditional banks. Hence, the emergence of new information and communication technology (IT) does not only threaten traditional banks but also open up new opportunities for these companies. In particular, these opportunities offer new ways to create customer value and to differentiate from other competitors.

One way to differentiate from low cost providers is to adjust the business model to a rigorous *customer-centric view*. In many banks, customer orientation has so far been misunderstood as just offering comprehensive advisory services and exploiting opportunities of cross-selling financial products. Still, business models are predominantly product-oriented (Shah et al., 2006). The problem with this approach is that product-orientation does not add real value since it encounters an "inside-out" perspective, i.e., convincing customers to buy products from the banks' shelves. Contrary, an "outside-in" perspective is strictly based on the customers' needs for establishing product offerings.
Hence, banks have to recognize that the need for financial services usually does not occur isolated but within a so called *customer process*. Generally, a customer process can be characterized as the entire procedure ("end-to-end process") that a customer passes through to meet a desired outcome. The initial point is a specific customer need. The process includes every step that the customer has to take until this specific need is satisfied or the problem has been solved (Behara et al., 2002). Taking customer processes into account and finding ways to link bank products to the customers´ processes or even supporting them holistically is a promising approach for differentiation (Heckl and Moormann, 2007).

For pursuing a differentiation strategy at the front end not only a business-based concept is necessary but also appropriate technology. We claim that the emergence of smartphones and related applications (*apps*) opens up new opportunities to provide support for customer processes. This paper presents the specification of a smartphone app which serves for this purpose. It delivers an approach for the holistic support of customer processes and shows how a smartphone app provided by banks can serve as a trigger to integrate the bank early into the customers' processes and to bring the bank in a favorable position – compared to a highly standardized low cost provider.
The paper is structured as follows. In section 2, prevalent approaches of banks towards customer centricity are described. In section 3, the concept of customer processes is reviewed and a motivation is provided why the support of customer processes is a valid opportunity to enforce customer centricity and to differentiate from competitors. In section 4, the functional design of a smartphone app to support customer processes is presented. The theoretical evaluation of this type of app is conducted in section 5 following the Theory of Reasoned Action and attitude change strategies. Section 6 concludes.

2. Directions of Customer Centricity in Banking

Since established banks are unlikely to succeed in a price war against low cost providers, they have to offer value adding products to their customers that clearly distinguish from competitors' offers. Differentiation in retail banking in terms of sophisticated product specifications has mostly failed. Usually the result is an increased complexity of products (e.g., certificates, exchange traded funds)

which might not be fully understood by either the customers or the advisers. In such cases, the customer might miss or even doubt the differentiating feature. The non-physical nature of bank products poses even more problems. For a customer it is not straight forward how to assess the value of an intangible product (Zeithaml et al. 2003).

Therefore, innovative approaches of differentiation, which cannot easily be copied by competitors, are required. Building up a strong relationship with the customers can be an essential factor of differentiation, especially considering low switching costs in retail banking. However, establishing an inimitable customer relation is difficult.

A number of researchers have been analyzing methods and approaches for customer-oriented banking (e.g., Karakostas et al., 2005; Shah et al., 2006; Omarini, 2011). Especially for retail banking, "satisfaction has been found to be the ultimate measure of service performance" (Neilson and Chadha, 2008, p. 204).

Being one of the new distribution channels in retail banking, interest is fast growing towards mobile devices (Meyer, 2010). This trend has been pushed by the rise of smartphones. According to Curtis (2009, p. 22) "even mobile services, which are often criticized for being user-hostile, are enjoying increased popularity on the back of the smartphone boom". Due to the boom of smartphone applications and the increase in the popularity of mobile banking, offering apps seems to be an auspicious strategy for banks to keep in close touch with their clients.

However, apps for banking should provide real value added, i.e., they should support a customer-centric strategy. We propose a type of applications that directly aim to support banking-related customer processes. Hence, the research question in this paper is: *How can the functional design of a banking smartphone app, which allows the support of customer processes, look like from a business point of view?*

The paper follows the Design Science paradigm. According to Hevner et al. (2004), Design Science research consists of the phases *Build/Develop* and *Evaluation.* In particular, this paper addresses aspects of theory building in terms of *Develop* regarding to Hevner et al. (2004). March and Smith (1995) state that this phase comprises the conceptualization of an artifact and, hence, is the most important step in Design Science. In this paper we present the conceptualization of an IT artifact, i.e., the smartphone app. The design explicitly focuses at a business perspective rather than a technical view.

3. Reasoning of Customer Processes

3.1. Defining customer processes

The chronological steps of a customer process can be derived by using the Customer Buying Cycle (CBC) (Heinrich, 2002). The CBC comprises four phases – stimulation, evaluation, purchase, and after-sales – which a customer has to pass in order to fully accomplish the buying cycle. Following the CBC, the steps of the customer process for a specific need (e.g., "housing") can be derived and the sub-needs resulting for each process step can be defined. Lots of information, services, but also financial products are demanded by the customer within this process. As a result, the customer encounters different tasks within the process, searches for solutions, and gets in touch with different suppliers to fully cover the superior need following the customer process.

3.2. Banking-related customer processes

Banks usually offer products for single parts of customer needs, e.g., financing, and neglect to identify the intrinsic need or generic desire of customers, e.g., “housing”, “raising a family”, “going on vacation”. The identification of banking-related customer processes requires a full understanding of customer needs and procedures. Thus, before applying a customer-centric business approach, the bank has to identify relevant banking-related customer processes. In a survey, Kahmer and Moormann (2005) detected for which customer processes a strong support by banks is generally desired and for which customer processes there is no need for a holistic support by banks (Table 1). The group involved in the survey was comprised of 373 participants.

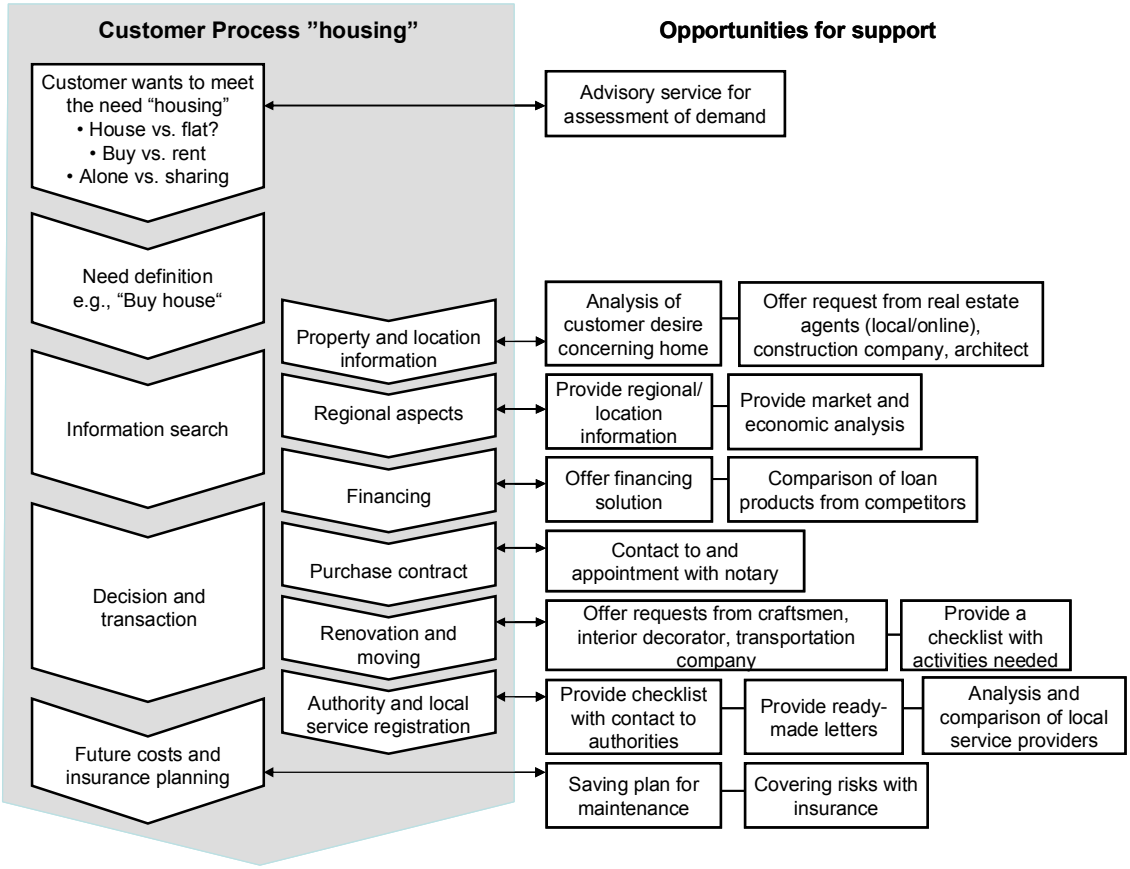
Table 1: Customer processes and the degree of desired support by banks (Kahmer and Moormann 2005)

Strong desire for support	Limited desire for support	No desire for support
Retirement	Buying or selling a car	Buying and administrating computer equipment
Buying or selling a house	Buying and protection of household goods	Travel planning
Pension Coverage	Private administration	Further (professional) education
Covering individual risk	Renting and furnishing an apartment	Renovation; home improvement
Death and inheritance process		
Asset building; financial planning		

3.3. Matching customer processes with bank processes

Based on the identified customer processes, the bank´s management can determine which processes should be handled by the bank to fulfill the customer needs. Figure 1 presents an example of the customer process “housing” and the opportunities for the bank to support this process.

Figure 1: Example for the customer process "housing" and opportunities for support



This example shows how a bank can provide comprehensive support for the customer process "housing". Within each step of this process, the customer needs support in terms of, e.g., information, services, and products from different kinds of suppliers in order to fulfill his/her superordinated need. The next step for the bank´s management is to decide which services should be accomplished by the bank and which activities should be carried out by external suppliers. These decisions are primarily based on the decision which role model to pursue. A bank could e.g. be a service integrator in a collaboration network and offer all customer process-related services to the customer, or it could join a network and participate as a service provider.

Servicing the whole process chain and producing or delivering all products, services, and information needed should not be a bank's objective. However, utilizing a smartphone app, the bank is able to deliver required information around the customer process in an integrated manner to its customers. Hence, the bank will secure its position as a primary contact point to the customer and eventually strengthen its customer relationships.

4. Design of a Smartphone App for Supporting Customer Processes

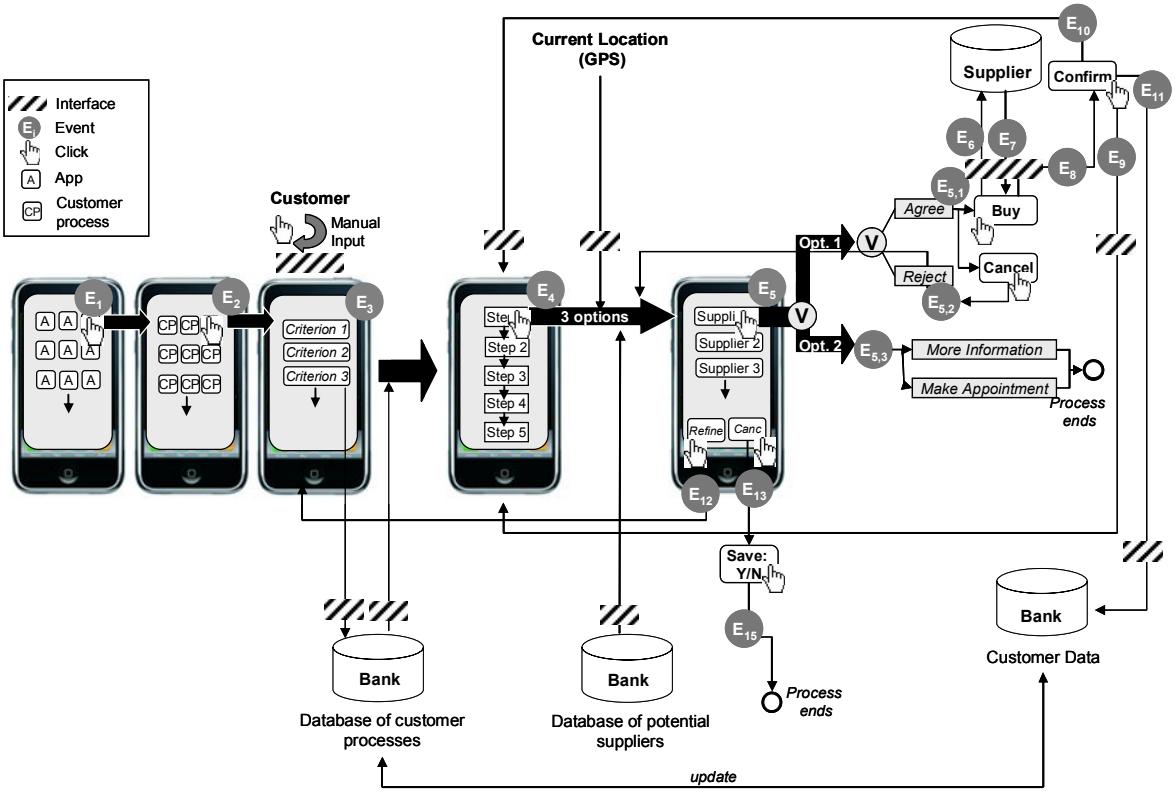
The conceptualization of a smartphone app to support customer processes in banking is exhibited in Figure 2 and briefly described in this section.

When clicking on the bank's app (E_1) a list of banking-related customer processes (e.g., "housing", "car purchase", "wealth accumulation") will be displayed. The amount and depth of customer

processes provided can be determined based on the results of Kahmer and Moormann (2005). However, each bank has to identify those customer processes which are most relevant to its own customers. This is a strategic decision because the choice of customer processes reflects the scope of the bank's service offering. Furthermore, it has to be examined beforehand which steps and which chronological sequence of steps each customer process comprises.

In the next step, the customer chooses the process he[1] is interested in (E_2). For instance, if the customer has selected the process "housing", he can individualize this process by choosing criteria according to the type of housing (rent vs. buy; commercial vs. private), location, size, etc. The criteria of choice should be predefined. Based on the data entered by the customer, the individualized customer process for "housing" will be derived and the sequence of customer process steps will be displayed.

Figure 2: Functionality of the smartphone app from a business perspective



All customer processes and the steps of each process should be stored in a "customer process database" of the bank. Here, it should also be predefined which combination of criteria chosen at E_3 leads to which version of a customer process. As a result of E_3, the smartphone user receives a graphical representation of his customized customer process where all his tasks and needs to be considered for "housing" are listed in a chronological order. This set of activities will help the customer to navigate through his process.

Clicking on one of the process steps (E_4) will result in a list of suggested services, products, and the corresponding suppliers within the respective step. For instance, within the phase of information search, step 1 of the customer process "housing" could be the specification of the need. At this point

[1] The masculine form has been chosen for easy reading.

it might be worthwhile for a customer to contact an estate agent. The smartphone app can provide suggestions for agents in the corresponding city or region. The app should further allow the customer to contact the agents directly.

In order to provide a list of suppliers for each process step, the app also needs to be connected to a database of the bank where offered products and services as well as the corresponding suppliers of the bank's cooperation network are stored. The customer can be given three options to proceed from E_4: (1) show suppliers at the current location of the mobile phone, (2) show suppliers at the location the customer had entered as a criterion in E_3, or (3) manually enter a preferred location. Conditional upon his choice, the customer receives suggestions for suppliers which can best fulfill the needs of this customer process step.

As a next step, the smartphone user can choose an offer (E_5), defined by a specific combination of a product/service and a supplier. In some cases it might *not* be appropriate to directly accept a certain offer via the app. This is especially true for most banking products where a signature is required for the contract or where the customer might have security concerns about buying the product via a mobile phone. In other cases, a direct offer to buy could be provided by a supplier, e.g., material for house renovation in the customer process "housing". Thus, there are two options depending on the kind of supplier: (a) receive a direct offer (and proceed with $E_{5,1}$ or $E_{5,2}$), or (b) get more information and/or make an appointment with a sales agents ($E_{5,3}$). For the second option, the customer can choose the relevant information or make an appointment. In case of the first option, the customer can decide whether to accept ($E_{5,1}$) or to reject ($E_{5,2}$) the offer. If the customer accepts, he can click on a "buy" button or cancel the purchasing process.

When deciding to accept the order he will be directed to the supplier's system, website, or e-shop (E_6) where the order will be identified and relevant additional information on price, conditions, etc. will be sent to the app (E_7).

The final agreement on purchase is processed by clicking on a "confirm" button (E_8). The confirmation should be conducted on the supplier's system, since all legal issues related to online-purchase will now be under the responsibility of the supplier. Moreover, there should be a connection from the supplier's system to the app for the purpose of (a) sending a confirmation and the related documents – e.g., confirmation, guarantee – after successful purchase (E_{10}) and (b) sending information that initiates an update of the individualized customer process (E_9). Depending on the products or services acquired after-sales offers might change. After confirmation, the purchasing information can also be sent to the bank's database in order to update the customer data (E_{11}) which e.g. can be used for marketing purposes.

If at node E_5 the customer denies to agree to any offer, he will be redirected to the supplier suggestions (E_5). The customer might further be given the opportunity to refine the criteria he entered at E_3 (E_{12}) or to finish the app (E_{13}). The latter choice should offer the option to save the individualized customer process (E_{15}).

The primary purpose of the presented app should be to serve as an interface between the customer, the bank, and the suppliers within a cooperation network. Thus, the app should mainly work as a service broker and should *not* be involved in the actual purchasing process.

5. Theoretical Evaluation of the App

An increased acceptance of bank products due to the support of customer processes via the suggested smartphone app can be justified following the Theory of Reasoned Action (TRA) (Ajzen, 1991; Peter and Olson, 2005) and attitude change strategies (Peter and Olson, 2005).

Consumer behavior is a wide topic in marketing literature. Within the context of this paper we focus on "buying a product" as a behavior (Peter and Olson, 2005). All conclusions about effects on the buying behavior to be drawn in the following are limited to the *intention* to perform this behavior since it is not possible to predict the actual behavior of a consumer.

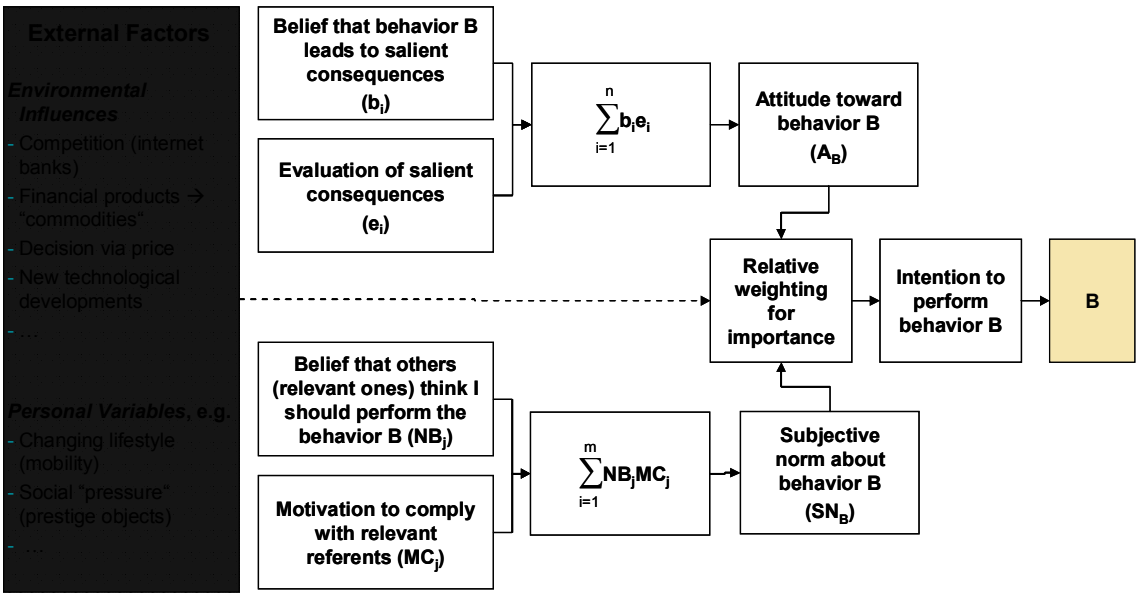
Beliefs towards an object "constitute an associative network of linked meanings stored in memory" (Peter and Olson, 2005, p. 140). They are determined by the knowledge about the product and its attributes. Beliefs can, e.g., be structured following the *Means-End-Chain*. This chain specifies that each product *attribute* has to lead to *functional consequences* to be a belief which further lead to *psychological consequences* and, in turn, *personal values*. The activated beliefs are called *salient beliefs*. Only the salient beliefs about an object (those that are activated at a particular time and in a specific context) create a person's attitude towards that object (Fishbein and Ajzen, 1975; Mitchell and Olson, 1981).

The consumer forms his attitude towards an object by a combination of his "knowledge, meanings, and beliefs about a product" or behavior in order to generate an overall evaluation (Peter and Olson, 2005, p. 142). One of the most prominent models in this context is the *Multiattribute Attitude Model* by Fishbein and Ajzen (1975). It "accounts for the integration process by which product knowledge (the evaluations and strengths of salient beliefs) is combined to form an overall evaluation or attitude" (Peter and Olson, 2005, p. 143).

The *Theory of Reasoned Action (TRA)* generally follows the conceptual framework depicted in Figure 3, exemplified by the behavior "Applying for a loan". The intention to perform any behavior is determined by the person's attitude towards the behavior (A_B) on the one hand and the subjective norm about behavior B (SN_B) on the other hand. Furthermore, external factors influence the relative weighting of importance of both determinants. Salient beliefs, or in this case salient consequences of a behavior, determine A_B. The attitude is formed following the Multiattribute Attitude Model and consists of the sum of beliefs that the behavior leads to *n* salient consequences (b_i) times the sum of the evaluation of these salient consequences (e_i) (Peter and Olson, 2005). The former one (b_i) can be interpreted as the strength of association between the behavior and the salient consequence and the latter one (e_i) as the evaluation of this link. The evaluation can be positive or negative and can incorporate different magnitudes.

The belief that others (relevant ones) support pursuing the behavior times the motivation to comply with the reference group (e.g., family, friends) determines the subjective norm towards a behavior. For instance, for the behavior "Applying for a loan", salient consequences could e.g. be: "I can buy a house", "I have to pay interests", "I have liabilities to a bank". Each of them is evaluated by each person differently. For example, "I can buy a house" would incorporate a positive evaluation whereas "I have liabilities to a bank" would be evaluated negatively. Considering the formation of the subjective norm it is possible that in the opinion of the reference group the person should not get into debt. The motivation to comply with this group is increased if these persons are very important to him, such as the family. In addition, external factors, like current interest rates or the need for a new house, further influence the intention to apply for a loan.

Figure 3: Framework for TRA, examplified for the behavior (B) „Applying for a Loan“ (based on Peter and Olson, 2005)



It is well conceivable that the attitude towards the behavior of applying for a loan generally includes salient beliefs that are evaluated more negatively (like paying interests). Applying for a loan is merely a necessity to fulfill individual wishes. Furthermore, the subjective norm will not be positive; nobody will encourage someone to apply for a loan if there is no actual need for it. The question is how the support of customer processes via the smartphone app can change the attitude or the subjective norm, i.e., how the customer can be *persuaded*.

Response changing can for example be achieved following several attitude change strategies. Basically, any attitude towards an object or a behavior can be changed by (a) adding a new salient belief, (b) increasing the strength of an existing positive belief, (c) improving the evaluation of a strongly held belief, and (d) making an existing belief more salient (Peter and Olson, 2005).

Following these strategies, a smartphone app like the one presented in this paper can be expected to change the attitude towards the behavior of buying bank products due to the following reasons. As an example the customer process “housing” and the core banking product within this process, ”Applying for a loan” is chosen for demonstration. In Table 2 possible consequences of using the smartphone app leading to changes in the attitude towards “Applying for a loan” are provided.

Table 2: Possible attitude changes due to the usage of the presented smartphone app

Attitude change strategy	**Expected consequences of using the app**
Add a new salient consequence	Supporting the complete customer process does not only add convenience to the customer but can also add new salient impacts to his behavior of applying for, e.g., a loan. These salient consequences can be beneficial for the bank. This is especially relevant for cross-selling other bank products with regard to the customer process "housing". In a traditional setting a customer would ask for a loan in isolation from his superordinated process. In this case he would probably not think about other bank products or services he might need in conjunction with the real estate. In case he gets support for his process via the smartphone app by providing the sequence of process steps he needs to accomplish, the customer will recognize that he might also need further services. Thus, the smartphone app links "applying for a loan" to new salient requirements like "I need insurance" or "I need financing for my new furniture" via the customer process.
Increase the strength of a positive consequence	One consequence of applying for a loan will be the possession of the real estate. This will be evaluated positively by customers. However, the association of this consequence might not be very strong, if other consequences like "paying interests" or "having liabilities" are more prevalent. A smartphone app supporting the complete customer process might change the strength of the association with "possessing the real estate" with the behavior "applying for a loan". Being permanently involved in needs resulting from other steps of his process, the customer is constantly reminded of the physical object the loan will enable and the wish that it will satisfy. Furthermore, showing pictures of houses, maybe even in the current location of the smartphone, will lead to a stronger association of "applying for a loan" with a specific house. As a consequence, this might lead to more positive associations because of feelings like "I want *that* house!".
Improve the evaluation of a strongly held belief	A salient consequence strongly associated with applying for a loan but evaluated negatively is "I have to pay interests". The direct evaluation of this salient consequence cannot be improved, since a person will never develop a positive association to "paying interests". However, if the customer uses the smartphone app, he is guided through his process and permanently reminded of the real estate. Thus, the required payment of interests might be weakened in its importance for the formation of the overall attitude. Other salient consequences like "possession of the real estate" might become more important instead.
Make an existing belief more salient	In cases the consequence "I get this house" is not a salient one, the direct association of the bank products with the superior need of the customer process might make the possession of the house as a positive consequence of applying of a loan a more salient belief.

6. Conclusion and Future Research

Standardization is a necessity in many areas, headmost in back office operations. In regard to front ends the situation is different. At the example of retail banking it can be observed that new entrants into the market usually offer a very limited spectrum of channels, products, and services. Hence, answering in the same way is no option for long-established banks. They need to differentiate and to create value added to their customers to ensure a competitive advantage and to stay in the market. Although establishing a strong relationship with the customers and pursuing rigorous customer centricity appears to be appropriate for differentiation strategies companies are still reluctant in identifying and supporting the processes of their customer. Also, the related literature has not yet elaborated this area sufficiently.

This paper contributes in this domain by applying the concept of customer processes as an approach for companies to differentiate from their competitors and by demonstrating how new technology, such as smartphone apps, can be utilized in order to create functional value to the customers. In

addition, the smartphone app enables to arouse emotional value. People nowadays are often devoted to their mobile devices such as smartphones, and it can be expected that this trend will further increase. Today's Generation Y is expected to place much more importance to their mobile device than the "traditional" desktop internet access.

The approach delivered here enables companies to better integrate themselves into people's lifestyle and their processes to position their products and services as an essential part of life events. Furthermore, the potential success of such an application is elaborated from a theoretical perspective of attitude formation theory. The proposed approach is usable in all industries. The example of retail banking has been chosen to make the idea as plausible as possible. The approach has been developed from a business rather than a technological perspective.

The results of the paper open up several avenues for further research. The described functionality of a smartphone app has to be regarded as a first conceptualization of a new IT artifact, and as such as an initial step of a more comprehensive design science research project. Subsequent stages of our research will seek empirical validation of our hypotheses that assume benefits to the stakeholders involved. This indicates also an analysis if the proposed theoretical evaluation, based on the attitude formation theory, holds as well in an empirical context.

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The Shift of the Current Financial Crisis Into a European Sovereign Debt Crisis: What Lessons Can We Learn?

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Abstract

This paper discusses several key issues regarding the European twin sovereign debt and banking crises. The shift of the current financial crisis into an European sovereign debt crisis is afforded analyzing how was it that via the banking system the contagion was extended from the US to Europe. The explanation focuses on the imbalances of European Monetary Union countries balance-of-payments. These are very difficult to adjust because of the new experience of a monetary Union of independent political countries which maintain different and not completely convergent fiscal policies: a situation which is different from traditional monetary unions of States belonging to the same political Union. The European crisis has shown that crises can spread quickly among closely integrated economies, either through the trade channel or the financial channel, or both. In an integrated region, no country can isolate itself from surrounding troubles. The crisis has exposed a major deficit of executive decision-making capability in the EU and Eurozone institutional framework, which helps to explain the insufficient policy response. It can thus be said that the banking and sovereign crises are compounded by a crisis of the EU institutions themselves. Therefore, a successful crisis resolution requires more political integration, which will need to include: first, a mechanism that ensures that fiscal policies in the Eurozone are partly centralized; and second, a framework for banking policy at the European level that credibly supports the vision of a single European market for financial services.

Keywords

Financial crisis, sovereign debt crisis, banking crisis, economic breakdown

1. The Shift of the Current Financial Crisis Into a European Twin Sovereign and Banking Crisis

One aspect of global contagion is the extension of the current financial crisis from the US to European countries. It began with Greece, but suddenly it spread over some other countries of the Eurozone like Portugal, Ireland, Italy and Spain (shortly indicated as the PIIGS countries).[1] Europe currently faces a severe financial crisis. It is often described as a sovereign debt crisis, but in fact it is really a sequence of interactions between sovereign problems and banking problems. The sovereign debt crisis has been directly linked to the global financial crisis and the ensuing problems of European countries' banking sectors after the bankruptcy of Lehman Brothers. With deteriorating public finances, sovereign risk has increased and worsened bank's balance sheets. So the situation is best described as twin sovereign and banking crises that mutually feed each other and the result of this interaction is a gradual contagion to more countries and more asset classes (Véron, 2011).

The origins of the European debt crisis can be directly traced back to the global financial crisis of 2007–2009, which spilled over into a sovereign debt crisis in several euro area countries in early 2010. To offset sharp falls in output, euro area governments (as governments in the rest of the world) responded with counter-cyclical fiscal policies that increased fiscal deficits. Moreover, fiscal positions worsened as tax revenues declined and transfer payments grew larger due to rising unemployment during the crisis. In many countries, government bailouts of banking systems also contributed to an increase in public debt. Private debt became public debt, be it through banking crises or the burst of housing bubbles, leading to sovereign crisis. The debt crisis in several member states of the euro area has raised doubts about the viability of European Monetary Union (EMU) and the future of the euro. The crisis has highlighted the problems and tensions that will inevitably arise within a monetary union when imbalances build up and become unsustainable (Volz, 2012).

The Eurozone sovereign crisis started when the government of Greece, freshly elected in October 2009, revealed that its predecessor had misled its Eurozone neighbors and the public about the true state of the country's public finances. The budget deficit for 2009 was 12.7% of GDP, more than double the previously published figure. This raised serious doubts about the country's ability to repay its debt. On December 2009, rating agencies downgraded Greek debt below investment grade. Government bond yields rose to unsustainable levels and by the end of April 2010 Greece turned to the European Union (EU) and the International Monetary Fund (IMF) to activate a €45 billion bailout package. By early May 2010, the EU-IMF rescue package had to be increased to an amount of €110 billion over three years.

Soon after Greece's bailout, since 2010 EU decided to set up an European Financial Stabilisation Facility (EFSF) with €440bn financial firepower to intervene in similar situations. Simultaneously, the ECB initiated a "Securities Markets Programme" under which it buys sovereign debt of troubled countries in secondary markets. Subsequently, the EFSF and IMF jointly agreed to provide conditional assistance packages to Ireland (November 2010) and Portugal (April 2011).

In July 2011, further assistance to Greece was decided by the Eurozone heads of state and government. A relatively mild debt restructuring scheme, euphemistically known as "private sector involvement" (PSI), was made a condition for the new assistance package to Greece, whose outline was announced on July 21st, 2011. Therefore, in March 2012 a new package of €130 billion to Greece was approved by the EU and IMF after Greece's creditors agreed to PSI to restructure Greek

[1] The potential mutation of the financial crisis into a sovereign debt one in Euro area countries is investigated by Candelon and Palm (2010), and De Grauwe (2010). More in general, Sturm and Sauter (2010) analyze the impact of the financial crisis on Mediterranean countries, while Wyplosz (2010) contrasts the United States and European situations during the crisis and examines how much of the crisis has been imported by Europe from the US. The paper argues that Europe never had a chance to avoid contagion from the US. Finally, the strong relation existing between the soundness of the public budgets and the international financial stability for the Italian case is illustrated by Banca d'Italia (2010).

government bonds, which implied losses of up to 75%. More than 85% of private bondholders agreed to the deal, but not doing the agreement could have meant that Greece would not qualify for more bailout money and could have faced default.[2]

The bailout, however, failed to restore market trust in the Greek economy. Moreover, it failed to halt contagion of the crisis to other countries of the euro area. In particular, the Greek crisis and the hesitant political response from the other European countries raised concerns over the debt situation and the structural and competitiveness problems of the economically weaker periphery member countries of the euro area. As a consequence, the borrowing costs for the PIIGS countries increased significantly and the cost of insuring sovereign debt against default soared as trust in their ability to repay vanished.

The interdependence between sovereign credit and banking systems has been a running theme of this sequence of events. Eurozone sovereign debt assets are held in large amounts by Eurozone banks, with a significant bias for the bonds of the country in which the bank is headquartered but also significant cross-border exposures to other Eurozone countries' sovereign debt. This is partly due to policy choices before the crisis which in retrospect appear questionable, particularly the risk-weighting at zero of Eurozone sovereign bonds in regulatory capital calculations, the longstanding acceptance of such bonds with no haircut by the ECB as collateral in its liquidity policies, and possible instances of moral suasion by home-country public authorities that resulted in large holdings of the home country's sovereign debt (Véron, 2011).

Between 2007 and 2010, the debt to GDP ratio of the euro area increased from 66.3% to 85.4%. Greece is a special case in the sense that the level of Greek debt had already been very high before the crisis, at 107.7% of GDP in 2007. Greek debt, which has been on a continuous rise since 2003, reached a level of 144.9% of GDP in 2010. Like Greece, Italy had a debt level above 100% of GDP prior to the crisis, but unlike in the case of Greece the debt to GDP ratio fell between Italy's adoption of the euro in 1999 and 2007.

Among euro area countries, the most dramatic increase in public debt occurred in Ireland, where the country's debt problems can be clearly ascribed to the country's banking crisis. Ireland did not have a fiscal or debt problem until 2008. Indeed, between 1997 and 2007, Ireland had a fiscal surplus every year except for 2002, when the government recorded a tiny deficit of -0.4% of GDP. Accordingly, the Irish debt to GDP ratio declined steadily over this period from 64.3% in 1997 to 24.9% in 2007, with Ireland being one of the EU countries with the lowest public debt burden. The situation changed in the course of the Irish banking crisis in September 2008 when the Irish government, under pressure from European governments and institutions (including the ECB) but also from the US government, guaranteed most liabilities of Irish-owned banks (Regling and Watson, 2010; McMahon, 2010). The government guarantee was initially €400 billion but was later increased to €440 billion. As a consequence, the Irish deficit ballooned and the debt to GDP ratio shot up from 24.9% in 2007 to 94.9% in 2010. The ensuing deterioration of Ireland's access to capital markets in the autumn of 2010 led it to seek an international financial rescue package by the IMF and the EU over €90 billion in November 2011 to finance its borrowing and bank recapitalization needs.

Like Ireland, Spain did not have a fiscal or debt problem before 2008. In the period 1999–2007, Spain had an average annual budget surplus of 0.3% of GDP. In 2007, Spain even recorded a fiscal surplus of 1.9%. Until the outbreak of the global financial crisis, Spain did not violate a single time the EU's Stability and Growth Pact (SGP).[3] Spain's fortunes changed when the global financial crisis put an abrupt end to a long cycle of high growth (which started around 1996) that had been accompanied

[2] For details of the PSI agreement, see Kirkegaard J. F. (2012).

[3] The SGP requires EU member countries to have an annual budget deficit no higher than 3% of GDP and a national debt lower than 60% of GDP or approaching that value.

by a construction and real estate boom (Suarez, 2010). When output contracted in 2008, the Spanish housing bubble burst and destabilized the banking system. The Spanish fiscal position deteriorated, with Spain recording fiscal deficits of -4.5% in 2008, -11.2% in 2009, and -9.3% in 2010. Spain's public debt rose from 36.5% of GDP in 2007 to 61.0% of GDP in 2010. Even in Portugal, which was the first country to breach the SGP in 2002 and which had seen a steady increase of its debt to GDP ratio since joining the euro area in 1999 (when debt stood at 49.6% of GDP), the by far largest increase of public debt occurred during and after the 2008–2009 crisis, with debt rising by 26.6% from 68.3% in 2007 to 94.9% in 2010 (Volz, 2012).

2. Mispricing of Risk, the Balance of Payments Crisis, and the Misalignment of Internal Real Exchange Rate

According to Volz (2012), an important element that contributed to the European financial crisis was a mispricing of risk by capital markets and an ensuing misallocation of capital in the decade before the outbreak of the crisis. European monetary unification brought about a convergence of interest rates among euro area members. Countries with weaker positions which introduced the Euro could refinance themselves roughly at the same cost as the most solvent states. Spreads of sovereign bonds of the PIIGS over Germany narrowed rapidly in the run-up to EMU membership and almost disappeared once they had become members of the euro area (Figure 1). By January 2001, the time of Greece's entry into the euro area, the yields on 10-year Greek bonds had fallen to 5% from 25% in 1992. Sovereign risk of virtually all euro area countries, including the PIIGS, was priced more or less the same as German sovereign debt. Financial markets were irrationally optimistic, depending on the fact that the risk of euro area central government bonds was weighted at zero in regulatory capital calculations and because the ECB treated such debt with no haircut - basically as risk-free collateral - when these were offered as collateral for repos and other collateral financing trades (Véron, 2011). Buiter and Siebert (2005) early highlighted this problem, maintaining that the ECB's open market operations created moral hazard by not discriminating sovereign risk within the euro area.

Mersch (2011, p. 6) points to flaws in the Maastricht Treaty. At the very core of that framework the no-bail-out clause and the SGP were installed. The first should have excluded free rider incentives and the second should have aligned national fiscal policies to prevent negative spillover effects to the currency union as a whole. The SGP was a compromise of quantifying fiscal soundness without interfering with the budgetary and fiscal policies of sovereign states. It aimed to maintain fiscal discipline within EMU. Member states adopting the euro had to meet the Maastricht convergence criteria, and the SGP should make sure that they continue to observe them. The compromise was also characterized by the strong belief that governments would be reactive to market discipline. The spirit of the Stability and Growth Pact was also characterized by a strong belief in the power of free markets to discipline governments.

But the global financial crisis has undoubtedly marked a turning point also in that context. With hindsight, it is now obvious that the availability of cheap credit led to an unsustainable accumulation of private (as in Ireland, Portugal, and Spain) and public (as in Greece and Portugal) debt in today's crisis countries. The drop in real interest rates in the periphery countries after their entry into the euro area and the inflowing capital fuelled unsustainable developments, including excessive credit dynamics and real estate bubbles in Spain and excessive fiscal spending in Greece. It also reduced the pressure for economic reform to improve competitiveness within the monetary union as countries could easily finance their current account deficits through abundant inflowing capital.

A high level of public debt is not a problem *per se*, as long as the government is able to refinance itself and roll over its debt. This requires public debt and the interest burden to grow more slowly than the economy and the tax base. This is not the case in the PIIGS anymore. Today's debt crisis in

the PIIGS is therefore not merely a debt crisis; it is first and foremost a competitiveness and growth crisis that has led to structural imbalances within the euro area (Bergsten and Kirkegaard, 2012; Mayer, 2011). In fact, below the surface of the sovereign public debt and banking crises lies a balance of payments crisis, caused by a misalignment of internal real exchange rate.

According to Mayer (2011), until the beginning of the Eurocrisis in 2009, EU officials tended to ignore the current account imbalances among EMU member countries. Some of them, who failed to grasp the difference between a common currency area within a political union and a currency union of politically sovereign states, even insisted that these imbalances were irrelevant. As long as financial markets were buoyant and credit easily available at rock bottom cost for borrowers of differing quality, the flaw in this argument was not laid bare. This changed abruptly when risk appetite in credit markets plunged in the course of the financial crisis and EMU member countries with high government deficits or debt and a bleak economic outlook experienced a “sudden stop” of capital inflows and even net capital outflows.

On the surface, the “sudden stop” has led to a government funding and banking crisis. In response, EU authorities began to extend financial support - associated with pressure for fiscal adjustment - to the affected countries while the ECB supported the banks. Below the surface, however, - as Mayer points out - lies a balance-of-payment-crisis, which has so far received only scant attention. Recall that the balance of payments is defined as the sum of the current and capital account. In a floating exchange rate system, the balance of payments is always zero as the exchange rate adjusts so as to equilibrate the current with capital account balance.

In a fixed exchange rate system, however, balance of payment imbalances can emerge when the exchange rate is above or below its equilibrium value. In the first case, when the exchange rate is overvalued, a country imports more than it exports so that the current account moves into deficit. At the same time, domestic asset prices in foreign currency are higher than foreign asset prices so that investors sell the first and buy the latter. This leads to net capital outflows and hence a deficit in the capital account. The combined deficits of the current and capital accounts then lead to a deficit of the balance of payments. Traditionally, balance of payment deficits have been funded by the sale of international reserves of the central bank. When the stock of reserves is depleted and the central bank can no longer fund the balance of payments deficit, the exchange rate drops so as to restore current and capital account balance.

In the second case, when the exchange rate is under-valued, the current and capital accounts and hence the balance of payments are in surplus and the central bank accumulates international reserves. This process comes only to an end when reserve accumulation has increased the money supply to an extent that inflation rises to intolerable levels and the authorities up-value the exchange rate in an effort to regain price stability. Since EMU has been built as a union of sovereign states, each state has retained its own national central bank, which has become a member of the so-called Eurosystem with the ECB at the top. National inter-bank payment systems have been merged into a euro area interbank payment system (Target2), where national central banks have assumed the role of the links between countries. A key consequence of this system is that each euro area country has a national balance of payments in the form of the net position of its central bank within Target2. This net position can result in a claim (balance-of-payment surplus) or liability (balance-of-payment deficit) against the ECB, which sits in the centre of the payment system.[4]

Therefore, according to Mayer (2011), the consequence of this system is that a country with a balance of payments deficit automatically receives unlimited funding. Take the example of a country

[4] On April 2012, for instance, Germany had a claim position of €673 billion against the ECB, while Spain and Italy had a liability position of respectively €271 billion and €267 billion. The total of PIIGS countries had a liability position of €810 billion.

which, due to an over-valued internal real exchange rate and a large government budget deficit, has a current account and capital account deficit (with the latter due to capital flight as residents exchange over-valued domestic assets against foreign assets). As the banks extend credit to an over-indebted government and an uncompetitive private sector, they are considered unsafe and are therefore cut off from private sources of funding. To ensure solvency, the banks in this country receive credit from their national central bank, which acts on behalf of the ECB. Thus, reserve money flows from the ECB to fund payment outflows induced by the current and capital account deficits. While banks in the country with the overvalued internal real exchange rate rely primarily on their national central banks and the ECB for funding of their balance sheets, banks in the country with the undervalued exchange rate that receive the payments have plenty of liquidity and therefore do not need ECB funds. Hence - Mayer concludes - the ECB's funding operations become tilted towards the countries with overvalued exchange rates.

So, the lacklustre growth performance in the euro area periphery over the past years has been due to an erosion of competitiveness, both against other euro area countries and the rest of the world. The domestic booms resulting from low real interest rates and capital inflows after accession to EMU led to large wage increases in excess of productivity growth and hence rising unit labor costs and higher price inflation than in Germany and other "core countries" of the euro area. The result was an erosion of competitiveness of peripheral members of the euro area vis-à-vis the core countries, in particular Germany, which has been able to improve its price competitiveness significantly since the launch of the euro through wage constraints and structural reforms (Weidmann, 2011).

So far, the structural imbalances, reflected by high current-account deficits of the periphery countries and matching surpluses in core countries, are at the heart of the current problems, since – as Volz (2012) points out - a lack of competitiveness impedes the periphery countries' chances of growing out of the crisis. To service their debt, deficit countries essentially need to become surplus countries. However, the fact that the PIIGS are members of a monetary union and hence cannot restore competitiveness by means of currency devaluation makes the adjustment much more painful. An internal devaluation requires harsh structural adjustments and real wage cuts to push down costs. This is politically much more difficult to administer than one-off currency devaluation. As emphasized by Véron (2011), Weidmann (2011) and others, besides fiscal adjustment and bank restructuring, structural reforms that enhance the crisis countries' growth potential are an indispensible dimension of any successful crisis resolution. It is the difficulties of economic adjustment, which require unpopular public policies that have caused markets to doubt the solvency of the periphery countries.

3. Erratic Responses and Tensions Among Euro Area Governments

The crisis is not merely an economic crisis. It is also a political crisis, stemming from erratic responses and tensions among euro area governments - representing surplus and deficit countries with contradictory interests - quarrelling over the right crisis diagnosis and response. According to Volz (2012), European leaders were caught wrong-footed in 2010, as they believed that a balance of payments crisis was impossible *within* a monetary union. Since such a crisis was not considered a priori, no crisis resolution mechanism had been put in place. European policymakers hence faced the challenge of crafting a crisis response from scratch in the midst of crisis, first agreeing on bilateral lending to Greece and, when this appeared insufficient, on the creation of the EFSF and the European Financial Stability Mechanism (EFSM). This task has been complicated not only because the negotiations involve a large number of parties,[5] but also because the chosen crisis resolution measures have serious ramifications for the long-term institutional framework and functioning of the

[5] Besides the governments of the euro area member countries and the other EU members, the European Commission, the ECB, and the IMF have been involved.

monetary union. As Bergsten and Kirkegaard (2012, p. 6) note, achieving the dual policy goals of solving a current crisis while trying also to prevent the next one - and using the same policy tools to do both - is rarely easy.

The fears of the surplus countries, led by Germany, that an easy bailout of Greece would set a negative precedent and create moral hazard problems with other deficit countries - especially the larger euro area members Spain and Italy, both of which are considered "too big to save" - prevented a quick resolution of the Greek crisis and led to piecemeal solutions, which were never comprehensive enough to end the crisis, and eventually caused contagion to other weak euro countries. Worries of moral hazard and a "transfer union", where deficit countries would have to be financed permanently through direct or indirect transfers and subsidies, made surplus countries also reluctant to endorse proposals such as those for eurobonds (Delpla and Von Weizsäcker, 2010 and 2011) or a partial guarantee of all euro area sovereign bonds by the ECB (Wyplosz, 2011).

A crisis resolution has been further complicated by the EU's legal framework. In particular, the so-called "no bailout" clause (Article 125 of the Treaty on the Functioning of the European Union) prohibits that a member of the EU assumes the debts of another. Also, Article 123 of the Treaty on the Functioning of the European Union forbids direct ECB credit to public institutions so as to avoid monetary financing of fiscal deficits. The slow negotiation processes between governments, which have needed to secure support from their domestic constituencies, have evoked the impression of a European political system that was ill-equipped to handle a financial crisis and lost control of events, turning a manageable solution into an increasingly unpredictable entanglement, in which potential losses are rising exponentially (Ortiz, 2011).

The European crisis has illustrated once more that any fixed exchange rate arrangement (including monetary union) is prone to crisis if countries do not adjust their economies internally and imbalances are allowed to grow too large. If economic policies are not able to keep the domestic price level competitive vis-à-vis the rest of the integrating area, and external adjustment via the exchange rate are precluded, real exchange rate appreciation will erode the countries' competitiveness. In most cases this will lead to current account deficits that at some point will trigger a balance of payments crisis.

Just like the 1992 crisis of the European Monetary System, the regional fixed exchange rate system that preceded EMU, the current European crisis highlights the dangers that advanced monetary integration brings in the face of economic and political divergences. Macroeconomic imbalances within any kind of fixed exchange rate system will cause problems at some point. And these will be exacerbated by political divergences. A high level of political agreement and commitment is needed among countries to pursue successful monetary integration, as well as close macroeconomic and fiscal coordination.

Prior to monetary unification, Europe had a discussion on the right strategy for monetary unification, with two opposing schools of thought, the "Nike approach" vs. the "coronation theory" of monetary unification. The Nike approach ("just do it"), which assumed that economies would converge endogenously once monetary union is completed, seems flawed with hindsight. Rather, the coronation theory (or Bundesbank view) which argued that monetary union should be the crowning achievement after a long process of convergence and political integration seems vindicated.

4. Concluding Remarks

The European crisis has highlighted that international financial integration will not automatically lead to an efficient allocation of capital, as predicted by neoclassical theory. The SGP's belief in the ability

of free markets to efficiently allocate capital and discipline governments was certainly not warranted (Mersch, 2011). What we have seen instead, is that unrestricted financial integration in the euro area contributed to the development of unsustainable imbalances and bubbles. While financial markets underpriced sovereign risk in the euro's first decade, the pendulum has swung back and gave way to excessive pessimism about the periphery countries' ability to repay their debt.

The European crisis countries are currently experiencing what a large number of developing and emerging countries went through over the past decades: a period of strong, yet unsustainable output growth fuelled by capital inflows comes to a halt at some point, leading to a "sudden stop" or reversal of capital flows (Reinhart and Reinhart, 2009). This pattern, which has often been repeated in the modern era of global finance, and now once more in Europe, should give pause to seriously reconsider the costs and benefits of international financial integration. Fortunately, the global financial crisis and now the European crisis have not only given impetus to fresh academic thinking on this matter, but also led the IMF to reconsider its position on capital account management and regulation of international capital flows (Ostry et al., 2010, 2011).

We should consider carefully which types of capital flows may be beneficial for their long-term development, and which may not be, given that financial institutions engaging in cross-border activities increase systemic risk and pose serious regulatory challenges. A pragmatic approach to capital account management, however, does not need to stand in contrast to regional financial integration. But the question of which sectors of financial markets should be integrated and to which extent needs to be addressed. As seen time and again, a greater degree of international (including regional) financial integration increases contagion risk; the crisis of a small European economy (Greece) triggered a full-blown European crisis not only because Greece happens to be a member of the euro area, but because banks and other financial institutions from other EU countries had built up exposure to Greece.

Since regional financial integration would require at least partial liberalization of domestic financial regulations and cross-border restrictions on financial services and financial flows, the regulatory architecture needs to keep pace with financial integration. In financially integrated areas, close cooperation between national regulators is needed. The European crisis has shown that crises can spread quickly among closely integrated economies, either through the trade channel, or the financial channel, or both. In an integrated region and world, no country can isolate itself from surrounding troubles. Since effective regulation, surveillance, and monitoring are the best crisis prevention, one should reinforce efforts to strengthen the regional financial architecture, in complement to strengthening domestic regulatory capacities and global financial cooperation.[6]

An important lesson of both the global financial crisis and the European crisis is that regulatory authorities must not focus only on microprudential regulation and supervision of individual financial firms. Rather, regulatory authorities need to try to identify and manage systemic risk, i.e., the risks imposed by interlinkages and interdependencies in a market, where a triggering event, such as the failure of a large financial firm, could seriously impair financial markets and harm the broader economy (Volz, 2012).

[6] Steps towards the creation of European supervisory authorities to help oversee Europe's financial sector from a pan-European perspective were taken only in late 2008, when the president of the European Commission mandated a high-level expert group on financial supervision in the EU. The expert group, led by Jacques de Larosière, proposed three new supervisory authorities, which were established in November 2010 and started operation in January 2011: the European Banking Authority (EBA) based in London, the European Securities and Markets Authority (ESMA) based in Paris, and the European Insurance and Occupational Pensions Authority (EIOPA) based in Frankfurt. These three supervisory authorities were complemented by the creation of the European Systemic Risk Board (ESRB), which is responsible for the macro-prudential oversight of the financial system within the EU and which has a secretariat hosted by the ECB.

In conclusion, according to Véron (2011), the key points of European debt crisis are the following: First, Europe's banking system has been in a continuous stage of systemic fragility since 2007-08, in contrast with the US where banking crisis resolution was swifter and was essentially completed in 2009. Second, had Western Europe's banks been in a better shape a year and a half ago, the policy approach to the Greek debt crisis would have been entirely different, possibly allowing for a much earlier sovereign debt restructuring. Third, the crisis has exposed a major deficit of executive decision-making capability in the EU and Eurozone institutional framework, which helps to explain the insufficient policy response. It can thus be said that the banking and sovereign crises are compounded by a crisis of the EU institutions themselves. Specialized European bodies, primarily the European Central Bank (ECB), have partly bridged this gap with policy initiatives that go beyond a narrow reading of their mandate, but they could do so only to a limited extent that has not been sufficient to stop the contagion.

Therefore, a successful crisis resolution will need to include at least four components at the European level, in addition to steps to be taken by individual countries:

a) a fiscal union, i.e. a mechanisms that ensure that fiscal policies in the Eurozone are partly centralized with shared backing across countries so as to meet the requirements of monetary union;
b) a banking union, i.e. a framework for banking policy and banking supervision at the European level that credibly supports the vision of a single European market for financial services;
c) an overhaul of EU/Eurozone institutions that would enable fiscal and banking unions to be sustainable, by allowing centralized executive decision-making to the extent necessary and by guaranteeing democratic accountability; and finally
d) short-term arrangements that chart a path towards the completion of the previous three points, which is bound to take some time.

The latest European summit of the heads of state and government, held in Brussels on June 28th and 29th, moved in that direction as Europe's political leaders committed themselves to the creation of a banking union and a unified banking supervision to be complited before the end of this year, and they also decided that troubled countries and their banking systems could directly access to euro-zone rescue funds. They also stressed, again, that a successful crisis resolution in the long run requires more political integration.

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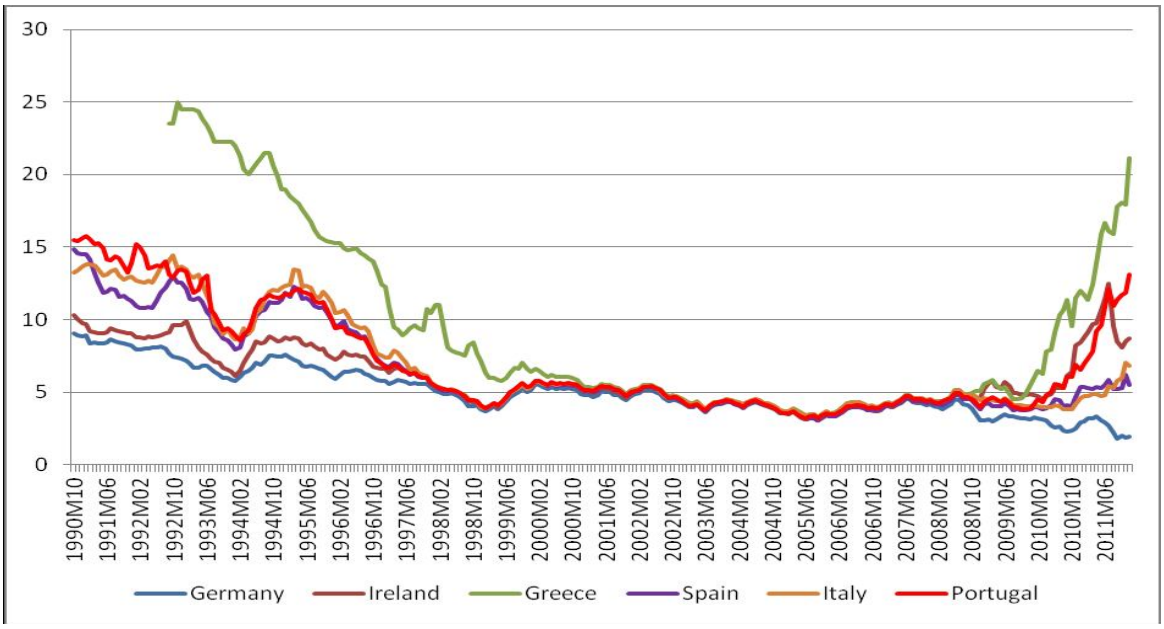
Figure 1: 10-Year Government Bond Yields (% per annum), October 1990–December 2011



Sourse: Volz (2012) with data from Eurostat.

Ownership and Wages: Spatial Econometric Approach

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Abstract

The aim of our paper is to disentangle the relationship between ownership and wages using cross-section data for Slovenian medium size and large companies, where we account for spatial dependencies in wage determination. Space here is not considered in geographical context, but as a set of relations between firms originating from the same owner. Using a detailed database on Slovenian ownership, we apply a spatial econometric approach to detect any ownership-based wage spillovers, while accounting for different standard factors, such as size, capital intensity and productivity, and also some ownership-based variables, such as ownership concentration and ratio of cash-flow to control rights. Our results indicate that ownership is an important factor in explaining differences in wage levels. Many large owners divert cash-flow into their own pockets which has a detrimental effect on wages and indicates that this behavior induced by owners is not sustainable.

Keywords

Spatial econometrics, ownership, wage differentials, sustainability

1. Introduction

"In theory, the ownership of a business in a capitalist economy is irrelevant. In practice, it is often controversial« (The Economist, 2010). Economists have long neglected the ownership of corporations in their empirical work, mostly due to the lack of precise data on ownership structure and the lack of an appropriate method to incorporate it in the empirical work. Although some attempts are found in the literature, most of them try to a priori group capital owners into specific groups such as state, domestic, and foreign ownership. If however we assume that these groups are not homogeneous at all, it is not surprising that no proper conclusion has been made. In this paper we try to overcome these problems by introducing a connectivity of firms on the basis of ownership. Ownership of each firm is traced to individuals where possible and tested whether firms with same owners perform similarly with regards to wages.

Differences in wages are results of different factors usually associated with economic and institutional environment. Wage gaps have been intensively studied by Buckley and Enderwick (1983), Blanchflower (1984), Globerman et al. (1994), Oulton (1998), Feliciano and Lipsey (1999), Girma et al. (2001), Gosh (2009). The main factor in these studies was labor productivity (Buckley and Enderwick, 1983). Due to technological factors, companies employing highly skilled and educated labor force would thus pay relatively higher wages compared to low tech firms, which are usually differences between foreign and domestic firms (Doms and Jensen, 1998). Better technology translates higher productivity into higher wages. This line of reasoning is in line with neoclassical theory, which argues that higher wages signal better firm performance (Winter-Ember and Zweimüller, 1999).

On the other hand, wage increases stimulate workers to produce more (i.e. raise labor productivity). While technology is difficult to measure, capital intensity according to Globerman et al. (1994) and Feliciano and Lipsey (1999) is another factor which contributes to explaining wage gaps between foreign and domestic firms, because lower wages might reduce employment. Globerman et al. (1994), after controlling for capital intensity and firm size, find that differences in wages associated with ownership disappear, which is additionally confirmed by Feliciano and Lipsey (1999) on the US manufacturing sector.

For the purposes of studying effects of ownership on corporate policies we introduce a capital connectivity matrix, which is based on direct and indirect ownership shares in Slovenian medium size and large corporations. With the use of spatial econometric tools we try to answer the question of relevance of ownership, by looking at the similarities between firms that are owned by the same individual. Our hypothesis is that different (individual) owners have different effects on wage levels in firms. We test this hypothesis via spatial error model and expect a positive spatial autocorrelation coefficient. This implies that differences in wages are not a sole result of differences in productivity, capital intensity, and size, but are additionally set by the owners of the firms.

The remainder of the paper is organized as follows. Section 2 provides an overview of the literature on ownership and wages. In Section 3 we introduce basic elements of spatial econometrics. Capital connectivity matrix, which uses information on individuals' direct and indirect ownership shares, is presented in Section 4. Section 5 contains results of spatial regression, with concluding remarks in Section 6.

2. Ownership and Wages

The main factor producing the wage gap is productivity, which is a consequence of higher skilled labor force, working in high-tech firms and, according to the existing literature, is not associated with

ownership but rather with factor intensity and firm size. On the other hand some authors have found that there is some linkage between ownership and corporate wage policy, since changes in ownership structure are accompanied with important consequences for corporate governance (Shleifer and Vishny, 1997). Effects of ownership concentration on firm performance have its roots in contributions from Berle and Means (1932). Although empirical studies have shown, that higher ownership concentration, measured as a share of largest blockholder, has a positive effect on performance (Cubbin and Leech, 1983), there was no theoretical background at the time for such findings. Demsetz (1983) argued that ownership structure is an endogenous result of competitive selection with a single goal of profit maximization expected by their owners; hence changes in ownership structure cannot affect firm performance. Accordingly, Demsetz and Lehn (1985) could not confirm any relationship between concentration and performance in US corporations.

Modern theory of corporate governance has evolved from earlier workings of Berle and Means (1932), with its pillars in dispersed ownership, which is well seen in the Theory of the Firm (Jensen and Meckling, 1976) and in contribution from Grossman and Hart (1980). Unique institutional environment (Roe, 1994; La Porta et al., 1997) that gave ground to the theory of a firm has its' origins from English speaking countries such as US and GB. This uniqueness of institutional environment provides a rather dispersed ownership structure, meaning that ownership concentration is low and portfolio investors play a large role. Such factors are rarely found in the rest of the world where investor protection is low, ownership concentration high, which in turn makes the identity of large owners (blockholders) an important factor.

At that time the empirical validity of dispersed ownership with strong managers and weak owners (Roe, 1994) view was being questioned by authors such as Eisenberg (1976), Demsetz (1983), Demsetz and Lehn (1985), Shleifer and Vishny (1986), Holderness and Sheehan (1988), Morck et al. (1988), La Porta et al. (1999), who have shown that even in US corporations there exists a moderate ownership concentration, while in the developing countries ownership is even more concentrated (La Porta et al., 1999). Shareholders in those countries have significant shares, which they use to actively influence corporate governance (Kang and Shivdasani, 1995). Active owners contradict Bearle-Means thesis as well as Roe's view of weak owners. La Porta et al. (1999) argue that identifying ultimate owners and associated voting rights is the only way to reveal the relationship between ownership and control. Controlling shareholders, who are often either state or a family, are present in most of the corporations where their control rights exceed cash-flow rights. A "better" ratio of cash-flow to control rights is most often achieved through pyramid structure based on the theory of pyramidal ownership and family business groups (Almeida and Wolfenzon, 2006), and with participation in management (La Porta et al., 1999). Better ratio of cash-flow to control rights, gained through pyramid structure, allows controlling shareholders to divert cash-flow to their own pockets (Almeida and Wolfenzon, 2006).

3. Brief Introduction to Spatial Econometrics

Shareholders, either large or small, are not randomly (and independently) distributed, since they can choose where to invest. Thus we can assume that firms are not independent units. According to Kmenta (1997) independence is the most unreasonable assumption in many cross-section studies. Maddala (2001), while studying households, further explains that residuals can be spatially correlated most likely due to omitted variable. Spatial correlation implies existence of similar value in the neighboring units. The first law of geography says that "everything is correlated with everything else, but close things are more correlated than things that are far away" (Tobler, 1970).

In Euclidian space neighborhood is defined with a distance measure:

$$\boldsymbol{d_{ij} = d(s_i, s_j) = \sqrt{(s_i - s_j)^T (s_i - s_j)}} \quad (1)$$

where d_{ij} is a distance between points s_i and s_j. Most used definitions of neighborhood are critical distance and n-nearest neighbours. Critical distance defines two points in space as neighbors if their distance is less than some cut-off distance $\tilde{d}$. According to this definition points s_i and s_j are said to be neighbors if $0 \leq d_{ij} < \tilde{d}$. Usally cut-off distance is defined as $min\left(max\left(d(s_i, s_j)\right)\right)$ in order that each point has at least one neighbour. Similarly, two points are said to be nearest neighbours if $d_{ij} = \min(d_{ik})\, \forall i, k$, where k is an arbitrary integer number referring to the number of nearest neighbors.

With distance (d) and neighborhood (N) properly defined, we can introduce a key concept of spatial econometrics, the spatial weights matrix (also known as a spatial connectivity matrix or W-matrix), which formally defines relationships between all points. Elements of a W-matrix are defined as:

$$\boldsymbol{w_{ij} = \begin{cases} \omega if j \in N(i) \\ 0 if j \notin N(i) \end{cases}, \; j \neq i} \quad (2)$$

After defining a W-matrix, it is a usual practice to standardize it in order to confine coefficients of spatial correlation to (-1,1) parameter space. A family of standardization techniques is defined as (Tiefelsdorf and Griffith, 2006):

$$\boldsymbol{V_{[q]} = \frac{n}{\sum_{i=1}^{n} d_i^{q+1}} D^q B} \quad (3)$$

where B is binary spatial weight (1 for neighbors and 0 otherwise), D^q matrix with spatial weights elements, d_i^q, n number of units, and q an element defining standardization. Some of the most common ways of standardization are (Patuelli et al., 2006):

i. q = 0. C-scheme or globally standardized spatial weights matrix is used when there are large differences in connectivity (different number of neighbours) between units and these need to be expressed. C-scheme also makes W-matrix symmetrical.
ii. q = -1. W-scheme or row standardized spatial weights matrix is most common and has an opposite effect to the C-scheme. It emphasizes points or areas with less connectivity at the edges of space.
iii. q = -0.5. S-scheme or variance stabilizing coding scheme (Tiefelsdorf et al., 1999) is right in between the first two, since it diminishes the differences with regards to connectivity.

With W-matrix defined and standardized, we can now introduce spatial models. Most spatial models come in variety of Cliff-Ord type models (Cliff and Ord, 1981). On one hand such models incorporate spatial lag of the dependant variable, while on the other a spatial autocorrelation of the residuals. Spatial lag model is defined as:

$$\boldsymbol{Y = \rho WY + X\beta + \varepsilon, \;\; \varepsilon \sim N(0, \sigma^2 I),} \quad (4)$$

while spatial error model is defined as:

$$\boldsymbol{Y = X\beta + \lambda Wu + \varepsilon, \;\; \varepsilon \sim N(0, \sigma^2 I).} \quad (5)$$

Combination of both spatial lag and spatial error produces the following SARAR model:

$$\boldsymbol{Y = \rho WY + X\beta + \lambda Wu + \varepsilon, \;\; \varepsilon \sim N(0, \sigma^2 I)} \quad (6)$$

SARAR stands for Spatial AutoRegressive (lag) AutoRegressive (error) model. If we only take first order neighbours then we can write it as a SARAR(1,1). Accordingly we can rename spatial lag model as SARAR(1,0) and spatial error model as SARAR (0,1). SARAR can be estimated with Feasible

Generalized Spatial two-stage least squares (FGS2SLS), a procedure developed by Kelejian in Prucha (1997; 2007; 2010), which is a combination of GM and IV estimation.

Although model (6) is well established in spatial econometrics literature, most regional scientist follow an approach, where they first estimate OLS regression and later try to determine whether the true data generating process is a spatial error, or a spatial lag model. Kalejian and Prucha (1998) believe that testing a joint hypothesis of no spatial spillovers originated from the endogenous variables or from the disturbances is superior, since model (6) allows for much richer spatial patterns. Even if corresponding spatial coefficients turn out not to be statistically different from zero, one could still estimate a reduced model (Piras, 2010)

4. Capital Connectivity Matrix

With basic elements of spatial econometrics defined, we canproceedwith the capital connectivity matrix. Before using real data, it is best to present a simplified version of the ownership structure data. In Table 1 there are 4 firms and 3 owners, each firm with 2 owners (O_A and O_B) and their share of stock C. Since we do not deal with geographical space but a space where relationships between points are defined with ownership of capital, we named it "*capital space*".

Table 1: Example of the ownership data

Firm	O_A	O_B	C_A	C_B
1	1	2	C_1	$1-C_1$
2	2	3	C_2	$1-C_2$
3	3	1	C_3	$1-C_3$
4	2	1	C_4	$1-C_4$

Source: Ogorevc and Šlander Wostner, 2011

In capital space a pair of firms are said to be neighbours if they have a common owner or in other words, if they are placed in the owner's neighbourhood *N(i)*. Elements of the matrix are defined as:

$$\boldsymbol{w_{ij}} = \begin{cases} \boldsymbol{\omega = C_{k,i} * C_{k,j} if j \in N(i)} \\ \boldsymbol{0 if j \notin N(i)} \end{cases}, \ \boldsymbol{j \neq i}. \tag{7}$$

Where $C_{k,i}$ denotes share of owner *k* in firm *i* and $C_{k,j}$ denotes share of owner *k* in firm *j*. According to the Table 1 we can see that firm *F1* has 4 relationships: two originating from owner *O1* and two from owner *O2*. Since firms *F1*and *F4* have the same owners (O1 and O2) we summed weights of the pair *F(1,4)* which lead to the following specification of the matrix.

Table 2: Example of non-standardized capital W-matrix

F	1	2	3	4
1	0	ω_3	ω_1	$\omega_2 + \omega_4$
2	ω_3	0	ω_7	ω_6
3	ω_1	ω_7	0	ω_{10}
4	$\omega_2 + \omega_4$	ω_6	ω_{10}	0

Source: Ogorevc and Šlander Wostner, 2011

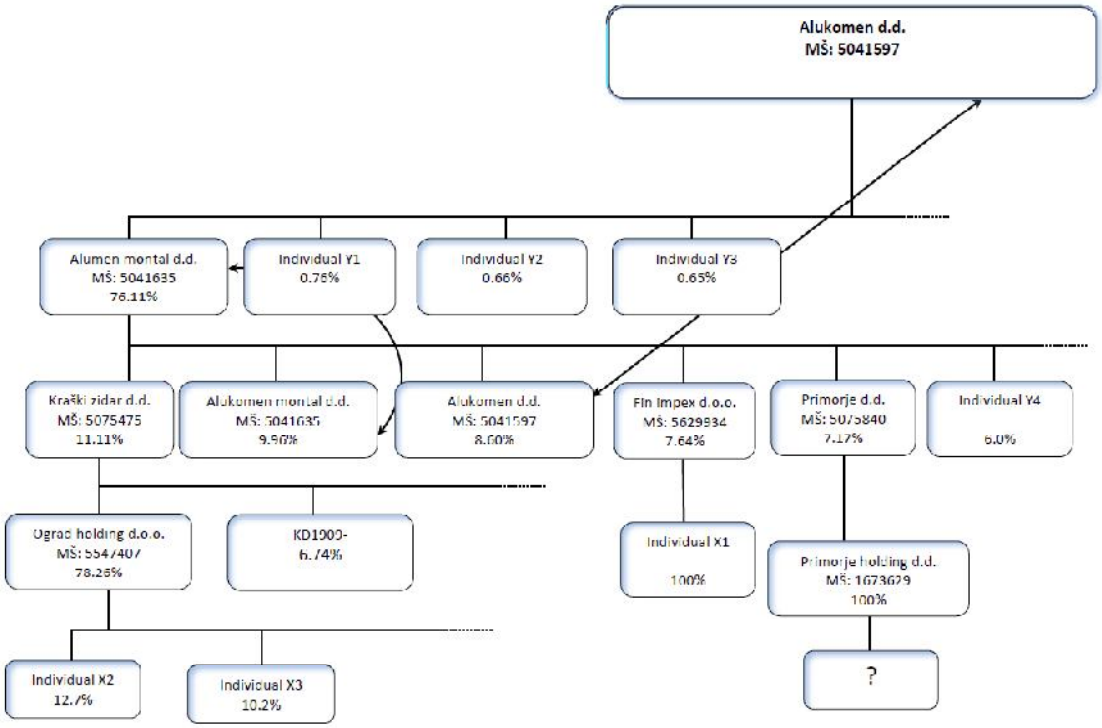
Using real data on ownership presents a difficult task, since we first need to calculate direct and indirect ownership shares for each individual owner. It is not uncommon to find the use cross-shareholdings, pyramid structures and other techniques to achieve a better ratio of cash-flow to control rights and also to hide real ownership information. One such example is shown in Figure 1, which reveals the ownership structure of joint stock company Alukomen d.d. On the first level of ownership structure (direct ownership) we can see that there is a majority stockholder Alumen montal d.d. with 76.11% of shares. Second largest owner with less than 1% is an individual and same goes for the third and so forth. We can say that Alukomen d.d. is controlled by Alukomen Montal d.d. On the second level we can see that the largest shareholder (blockholder) of Alukomen d.d. is Kraški zidar d.d. with 11.11%, followed by the company itself with nearly 10% and also a cross-shareholding by Alukomen d.d with 8.6% ownership. Other shareholders are Fin Impex d.o.o., owned by individual *X1* with 7.64% and Primorje d.d., owned by Primorje holding d.d., for which ownership structure information was not available.

In order to calculate direct and indirect ownership shares we used two databases. First one contained ownership information of Slovenian joint stock companies. Ownership data for joint stock companies was provided by the Central Securities Clearing Corporation (KDD) for the top 50 holders at the end of the march 2009. For limited liability companies we used Business register of Slovenia (PRS) provided by AJPES. Although PRS contained ownership information for a longer time period, we matched it to coincide with a date of KDD top 50 data.

Procedure for calculating direct and indirect ownership shares was a four-step routine with iteration of the final step, while at each step limiting the number of owners to 50 in order to reduce computation time:

i. First step was used to obtain direct ownership shares of companies; which is the case for first level (direct) ownership in Figure 1.
ii. In the second step all owners that are limited liability companies were replaced by their owners in order to obtain individuals, joint stock companies or foreign firms for which we did not have data on ownership structure. Looking again at Figure 1, Fin Impex d.o.o. was replaced by individual X1 and Ograd holding d.o.o was replaced by individual X2, X3 and so on.
iii. The third step was similar to the second but this time all the direct owners of joint stock companies were replaced by their owners.
iv. The goal of the final step was to account for cross-shareholdings and for companies holding their own stock. Again, looking at Figure 1, since Alumen montal d.d. has its own shares, they were replaced by the owners of Alumen montal d.d. This was done iteratively for as long as the Alumen montal d.d. remained its own shareholder above 0.00001%. At the third step of the procedure Alumen montal d.d. had 9.96% of its own shares. Starting the forth step, it share was diminishing from 0.0099% then 0.000098%, 0.000000009%, at which time the iteration procedure would stop and changing that number of ownership share to 0.

Figure 1: Ownership structure of Alukomen d.d.



Source: KDD, 2010; AJPES PRS, 2011; own calculation

In the case of illustrative example from Figure 1, combined direct and indirect ownership shares reveal the following top five owners (in Table 3). Based on this information we computed ratio of cash-flow to control rights by comparing the control rights of direct owners to cash-flow rights of largest indirect owners. Computation of the ownership concentration measure (C4) was done by summing the top four owners' shares. Again, due to data limitation both measures are imprecise since we did not have all the necessary information on ownership for some corporations. Many of these corporations, which are large shareholders, were treated as a single individual (e.g. Primorje holding d.d.).

Table 3: Top 5 owners of Alukomen d.d.

Individual X1	Primorje holding d.d.	Individual Y4	Individual X2	Individual X3
6.78%	5.46%	5.36%	4.90%	3.93%

Source: KDD, 2010; AJPES PRS, 2011; own calculation

Combination of direct and indirect ownership shares were then used to produce a capital W-matrix. By using data from Table 1 we have shown, that elements were computed using a product of ownership shares while accounting for the ownership information with summation of ownership shares in a given firm. For an easier overview of the ownership structure of Slovenian medium size and large companies we present assets and labor cost multiplied by direct and indirect ownership shares for the first 10 largest owners in the sample, sorted by labor costs. It can be seen from Table 4 that Slovenian state, with a portfolio of 280 investments controls more than one third of all the assets in the economy's medium size and large companies, while its share in labor costs is about a fifth. Due to sample restrictions or owners uniqueness these shares tend to be inflated in the sample and producing values for assets and labor 42% and 31% respectively. It should be mentioned here that municipality ownership is not included in the ownership by the Republic of Slovenia, although it is a part of the state ownership. The largest of the municipalities is Ljubljana with 1% both in assets and labor costs, while all municipalities combined control about 2% of assets and 3.5% of labor costs

with 466 investments. Second largest owner measured by assets is a Slovene entrepreneur who controlled 2.3% of assets and 1% of labor costs. Ownership information for the rest of the top 10 list could not be traced to individuals due to database limitation.

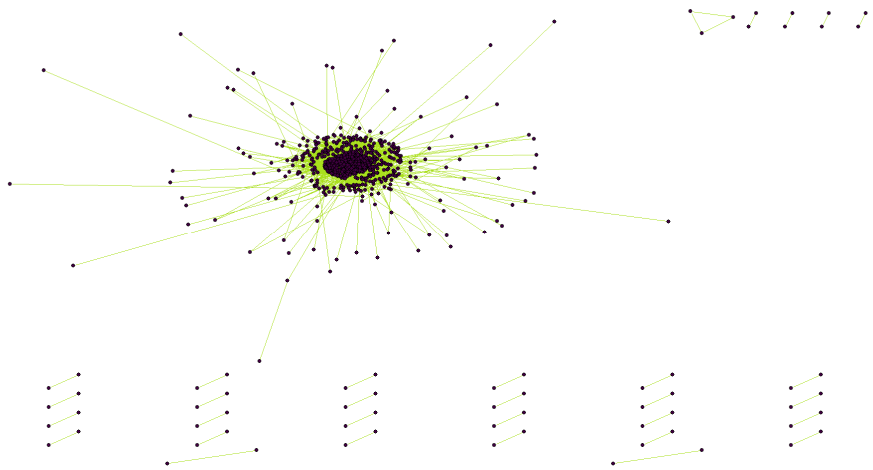
Table 4: Top 10 owners by labor costs in the sample

		economy		sample	
Name	N	Assets	Labor costs	Assets	Labor costs
R. Slovenia	280	33.84%	21.39%	41.85%	30.65%
Ag Novartis pharma	4	1.70%	2.24%	2.12%	3.22%
M. Ljubljana	14	0.97%	0.99%	1.21%	1.43%
Center naložbe, d.d.	27	1.30%	0.92%	1.62%	1.31%
Entrepreneur	9	2.30%	0.99%	2.70%	1.24%
Primorje holding d.d.	33	0.84%	0.88%	0.91%	1.14%
Dilon coöperatief u.a.	9	0.66%	0.66%	0.82%	0.95%
Hidria, d.d.	12	0.49%	0.53%	0.61%	0.77%
Siemens aktiengesellschaft	82	0.45%	0.52%	0.56%	0.75%
Infond holding, d.d.	18	0.64%	0.46%	0.80%	0.66%

Source: KDD, 2010; AJPES PRS, 2011; own calculation

Another way of looking at ownership information is by drawing it on a two dimensional space. Figure 1 was drawn using software Pajek / Kamada-Kawai separate components technique (Kamada and Kawai, 1989), where distances between points represent (inverse) capital spatial weights. Points represent firms and lines connecting points represent ownership ties; the same individual owner in both (connected) firms. Similar to the Table 4, we can observe a concentrated ownership in the middle of Figure 2 as a result of a state ownership. Points that are further out are indirectly less connected to the state's portfolio than the ones in the inner circle, while the separate components present firms with no ownership ties with the state. The main insight of the Figure 2 is the finding that the Slovenian government has potential control of the economy, since only 63 firms in the sample are independent of the highly connected centre.

Figure 2: Graphical representation of capital W-matrix



Source: KDD, 2010; AJPES PRS, 2011; own calculation
Note: Points represent firms. Lines represent inverse capital weights

Standardization of the capital W-matrix was a combination of row standardization (W) and variance stabilizing scheme (S). W-coding was first used in order to confine spatial correlation coefficients to (-1,1) parameter space. Using only this coding is problematic in the case of capital W-matrix since a pair of firms are said to be neighbors if they have a common owner. A problem of row standardization can be shown in the following example. Imagine we have only two pairs of neighboring firms, each pair connected through a different owner and all other owners of the four firms are unique. Then suppose that owner of the first pair has a 100% share in both firms, while the owner of the second pair has only 5% share in one firm and 10% share in the other. Without any standardization the weights of the first pair would be 1 and only 0.005 for the second. Row-standardization in this case would lead to weight equality, which is not correct because it implies that only a non-unique owner can influence firms' governance. For that reason we applied a correction factor, which is equal to the sum of non-unique owners' shares in a given firm. Also, the correction factor was different in the (5%, 10%) pair, which made connectivity matrix asymmetric. Because of the use of the correction factor, parameter space was no longer confined to (-1,1) and for that reason amongst the others we used S-coding scheme in the second step. But why didn't we use only S-coding? The answer to that lies in the varying size of portfolio of the owners. If we take two extremes; one owner has shares in 280 firms, while the other only in 2 and for ease of interpretation we assume that the two owners have each 100% in all of their firms. Then the weights for the larger owner would be much higher than those of the smaller one. Using a combination of corrected row-standardized S-coding scheme thus confines spatial correlation parameters to (-1,1) while accounting for the information lost due to unique owners.

5. Empirical Evidence

The core of this study is to provide some empirical evidence on whether owners affect corporate policies in a detectable manner, in this case the corporate wage policy (or wage setting) using a capital W-matrix and a simple statistical model with labor cost per worker as a dependant variable and a set of independent variables most commonly found in the literature. We present these variables in Table 5.

Table 5: Definition of firm level variables

Variable	Code	Definition	AJPES CODE
Labor cost per worker	Lcost	Total labor costs per month divided by average number of workers	$\frac{\text{AOP140}}{\text{AOP188} * \text{AOP189}} * 100$
Labor productivity	Lprod	(Net sales minus costs of materials and services per month) divided by average number of workers	$\frac{\text{AOP110} - \text{AOP128}}{\text{AOP188} * \text{AOP189}} * 100$
Capital intensity	Kint	Capital stock divided by average number of workers	$\frac{\text{AOP58}}{\text{AOP188}} * 100$
Employment	Empl	Number of workers	$\frac{\text{AOP188}}{100}$
Profit margin	PM	Gross revenue divided by operating expenses	$\frac{\text{AOP126}}{\text{AOP127}}$
Ownership concentration	C4	Sum of top 4 owners	
Cash-flow to control rights ratio	cf.cr	Largest direct owner's share divided by largest indirect owner's share	
Regional average labor costs	WREG	Average labor costs in a NUTS-3 region	
Sector average labor costs	WSKD	Average NACE level 3 labor costs	

Source: AJPES, 2011; own calculation

To illustrate the potential impact of independent variables on labor costs, we present average values of individual variables by groups of owners (foreign, domestic, and state ownership). A company was

assigned to a specific group, if a single group of owners held at least 50 percent equity share. Sample included all medium size and large companies in Slovenia (more than 50 employees), excluding financial sector and those with unique owners (capital owners with only 1 investment in Slovenian medium size and large firms).

Table 6: Decriptive statistics

	Average	Foreign ownership	Domestic ownership	State ownership
Labor cost per worker	1440.00	1588.43	1317.66	1756.72
Labor productivity	2997.0	3518.9	2469.6	4561.1
Employment	244.8	226.52	178.61	425.93
Capital intensity	4.70	3.60	3.69	10.92
Profit margin	1.01	1.00	1.01	1.03
Ownership concentration	0.78	0.96	0.81	0.92
Cash-flow to control rights ratio	1.82	1.18	1.92	1.09
Regional average labor costs	1210.00	1224.27	1211.89	1206.91
Sector average labor costs	1245.00	1308.83	1186.24	1456.48

Source: KDD, 2010; AJPES PRS, 2011; AJPES, 2010; own calculation

Average monthly labor cost per employee amounted to €1440. Moreover, the differences are evident between groups of owners. The highest average monthly labor costs are in state enterprises, which amount to €1757 and are 22% above average. Foreign companies exhibited average monthly labor costs of €1588, which is 10% higher than average. On the other hand, domestic private enterprises showed 8% below average labor costs, which amounted to €1318. The differences observed between labor costs by groups of owners can be explained by differences in productivity. The highest labor productivity is found in the state ownership group with €4,561 per employee. State owned companies are found to be larger and more capital intensive. Average number of employees in state enterprises (in the sample) is 426, which is 73% higher than the average value of the whole sample. Both domestic and foreign companies have below average number of employees and have similar capital intensity. Minor differences are also observed in profit margin, defined as ratio of revenue and operating expenses, but close to 1 in all cases.

In the group of variables that reflect information about ownership (C4, cf.cr), domestic private owners have on average lower ownership concentration and higher ratio of cash-flow to control rights. Surprisingly, ratio is found to be low in the case of foreign owned enterprises. Given the prediction made by the theory of pyramidal ownership, ratio should be similar, as it applies to the same institutional environment. The last two variables reflect mainly the choice of groups of owners on where to invest. Foreign owners invest mainly in the NUTS-3 regions and industries where average labor costs are higher, while the opposite is true for domestic private owners.

Before starting with the estimation of spatial parameters, which are of prime interest to this study, we estimated the following OLS model and later tested for presence of spatial correlation using diagnostic test in form of Lagrange multiplier test.

Estimated model was in the following form:

$$\boldsymbol{ln(Lcost) = \beta_0 + \beta_1\, ln(Empl) + \beta_2\, ln(Lprod) + \beta_3\, ln(Kint) + \beta_4\, ln(PM) + \beta_5\, ln(cf.cr) + \beta_6\, ln(C4) + \beta_7\, ln(WREG) + \beta_7\, ln(WSKD) + \varepsilon,\ \varepsilon \sim N(0, \sigma^2)} \quad (8)$$

Table 7: Results of OLS model

	Estimate	Std. Error
Intercept	-3.909**	1.266
Employment	-0.027**	0.008
Labor productivity	0.277***	0.013
Capital intensity	0.016***	0.004
Profit margin	-0.292***	0.051
Cash-flow to control rights ratio	-0.031*	0.014
Ownership concentration	-0.085***	0.023
Regional average labor costs	0.813***	0.178
Sector average labor costs	0.457***	0.040
n	798	
S_e	0.204	
R^2	0.605	
Adjusted R^2	0.601	
F-statistic (p-value)	150.9 (0.000)	

Note: *** stat. sign. at the 0.1% level; **stat. sign. at the 1% level; *stat. sign. at. the 5% level
Source: KDD, 2010; AJPES PRS, 2011; own calculation

Labor costs are positively correlated with the average regional and sector labor costs. Similar result is shown for the labor productivity and capital intensity. Increase in labor productivity by 1% raises labor costs on average by 0.28%, ceteris paribus. On the other hand, contrary to the expectation employment has a small, yet negative effect. Although large firms on average pay higher wages than small firms for workers with equivalent measured characteristics, firm size wage effect contradicts the idea that competition should force similar individuals to receive similar pay (Hollister, 2004). The positive relationship between firm size and wages has been found across industries, sectors, and countries (Bayard and Troske, 1999; Brown and Medoff, 1989). On the other hand, Hollister (2004) found a significant decline of firm size wage effect between 1998 and 2003, which is a reversal of earlier trends. Šlander (2007) found that the firm size wage effect in Slovenian economy is non-linear, inverse U-shaped, where the negative effect starts at around 100 workers. Similar findings can be observed in Magda et al. (2008); average wages in some countries (Italy, Netherlands, Norway, and Portugal) tend to be lower in large enterprises compared to medium size enterprises for workers with equivalent measured characteristics. Šlander (2007) explains this empirical finding with an observation that the privatisation of larger, mostly state-owned firms has brought about their restructuring and downsizing along with an increase in their productivity and average wages. In the light of above mentioned empirical literature, “negative” firm size wage effect no longer contradicts previous empirical findings. Sample included only medium size and large firms, and so this does not indicate that large firms pay higher wages than small firms.

Surprisingly, profits are also found to have a negative effect on wage levels. “If shareholders have gained power, they must have done so at the expense of someone else” (Stockhammer, 2005-6, pp.194). So the question that arises is whether higher profits are made at the expense of underpaid labor. If owners are highly indebted due to takeovers, reducing the average labor costs and thus increasing the profitability might explain the negative relationship. Since we do not have enough data to answer this question, profit-wage relationship remains unsolved. However, other variables related to ownership seem to indicate just that. Higher ownership concentration reveals a negative correlation to average labor costs. Increase of ownership concentration by 1% reduces average labor costs by 0.085%, which is not in accordance to the Cubbin and Leech (1983), who found a positive relationship between concentration and firm performance. Apparently pyramid structures make it

easier to divert cash-flow from companies to owner's pockets so it leaves less for the wages. Decreasing the ratio of cash-flow to control rights by 1% is accompanied by the increase of average labor costs by 0.031% on average, ceteris paribus. In light of these two findings of negative effect of both ownership related variables to wages, profit-wage relationship as found in Slovenian sample no longer appears contradictory. Another possible explanation to the negative relationship between profits and labor costs could be endogeneity of the profit margin, since labor costs are part of the denominator. We also estimated a model with the profit margin cleared from labor costs, but the results were similar (negative and statistically significant coefficient at the 0.1% level). Moreover, exclusion of the profit margin from the analysis did not reflect in changes to any other coefficients.

Testing for spatial correlation (Table 8) reveals that both residuals of OLS model and spatial lag of dependent variable are spatially correlated, meaning that we might expect similar values of both the dependent variable and disturbances in firms belonging to the same individual(s). This is a first indication in this study that ownership of a business does matter with regards to wages. Lagrange multiplier tests show that both lag of dependent variable as well as errors of OLS are spatially correlated, which signals that the data generating process takes a form of spatial error model.

Table 8: LM tests

	LM test
SARAR(0,1)	20.402***
SARAR(1,0)	5.543*
SARAR(1,1)	26.164***

Note: *** stat. sign. at the 0.1% level; **stat. sign. at the 1% level; *stat. sign. at. the 5% level
Source: KDD, 2010; AJPES PRS, 2011; own calculation

In the case of spatial lag model, OLS estimates will be biased and inconsistent due to the simultaneity bias. On the other hand, if the true data generating process is spatial error model, in which the off-diagonal elements of the covariance matrix determine the structure of spatial dependence, OLS will remain unbiased, yet inefficient, since estimators for standard errors will be biased in small samples. In Table 9 we present the results of SARAR models using spatial autocorrelation and heteroscedastic consistent estimator (FGS2SLS-HAC). Results were obtained using R software and the SPHET library (Piras, 2010).

Table 9: Results of spatial models

	SARAR(1,0)		SARAR(0,1)		SARAR(1,1)	
	Estimate	HAC St.Er.	Estimate	HAC St.Er.	Estimate	HAC St.Er.
Intercept	-3.980**	1.387	-4.150**	1.467	-4.065**	1.459
Employment	-0.032**	0.011	-0.032**	0.010	-0.031**	0.010
Labor productivity	0.252***	0.026	0.275***	0.029	0.246***	0.029
Capital intensity	0.013*	0.005	0.012*	0.005	0.012*	0.005
Profit margin	-0.289***	0.087	-0.289***	0.075	-0.289***	0.075
Cash-flow/control	-0.032***	0.009	-0.032*	0.014	-0.032*	0.014
Own. concentration	-0.073**	0.008	-0.072*	0.024	-0.074**	0.026
Regional labor c.	0.834***	0.185	0.858***	0.204	0.847***	0.202
Sector labor c.	0.460***	0.046	0.461***	0.051	0.459***	0.051
Lambda	0.003**	0.001	-	-	0.001	0.001
Rho	-	-	0.387***	0.085	0.401***	0.092
n	798		798		798	
S_e	0.203		0.160		0.157	
R^2	0.603		0.752		0.762	
Adjusted R^2	0.595		0.743		0.752	

Note: *** stat. sign. at the 0.1% level; **stat. sign. at the 1% level; *stat. sign. at the 5% level
Source: KDD, 2010; AJPES PRS, 2011; own calculation

Although LM tests indicate that spatial error model is a proper specification of the given model, we nonetheless estimated the SARAR (1,1) model in order to confirm our previous findings. Looking only at the spatial parameters in the SARAR (1,1) model we can see that spatial lag is not statistically different from zero. For that reason we excluded it and estimated a spatial error model. Comparing results of the OLS model to the spatial error model does not reveal any significant changes to the estimates, although adjusted R^2 shows a better fit of the spatial error model compared to the OLS model. Adjusted R^2 in the case of OLS is 0.60 compared to 0.74 in the spatial error model. This is in line with our expectations, since we explicitly try to find ownership based effects in the disturbances. Coefficient of spatial autocorrelation of the disturbances, with value of 0.387, reveals positive moderate ownership effects on labor costs. Disturbances are not independently and identically distributed but exhibit similar values around each individual owner; values of disturbances are dependent on the position in the capital space. Since capital connectivity matrix was designed using individual ownership shares, this confirms that the identity of owners do matter, at least in the case of corporate wage policy in Slovenia. Hence, shareholders increasingly influence the behavior of nonfinancial firms. Negative effects of all ownership based variables (including profits) on average labor costs, which is accompanied by a positive coefficient of spatial correlation is a clear indication that corporate behavior in the name of creating shareholder value at the expense of labor is a wide-spread phenomenon in the Slovenian economy . While some economists appraise it as an increase in efficiency, some believe in negative effects it has on employment and growth (Stockhammer, 2005-6). It has become apparent that shareholders have gained power at the expense of labor, which has been the main source of fear from labor unions. Reducing wages has a negative effect on labor productivity, which in turn has a detrimental effect on growth. Clearly this kind of action from the owners is not sustainable for the workers and the economy as a whole as we witness the on-going financial crisis and recession.

6. Concluding Remarks

This paper introduces the capital space and a capital connectivity matrix to the field of corporate governance. Although owners are usually seen as solely seeking highest returns on their investments, maximizing profits, it was therefore concluded that ownership is not an important factor. In this paper we provided empirical evidence that there is a non-negligible effect of ownership on corporate wage policy. We believe that past difficulties in providing such empirical evidence lies in the unavailability of detailed ownership structure data and a lack of appropriate methods. In this paper we used ownership data on individual level and spatial econometric techniques to show that ownership does matter in the case of corporate wage setting. It has been found that both ownership concentration and excess of cash-flow rights with regards to control rights have a detrimental effect on wages. Not only that, it has been found that identity of owners is also an important factor as firms with same owners similarly affect average labor costs even after controlling for standard factors such as labor productivity, employment, capital intensity and profitability. A surprising finding was a relationship between wages and profitability. Results indicate that firms with higher profits (ceteris paribus) pay lower wages. We argue that this effect could be explained by owners increasing influence on the behavior of nonfinancial firms. Highly indebted owners, seeking higher returns on their investment by reducing labor costs.

One limitation needs to be acknowledged and addressed regarding the present study. Using a cross-sectional data does not enable us to distinguish between the true effects of the owners from their selection. It is possible that individuals invest in firms that reflect some similarities in wage levels; hence spatial error might reflect their investment decision patterns and not their effects on corporate policies, which is what the further research will reveal. Also, a finding that a presence of a specific individual owner in a group of firms shows resemblance in their wage levels gives ground to studying effects of ownership on other corporate policies.

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Risk Management of Exchange Rate and Sensitivity in Foreign Trade Companies: A Case of Konya

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Abstract

It is a matter of subject that foreign trade companies face with commercial risks as a result of exchange rate fluctuations due to their transactions with both types of domestic currency and foreign currency. These companies are in a struggle for risk management with various financial supports against the risk of exchange rate.

This study presents the sensitiveness of enterprises on the subject of risk management and protection, these enterprises are engaged in foreign trade in Konya city, and so they face with the risk of exchange rate. Within the scope of this study, a questionnaire was made for enterprises operating in different sectors.

According to the survey results, the evaluation was conducted, and it was understood that enterprises did not use the financial techniques regarding the management of exchange rate, and that they could face the risks.

Keywords

Exchange rate risk, foreign trade, transaction risk, hedging strategies, derivatives

Introduction

The enterprises involved in international trade face with various risks such as different market conditions, customer relations, currency circulations since they appear in markets different from each other. The enterprises need to manage these risks well to obtain market opportunities for their commerce.

Risk is the possibility that an economic benefit reduces, which results in any expense or loss or economic damage regarding any transaction (Yüzbaşioğlu, 2003). In accordance with this definition, the risks the enterprises face in international trade transactions are *Risks Regarding Goods, Buyer Risk-Commercial Risk, Political Risks, Exchange Risk*.

Exchange risks are possible positive and negative changes in the value of the domestic currency against the foreign currencies due to certain factors (political events, payment balance deficit, etc.). An exchange risk is seen by leading to profit or loss on balance sheets or investment portfolios of the enterprises due to the changes in exchange rates.

In this study, the management of the risk and the measures to be taken are mentioned while giving information about the occurrence of exchange risk and its effects. Within this scope, it has been researched how foreign trade enterprises are sensitive to the exchange rate risk and which instruments they use in the management of the risk, and a questionnaire has been done on the firms and analysed.

1. Exchange Rate Risk

An exchange rate means the conversion rate for the currencies of two countries. The rates occur in accordance with the real income levels of the countries and the differences in transnational price and interest rates. The rate risk is a loss situation of an enterprise, because there are no foreign currencies of the same quantity and type in assets and liabilities of the balance sheet for any enterprise.

If an enterprise's assets are more than its liabilities on the type of foreign currency, an appreciation of domestic currency against foreign currencies causes harm. On the contrary, if the liabilities of an enterprise are more than its assets (that is, if any deficit position) on the type of foreign currency, an appreciation of domestic currency against foreign currencies increases profit because of decreases in debts of an enterprise on the type of foreign currency (İşleyen, 2011).

When an exchange rate, the value of one country's currency in terms of another currency is determined more than its value, purchasing the foreign currency will reduce in that country, so it will be difficult to sell goods for those countries and export will decrease, maybe export will be never done, contrary to this, import will be cheap. This situation is called over-valuation of the domestic currency against foreign currencies. To keep away from the negative items brought by over-valuation, the exchange rate must be reduced. The exchange rate policy which is used for reducing the exchange rate of currency suddenly and knowingly by the governments, is called devaluation. But as a result of the inflation in the domestic market, the domestic currency with low purchase power and low value and the foreign currency with high purchase power are not based on the will, so these are not regarded as devaluation (Oksay, 2001).

1.1. Reasons of exchange rate risk

It is difficult to give an absolute factor about the reasons of exchange rate risk, furthermore, we can classify all types of factors affecting exchange rates as the reasons of exchange rate risk. These factors sometimes affect exchange rates independently, they also affect them as a series of reasons dependent on each other in some situations. The main reasons affecting exchange rate movements are as follows: fluctuation, political risk, preferred rate regime, current account deficit-surplus, inflation-interest rates, effect of financial crisis and speculative movements.

1.2. Types of exchange rate

In the literature, under the conditions of floating exchange rate regime, three types of exchange rates are mentioned including economic risk, translation risk and transaction risk (Popov ve Stutzmann, 2003).

1.2.1. Transaction risk

A transaction risk can be defined as the probability of profit and loss resulting from the effects of exchange rate fluctuations on the expected cash flows (Redhead, 1988). Also, it focuses on the cash flows requiring that different currency units are exchanged with each other and results from the time difference between the enterprises' foreign exchange-based cash flow (payment) commitment and revenue (payment) realization (Kula, 2002).

These risks are ones which are mostly experienced by the exporters. The transaction risk has impacts on the exporters about (a) with which foreign exchanges sale invoices will be done; (b) whichever of them will have depreciation in its value with respect to making transaction with the domestic currency or the foreign currency until the time for payment; (c) the period for sale transaction (Redhead, 1988).

The rate risk is directly related with the product pricing. The pricing has an effect upon the competitive positions and economic futures of the firms. The profit margins, which are determined by the prices to the costs in the country, are perceived as different ones in other countries.

1.2.2. Economic risk

An economic risk means the effects of unexpected exchange rate fluctuations on the cash flow and the firm value. In particular, it includes forward-looking expectations, that's why, guiding the activities and guessing the risks are important factors. For this reason, the management of economic risk is more difficult and more significant for the enterprise managers (Seyidoğlu, 1997). *As a result* of a change *in exchange rates, the effect on the economic value of the enterprise is an* economic risk. This means that the difference between the assets and liabilities of the enterprise affects the current value with the change of exchange rate (Demirağ, 1994).

In an economic risk, it is important to predict both cash flows resulting from the activity and finance of the enterprises and the behaviors of the competitors in relation to the changes in an exchange rate. For this reason, an economic risk is more comprehensive than accounting and transaction risks. In short, the estimation of two factors has importance for the future of the firm due to the economic risk (Kanas, 1996).

1) The estimation of foreign exchange positions for the firm in future, that is, the determination of whether the firm will have short or long foreign exchange position is important. Because these positions carry risks. 2) The estimation of the behaviors for the competitors in relation to the rate changes in the firm is important for following the competitors' behaviors against the rate risks, determining the strategies related with the company's own marketing, production and financing against the economic risks and applying these strategies.

The economic risk is also called the enterprise risk, the competitive risk or the strategic risk (International Chamber of Commerce, 1982).

1.2.3. Accounting (transformation, translation) risk

An accounting (Transformation, Translation) risk *is one which comes from the necessity for keeping assets and liabilities with different exchange rates and occurs when exchange rates are translated into each other.* A Balance Sheet and Income Table are showed by a currency unit even if transactions are made with different foreign currencies. At this point, the difference in exchange rates causes the differences arising from translation during the collectin of transactions. When the profits obtained with different exchange rates are translated into the currency unit in which the accounts are kept, increases or decreases occur. The enterprise is obliged to show the current profits with average numbers in cost and profit calculation (Buckley, 1996).

Since multinational enterprises carry out transaction with foreign exchange in both their sales and their purchases, even their credits comprise of foreign exchange, they face with the accounting risk. These enterprises register profit and loss statements as rate loss and rate profit at the end of periods and in times of valuation due to the changes in rates.

2. Management of Exchange Rate Risk

The future prediction is the biggest risk which enterprises face while making investment decisions or going on commercial activities. The foreign trade enterprises must follow speculations and fluctuations on exchange rates carefully. The enterprises' forward-looking predictions, analyses and some negative items contrary to their own positions may give big financial damages to the firms. In this way, an active risk management must be provided for preventing the damages or minimizing them on exchange rates.

2.1. Alternative methods in management of exchange rate risk

Various methods are used in the management of exchange rate risk. Due to the aim of risk management for preventing or minimizing the risk, firstly *Hedging* technique, which means protection from risk, must be known.

Hedging is a stock exchange technique in which ones engaged in foreign exchange transactions apply for being protected from the foreign exchange risk. Today the rates always change in spot exchange markets. As a result of this, the enterprises to pay with foreign currency in future may incur losses because of the rate change. Except for ones dealing with foreign exchange speculations, each one wants to make transaction over the exchange rate on the date for payment. As soon as possible, they want to protect themselves from the movements in the foreign exchange rates. In order to

compensate the damage arising from the risk in Hedging technique, any aggrement must be made about the purchase and sale of foreign Exchange on the rate in the future (Karluk, 2002).

Like Hedging technique, the markets where transactions are made to be protected from price and exchange rate risks in future, are named futures markets or derivatives markets. These markets include all types of derivatives such as forward, futures, options ve swap.

2.1.1. Derivatives

Generally, the financial techniques which are dealt in markets called derivatives markets or futures markets, are named derivatives. These derivatives are traded through organized exchanges or unorganized exchanges.

Among the derivatives operate in organized exchanges and over-the-counter markets, there are some differences such as the standard contracts, the existence of clearing house for undertaking the credit risk of the opposing party in the contract, the regulatory framework and types of trading products (Gonzáles, 1994).

The financial derivatives markets are the biggest and fastest growing markets of the world (Dodd, 2004). The most effective way for managing financial risks including the risks such as changes in exchange rates, interest rates and stock prices is to use derivatives (Sobol, 2008).

2.1.1.1. Forward

The term forward means to throw something forward, to send something forward in a lexical meaning. The equivalent of this expression in foreign trade is described as *a foreign trade contract which provides that different exchanges and currency units are changed over the rates and parties determined as of today at future time, and these are bought and sold* (İşleyen, 2011).

Forward is a contract which regulates the purchase and sale of a currency unit over the pre-determined date and rate to another currency unit. The most important advantage is that the contract term and volume are determined by the requirements. In this term, the parties must fulfill the liabilities regarding the pre-determined rate and volume (İşleyen, 2011).

In forward markets also called over-the-counter markets, the contracts are made in accordance with the conditions determined by the parties rather than the standard contracts. In forward contracts based on confidence and having no guarantee system, the conditions of the contract are satisfied by giving credit or debt entry in the relevant bank accounts without delivering physical goods during the payment.

As mentioned above, even if the exchange forward contract is defined, there are interest forward and commercial goods forward in forward transactions. Under these transactions, the basic aim is to fulfill the liabilities regarding the purchase and the sale agreed upon today at a future date. The differences are *rate* and *parity* determined as of today in exchange, *rate* in interest, *price* in commercial goods.

2.1.1.2. Futures

Futures contracts are similar to forward contracts in terms of definition and aim. Futures contracts require fulfilling a liability determined as of today at a determined date in future. Futures contracts based on exchange are ones which a certain exchange is expressed in with a certain date and a standard quantity in details and operate in organised exchanges (Papaioannou, 2006).

Moreover, futures contracts sometimes differ from forward contracts. It can be said that futures contracts operate in organised exchanges having a clearing house in general and these are standardized contracts in terms of contract subject, unit value, settlement date, settlement term and conditions. Futures contracts are arranged on stocks, stock indexes and interest rates as well as exchange rates (Vashishtha ve Kumar, 2010). Since futures contracts operate in organised exchanges, they also have secondary markets, and this allows futures contracts pass into other hands before due date (Ceylan, 2004).

The clearing houses or in other words, the clearing centers are structures which depend on the relevant stock exchange in an organizational way and guarantee the rights of ones making transactions in futures markets (Kaya, 2011). The clearing houses ensure responsibilities. The margins used by stock brocker in secured transactions are as follows: initial margin, continuity margin and variation margin.

2.1.1.3. Swap

Swap means to trade and to exchange one thing for another. Swap transactions are based on a forward contract at least, these are mutual changes in which financial flows are in favour of both parties between the buyers and the sellers at pre-determined time (Kaya, 2011).

Swap contracts can be defined as contracts in which the parties exchange their own liabilities given the underlying contracts made before, or two or more parties exchange the composition of cash flows (Vashishtha ve Kumar, 2010). In a swap transaction, cash flows in exchange may be based on fixed or varying interest rates or a same or different exchange type (Gonzáles, Sandiás, López ve Búa, 2006). When compared to forward, futures and option contracts, swap contracts are the newest contracts in the category of basic derivatives (Dodd, 2004).

2.1.1.4. Option

An option contract is a contract which gives the right of purchase or sale for any asset to its buyer and does not lay any burden on its buyer (Gonzáles, Sandiás, López ve Búa, 2006). An option transaction based on exchange is a contract which gives the right to buy or sell a certain exchange of a certain quantity as equivalent to another fixed price called the strike price or the exercise price and does not impose any obligations (Sivakumar ve Sarkar, 2010).

In forward and futures contracts, there are mutual obligations and these must be fulfilled, but in option contracts there are alternatives about the transaction for the right holder. An option owner cannot use this right when he or she wants.

Under the option contracts, the buyer is entitled to a charge called the option bonus in response to the risk undertaken by the seller, whether the buyer uses the right of choice or not, and this change is paid by cash without considering whether the option will be used or not (Nurcan, 2005).

There are two types of option including purchase and sale options. Option contracts operate in both organized exchanges and over-the-counter markets. Option contracts can be arranged on the financial values such as exchange, interest rates, stock indexes or futures contracts as well as commodity (Nurcan, 2005).

2.2. Other financial methods

2.2.1. Leasing (finance lease)

Leasing is a financial technique which is commonly used in developed countries and also develops in our country in recent times. In the most general definition, leasing is *an arrangement in which the right to use an asset is transferred from the lessor to the lessee for a certain period of time* (Akgüç, 1998).

Leasing is a financial technique based on a type of rent. Hereby, leasing companies let investment goods especially requiring big capital on lease for natural and legal persons in exchange for the contract for a certain period of time.

In Turkey, instead of the word leasing, the idiom “finance lease” is used; one giving leasing called “the lessee”, one taking leasing called “the lessor”. “Finance lease is a contract which stipulates the possession of goods (right to use) must be given to the lessee for a good and valuable consideration in order to provide all types of benefits provided that the contract cannot be annulled for a certain period of time, the lessee takes the possession of goods from the third party on the lessor’s demand or in a different way (Kaya, 2011).

2.2.2. Factoring

Factoring is a transaction in which “short-term receivables are bought by a financial institution called a factor, their collection is taken on by this one at the term of sale price, a certain amount is paid by cash before the term if required, the risk for not collecting is considered and the receivable accounting is kept, these receivables result from the current or possible sale of goods and services for producing and trading companies engaged in the sale of goods and services for domestic and foreign markets” (Akgüç, 1998).

Given the purchase of rights arising from the sales with a factoring contract signed between the parties by “a factoring company” as 60-180 days term for firms making sales on credit, a factoring company pays the selling firm by cash immediately except for finance service and buys all receivables, provides debt collection at their term by following the receivables, keeps boks for accounting about these receivables and collects information about the potential customers’ financial structures (Özdemir, 2005).

Since factoring transactions guarantee debt collection and protect against the risk of payment in future, they provide a plan of cash flows for any enterprise in advance. Especially, it is a financial technique which helps the enterprise against the uncertainty of exchange in future.

2.2.3. Forfaiting

Forfaiting is "the purchase of receivables generally arising from goods and service export and considering a certain plan of payment by a bank or a specialized financial institute on this subject without the right of recourse for the previous right owners." Forfaiting is a medium-term finance source (Akgüç, 1998).

Forfaiting transactions are financial methods quitely similar to factoring transactions. The transfer of receivables to the financial institution and the conversion of the receivables into cash as of today are valid for two systems. The differences for forfaiting from factoring are that transactions are related with the receivables arising from international, commercial activity more and they have long-terms.

Forfaiting secures the enterprises about debt collection and protects them against the risks of rate and foreign exchange.

3. Management of Exchange Rate Risk in Foreign Trade Firms and Their Sensitivity

An ampirical study was done for measuring management of exchange rate risk and sensitiveness to the risk. This study focuses on the enterprises engaged in foreign trade activities in Konya which is one of the important cities in Turkey in terms of trade.

Konya province is in the 14th order of Turkey which has 81 provinces, in 2011 export classification with the export volume of 1.167.679.000 US Dollars and in the 5th order of Turkey, with 1.249 exporting firms. Also, according to 2011 import figures, it is in the 17th order of the country, with 1.170.270.000 US Dollars and in the 6th order, with 1.177 importing firms (www.ekonomi.gov.tr, 2012).

Although the number of foreign trade enterprises is considerable in Konya, it is observed that foreign trade figures are low. This situation shows us that there are lots of small and medium enterprises.

In this study, a questionnaire was made on the exporting and importing enterprises in Konya. The questionnaire form, which consists of three sections and includes 28 questions in these sections, was sent to the enterprises in an electronical environment with an e-mail. The e-mail addresses of the enterprises were taken from Konya Chambers of Industry and Commerce. The e-mails were sent to 1.536 e-mail addresses, it was seen that 685 enterprises got this e-mail due to the technical problems and non-current information. It was determined that 62 questionnaires were appropriate for the evaluation of the study among the questionnaires 86 enterprises involved in.

In this part, the questionnaire information was analysed as statistical data including three sections.

3.1. Characteristics of enterprises

At Table-1, the legal structures, statutes and staff numbers of the enteprises are given. According to this, 25 (59,7%) of the participant enterprises are Joint Stock Companies while 37 (40,3%) of them are Limited Companies. 58 enterprises are private ones with domestic capital by 93,5%, 4 enterprises are based on domestic-foreign capital by 6,5%. According to Turkey Undersecretariat of Treasury, the enterprises involved in the questionnaire consist of **Micro Enterprises** employing between 1 and 9 employees by 30,6%, **Small Enterprises** employing between 10 and 49 employees by 16,1%, **Medium Sized Enterprises** employing between 50 and 249 employees by 43,5% and **Large Sized Enterprises** employing 250 and over employees by 9,7%.

Table 1: Characteristics of Enterprises: legal structures, statutes, employee number

Legal Structures of Enterprises	**Frequency**	**%**
Joint-Stock Company	25	40,3
Limited Company	37	59,7
Total	62	100
Statutes of Enterprises	**Frequency**	**%**
Private enterprise with domestic capital only	58	93,5
Private enterprise with foreign capital only	0	0,0
Private enterprise with both domestic capital and foreign capital jointly	4	6,5
Public Enterprise	0	0,0
Total	62	100
Staff Number of Enterprises	**Frequency**	**%**
1-9 employees	19	30,6
10-49 employees	10	16,1
50-249 employees	27	43,5
250 and over employees	6	9,7
Total	62	100

At Table-2, the sectoral distribution of the enterprises and the registers of these enterprises in İstanbul Stock Exchange (İMKB) are showed. While the automotive sector comes the first by 38,7%, Machine (17,7%) and Mining&Metal Industry (16,1%) follow this sector. Only 4 of the enterprises (6,5%) involved in the questionnaire are registered in İMKB.

Table 2: Characteristics of Enterprises: Sectoral distribution and Registers in İMKB

Sectors of Enterprises	**Frequency**		**%**	
Package	6		9,7	
Office Stationery	2		3,2	
Consultancy and Education	1		1,6	
Chemical Industry	7		11,3	
Construction & Real Estate	6		9,7	
Mining&Metal Industry	10		16,1	
Machine	11		17,7	
Automotive	24		38,7	
Agriculture	3		4,8	
Food	2		3,2	
Note : Some enterprises operate in more sectors than one.				
Registration of Enterprises in Istanbul Stock Exchange	**Frequency**	**%**	**Frequency**	**%**
	YES		**NO**	
	4	6,5	58	93,5

The foreign trade activities of the enterprises are studied, accordingly, 33,9% (21) only export, and 66,1% (41) both export and import. 51,6 of the enterprises have started foreign trade between 2001 and 2010, their lives in foreign trade are of 10 years on average. At Table-3, sale volume and foreign trade figures are given.

Table 3: Characteristics of Enterprises: Starting Date in Foreign Trade, Sale and Foreign Trade Volumes in 2011

Starting date in foreign trade for enterprises	**Frequency**	**%**
1960 and before	1	1,6
Between 1961-1980	3	4,8
Between 1981-1990	1	1,6
Between 1991-2000	20	32,3
Between 2001-2010	32	51,6
2010 and after	5	8,1
Total	62	100
Sale volume of enterprises in 2011	**Frequency**	**%**
50-1.000.000 TL	11	17,7
1.000.000-5.000.000 TL	17	27,4
5.000.001-25.000.000 TL	19	30,6
25.000.001 TL and over	15	24,2
Total	62	100
Foreign trade volume of enterprises in 2011	**Frequency**	**%**
50-1.000.000 TL	17	27,4
1.000.000-5.000.000 TL	16	25,8
5.000.001-10.000.000 TL	12	19,4
10.000.001 TL and over	17	27,4
Total	62	100

According to Undersecretariat of Treasury and State Institute of Statics (DİE), of the enterprises, 17,7% are **Micro Enterprises** having the sale volume between 50-1.000.000 TL, 27,4% are **Small Enterprises** having the sale volume between 1.000.000-5.000.000 TL, 30,6% are **Medium Sized Enterprises** having the sale volume between 5.000.001-25.000.000 TL, 24,2% are **Large Sized Enterprises** having 25.000.001 TL and over. Also 27,4% of the enterprises have reached at foreign trade volume of 10.000.000 TL and over.

Table 4: Characteristics of Enterprises: Export Markets of Enterprises

Export Markets of Enterprises	**Frequency**	**%**
European Union Countries	43	69,4
Central Asian Turkish Republics	27	43,5
Middle East Countries	58	93,5
Russia and Eastern European Countries	31	50,0
North American Countries	12	19,4
South American Countries	14	22,6
China, Japan and Far East Countries	12	19,4
African Countries	34	54,8
North African Countries	19	30,6
Note : Some enterprises export in more regions than one.		

Looking at Table-4 and considering the export markets of the enterprises, the exports mostly belong to Middle East countries by 93,5% and European Union (EU) countries by 69,4%.

3.2. Following exchange rate movements and their place in organization

Table-5 shows the rate sources of the enterprises. The Central Bank rates are followed by 88,7%. And the movements of exchange rate are mostly followed in the enterprises by Top Management with 56,5% and Financing Department with 51,6%.

Table 5: Following Exchange Rate Movements and Their Place in Organization: Sources of Rate and Units Following Exchange Rate in Enterprise

Basic rate sources in arrangement of financial tables	**Frequency**	**%**
Central Bank	55	88,7
Capital Market Rates	10	16,1
Rates of Any Bank	10	16,1
Note : Some enterprises use more sources of rate than one.		
Unit which follows exchange rate movements in enterprise	**Frequency**	**%**
Top Management	35	56,5
Financing Department	32	51,6
Accounting Department	17	27,4
International Marketing/Export	22	35,5
Note : Some enterprises follow rate movements in more units than one.		

Table 6: Following Exchange Rate Movements and Their Place in Organization: Follow-up Instrument for Rate Changes in Next Future and Reason for Predicting Rate Movements

Follow-up instrument for possible changes in exchange rate in next future (1-6 months)	**Frequency**	**%**
From special reports and works by a bank or private institutions	42	67,7
From data by a private counsultancy company	17	27,4
From predictions in economy-policy newspaper and journal	44	71,0
Note : Some enterprises use more sources of following rate than one.		
Reasons for predicting exchange rate movements	**Frequency**	**%**
For export transactions (Pricing, Debt Collection, Debt Term)	58	93,5
For income-expense predictions of enterprise	26	41,9
For managing exchange debts	31	50,0
For keeping the value of exchange in savings	12	19,4
Note : Some enterprises have more reasons than one for predicting rate.		

The enterprises benefit from economy-policy newspapers and journals by 71%, banks and private institutions by 67,7% consultancy companies by 27,4% for rate predictions in next future.

Table 7: Following Exchange Rate Movements and Their Place in Organization: Following Exchange Rate Movements and Reactions Against Rate Movements.

Following Exchange Rate Movements and Reactions Against Rate Movements	**Frequency**	**%**	**Frequency**	**%**
	YES		**NO**	
Does your enterprise follow exchange rate movements?	58	93,5	4	6,5
Do you predict exchange rate movements in next future (1-6 months)?	40	64,5	22	35,5
Do you make any change in enterprise functions when a change occurs in the exchange rate?	39	62,9	23	37,1
Does your enterprise follow a long-term plan or program such as the enterprise's value, its competitive power, the determination of the current value of next cash flows in accordance with long-term exchange rate movements?	21	33,9	41	66,1

At Table-7, following rate movements is analyzed. The enterprises follow the movements by 93,5%, make predictions over 60 percent and make changes in the movements of the enterprise. But 33,9% keep a long-term plan for their future.

Table 8: Following Exchange Rate Movements and Their Place in Organization: Arrangement of Cash Flow Table and Pursuit of Exchange Movements in Tables

Arrangement of Cash Flow Table and Pursuit of Exchange Movements in Tables	**Frequency**	**%**	**Frequency**	**%**
	YES		**NO**	
Is a long-term cash flow table being arranged in your enterprise?	39	62,9	23	37,1
Are exchange rate changes at cash flow table being evaluated in your enterprise?	30	48,4	32	51,6
Is there any classification on debts and debt term based on exchange at cash flow table in your enterprise?	50	80,6	12	19,4
Is the risk being repaired by putting the same types of exchanges into the same term in a cash flow table in your enterprise?	34	54,8	28	45,2
Are financial tables being arranged with foreign currency unit in your enterprise?	32	51,6	30	48,4

While organizing a cash flow table in general, half of the enterprises evaluate changes in an exchange rate at these tables on average. 80,6% make classifications of debt and debt term at cash flow tables and 54,8% match terms of exchange types.

3.3. Sensitivity to exchange rate risk

Table 9: Sensitivity to Exchange Rate Risk: The most important risk perceived in foreign trade and exchange rate risk

The most important risk which is perceived in foreign trade transactions	**Frequency**	**%**
Political risks in other countries (war, legal situation, political regime, etc.)	33	53,2
Commercial risks (transportation, insurance, quality of goods,standards, etc.)	13	21,0
Socio-cultural risks (language difference, cultural difference, racism, etc.)	0	0,0
Risks caused by the uncertainty of exchange rate in a country	16	25,8
Total	62	100
Perceived exchange rate risk	**Frequency**	**%**
Accounting (Conversion, Translation) Risk	20	32,3
Transaction Risk	25	40,3
Economic Risk	13	21,0
All	21	33,9
Note : The enterprises can perceive more risks of exchange rate than one.		

According to the enterprises involved in the questionnaire, the most important risk which is perceived in foreign trade transactions, is a political risk (war, legal situation, political regime) in other countries by 53,2% (33 items). The enterprises perceive the exchange rate risk as the transaction risk by 40,3% at most.

The enterprises' attributes to the risk are given at Table-10. Hereby, the enterprises display courageous attributes about taking any risk, 67,7% (42 ones) say: "The exchange rate risk can be undertaken at certain level, managed." Also,22,6 önceden tahmin etme tutumundayken sadece %9,7'si riskin yönetilemeyeceğini savunmuştur.

The enterprises try lots of methods against the exchange rate risk. The preferred methods are distributing risk by creating portfolio with different exchanges by 62,9%, applying an earlier date for payment or delaying it and matching debt and debt terms by 51,6%, taking exchange credit by 48,4%.

Table 10: Sensitivity to Exchange Rate Risk: Attribute to Management of Exchange Rate Risk, Transactions against the Risk

Attribute to Management of Exchange Rate Risk	**Frequency**	**%**
The exchange rate risk cannot be managed, the risk should not be undertaken.	6	9,7
The exchange rate risk can be undertaken at certain level, managed.	42	67,7
The exchange rate risk can be predicted before, managed.	14	22,6
Total	62	100
Transactions against Exchange Rate Risk	**Frequency**	**%**
Applying an earlier date for payment or delaying it	32	51,6
Distributing risk by creating portfolio with different exchanges	39	62,9
Taking exchange credit	30	48,4
Matching debt and debt terms	32	51,6
Factoring	0	0,0
Forfaiting	0	0,0
Leasing (Finance Lease)	7	11,3
Making transactions at Futures and Option Exchanges (Derivatives)	3	4,8
Note : The enterprises makes more transactions than one against the exchange rate risk.		

Table 11: Sensitivity to Exchange Rate Risk: Popularity and Usage of Derivatives and Financial Methods in Exchange Rate Risk Management

Popularity and Usage of Derivatives and Financial Methods in Exchange Rate Risk Management	**Frequency**	**%**	**Frequency**	**%**	**Frequency**	**%**	**Frequency**	**%**	**Frequency**	**%**
	Don't know / Haven't Heard Before		**Heard / Don't Know**		**Partly Know**		**Know**		**Totally know**	
What do you know about VOB?	10	16,1	19	30,6	22	35,5	6	9,7	5	8,1
What do you know about derivatives exchange (Forward, Futures, etc.)?	15	24,2	15	24,2	20	32,3	8	12,9	4	6,5
What do you know about the financial instruments such as Factoring, Forfaiting, Leasing?	5	8,1	11	17,7	11	17,7	18	29,0	17	27,4

Looking at Table-11, 35,5% of the enterprises partly know about Futures and Option Exchanges (VOB) while 16,12% do not know about them. The derivatives (Forward, Futures, etc.) are partly known by 32,3%. The financial instruments such as Factoring, Forfaiting, Leasing are commonly known rather than other methods, 29% of the enterprises state that they know and 27,4% totally know about these.

Table 12: Sensitivity to Exchange Rate Risk: How Often Finansal Techniques Are Used

How Often Finansal Techniques Are Used	Frequency	%	Frequency	%	Frequency	%
	Always		Sometimes		Never	
Repurchase agreement	0	0,0	14	22,6	48	77,4
Factoring	0	0,0	16	25,8	46	74,2
Forfaiting	0	0,0	6	9,7	56	90,3
Leasing (Finance Lease)	0	0,0	30	48,4	32	51,6
Futures Transactions	0	0,0	8	12,9	54	87,1
Option Transactions	0	0,0	6	9,7	56	90,3
Forward Transactions	0	0,0	8	12,9	54	87,1
Swap Transactions	0	0,0	2	3,2	60	96,8

At Table-12, the usage frequencies of financial techniques are given. According to this, the most frequently used technique is Leasing (Finance Lease) with a reply of “sometimes” by 48,4%. The least preferred technique is Swap Transactions by 3,2%.

Table 13: Sensitivity to Exchange Rate Risk: Reasons for not practicing protection strategies in the management of exchange rate risk in enterprises

Reasons for not practicing protection strategies for the managamenet of exchange rate risk in enterprises	Frequency	%
We Döviz kuru riskini çeşitli yöntemlerle yönetiyoruz	53	85,5
We have no information about these techniques	16	25,8
It is not possible to practice these strategies in Turkey	12	19,4
Derivatives markets are not developed	5	8,1
The consulting firms and financial institutions do not inform	10	16,1
We have had no need until this time	16	25,8
Insufficient legal infrastructure	7	11,3
Note: The enterprises give more reasons than one for not practicing protection strategies against the exchange rate risk.		

By 85,5, 53 enterprises say “We have been managing the risk of exchange rate with various methods”.

Conclusion

The exchange rate risk arising from market fluctuations and other reasons in foreign trade is one of the important risks experienced by the enterprises, furthermore, this affects the economic activities of the enterprises in future. The future uncertainty of exchange rates limits the movements of the enterprises in the current competitive environment, gives some damages. In order to remove or to minimize these uncertainties and their effects, the perception and management of risk for the exchange rate will bring an advantage for the enterprise’s future plan.

In this study, the reasons of exchange rate risk and types of exchange rate are analyzed. This focuses on alternative methods and financial methods about the management of exchange rate risk. The derivatives are explained as one of the most effective methods in risk management. It has been understood that the enterprises will be protected from the risks with the alternative methods such as Forward, Futures, Swap, Option and the other financial methods such as Leasing, Forfaiting, Factoring.

About the perception and management of exchange rate risk the attributes and activities of the enterprise are studied in a questionnaire. Some opinions are given about their sensitiveness to the risk management and protection methods for the enterprises in this study.

According to this, the enterprises operating in Konya generally fall into the category of Small and Medium Sized Enterprises, these enterprises have not been developed enough as institutions. Although they have positive attributes about the perception of exchange rate risk, it is observed that they cannot use the protection strategies about the risk management and the sensitiveness to the risk.

The enterprises try to manage the exchange rate risk by closely following the rates, leading to short-term transactions, keeping away from long-term transactions, matching term-debt and using alternative exchange portfolios and exchange credits. The enterprises cannot still use the alternative protection methods and financial techniques enough. The results here show that the enterprises are courageous for taking and managing risk but they do not have enough information about these.

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Service Standards: Measuring and Optimizing the Value of Service in Cloud Computing

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Abstract

Economies are increasingly dominated by the service sector. More than ever, research is needed to address approaches that measure and optimize service. This paper examines service value in cloud computing and develops a conceptual framework for a service value model. It seeks to address the essential research question of how service value is measured within the cloud computing context. This paper argues that a clear definition of the concept of service value is of critical relevance in measuring the concept within the cloud computing phenomena.

By having reliable metrics and consistent service, cloud computing service providers can optimize all the dynamic entities needed to deliver service value. A higher standard of service delivery is more likely to occur as a result of the IT service provider's measurable performance outcomes. Only then will academics and business practitioners have the solid data to correlate the value of cloud computing services to the financial performance of the organization. The paper advances the literature on the science of service by underscoring the benefits of service value optimization and measurement.

Keywords

Cloud computing, service value, measurement, standards

Online Presence – The Case of the Hungarian Travel Agencies

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Abstract

The importance of online presence is no longer a question to ask for neither tour operators nor travel retail agencies. It can be a good marketing tool; an information resource; and it is more and more the place of two-way communication and sales activity. In this study the homepages of almost 440 eligible Hungarian outbound agencies are examined by a predefined check list. The main research questions are:

- What points are typical regarding the content and the look of the homepages?
- Are there any characteristics that are common – as a standard?

As the result of the research the authors are able to identify the standard elements of the tour operator and retail travel agency websites. These findings can help a new actor in the market to save the time and money, and make the website for their customers easier to handle– or (on the other hand) it can help agencies to differentiate themselves.

Keywords

Webpage, travel agency, standard elements

1. Brief Overview of the Hungarian Travel Agency Market

The travel agency market in Europe is quite different regarding the Northern part with mainly outbound tourism characteristics and the Southern, traditionally hosting countries. In Germany and Great Britain for instance there are big integrations, which rule the market. Such integrations are:

- Rewe Group, which remained the leading German company for travel retail in 2010, with growth in revenue as well. (euromonitor.com)
- TUI Travel Plc has been the leading company in Great Britain for some years now. Having several strong brands like Thomson or First Choice, it could survive recession and maintain its position. (euromonitor.com)
- Thomas Cook Group Plc stays as the second largest travel retailer in the UK.

These three are present and determining in other European countries as well – for example in Austria, Ireland or Czech Republic. On the other hand stands Italy where there are no large integrations and the market is much more fragmented with several small and medium sized enterprises.

The Hungarian market is a little bit between the Northern and the Southern examples. There are also large companies, but they do not have such serious influence than TUI in the UK for instance. Traditionally the Hungarian market has been dominated by medium and small-sized travel agencies. According to the Hungarian Commercial Authorization Office 1160 enterprises has been registered as travel agencies in Hungary at the time of the research (April, 2012) (mkeh.gov.hu). 74% of the agencies had the license for tour operation and sales agency at the same time and approximately half of them originated in the capital, Budapest. Regarding the one-functioned agencies, most of the operators are in Budapest and less than 40% works down in the country – while at the case of the sales agencies it is just on the contrary.

Although Hungary is traditionally an inbound country it is also a great amount of tourists that travels outside for city breaks, cultural round trips or summer holidays. To fulfill the demand there are outbound, inbound, domestic, online, and mediating offices as well. The biggest enterprises have several agencies in the country. Considering the number of these operating locations the first five enterprises are shown in Table 1.

Table 1: Companies with the most of own agencies

Name	Number of agencies	of which in Budapest
NUR Neckermann	88	22
IBUSZ	40	9
Questor	20	4
OTP Travel	15	6
Vista Travel Agencies	14	7

Source: own compilation after mkeh.gov.hu

But regarding the market share the ranking of the largest companies changes. IBUSZ Rt is the leading travel retailer, followed closely by (German originated) NUR Neckermann Kft, Vista Travel Agencies Kft and Best Reisen Kft. While IBUSZ is the leader in terms of domestic travel, Neckermann is the most significant player in terms of outbound destinations, Vista is strong in airline ticket sales and Best Reisen is one of the largest players in the package holiday category in Hungary (euromonitor.com).

In Hungary there is a special customer attitude towards the travel agencies. After the transition in 1989-1990 many agencies had been launched with more – but usually less success. In the 1990s there was a series of breakdowns and the Hungarian travelers became disbelieving. This wobbliness and the mistrust of the customers remain although now the market is better regulated.

After successful years in 2005 and 2006 the sales of travel retail products started to decline in 2007, due to decreasing real wages and the fact that holidays had become less of a priority for Hungarians. The economic crisis exacerbated the situation from 2008. The lowest-income segments fell out of the travelling population completely during 2009-2010, and the middle-income segment, the traditional target of travel retailers, also lowered their travel expenditures (euromonitor.com).

2. The Role of the Internet

The Internet is the most important innovation since the development of the printing press (Hoffman, 2000, Klausz, 2011). In 2011, worldwide Internet users reached 2.27 billion (32.7% of the population worldwide) including more than 500 million Internet users in Europe (www.internetworldstats.com). This statistic represents an increase of 528% compared to year 2000. With a continuous growth in 2010 Internet penetration reached 61.8% in Hungary as well (internetworldstats.com).

Since the emergence of the Internet, travel planning (e.g., travel information search and booking) has always been one of the main reasons that people use the Internet (Buhalis and Jun, 2011). Numerous studies and articles pronounced that the Internet and the World Wide Web has also created a new competitive business environment (Kim et al, 2007) – and indeed it has not finished yet. First there was a panic attack – mostly in the agents' side; they viewed the Internet as a threat to their livelihoods, as something that would 'kill' travel agencies (Syratt, 2003; Özturan and Roney, 2004). Tour operators saw it otherwise: as an opportunity to expand their distribution outlets that is to get their products (namely their holidays) in front of more potential customers – while also cutting (human resource) costs. It is now clear that the Internet means not the end but the beginning of a new era where the web is the most widely used tool (Chiou et al, 2011).

Therefore the importance of online presence and maintaining an effective web site is essential (Law et al, 2010) – for both tour operators and travel retail agencies. Syratt (2003) adds also that a fully interactive site is what really needed. Potential clients visit the website any time of the day or night to search for holidays and, if they want, to book also. Actually this "lack of opening hours" is one of the numerous benefits of the online presence, like (Buhalis and Jun, 2011):

- Reduce cost of information processing, storage, distribution
- Customization/personalization at a reasonable cost
- Seller can specialize in a narrow field
- Rapid time-to-market and increased speed
- Lower communication cost
- All distributed material can be up-to-date

Undeniably it was the marketing that has been drastically changed with the emergence of the Internet (Zhang, 2003), but nowadays the Internet means much more: it is mainly the place of two-way communication. Tour operators or travel agencies can realize interactive communication on many platforms, like social media, travel portals, or their own homepages.

But the goal of this paper is not to look at all the possibilities travel agencies use – or could use. Only the own webpage is examined this time, researching if there is anything common, which can be identified as a standard element.

3. Standardization vs. Customization

Researchers use different words and concepts to define standardization and customization. Sundbo (2002) interprets standardization as a way of lowering costs and prices, but increasing productivity. He sees standardization as a method which 'produce' the same service product every time (Sundbo, 2002). In case of standardization consumers need to assess the quality of a product and compare its price with the price of similar products (Sundbo, 1994). According to Tether et al (2001) a well-functioning standardization can cause high production volumes, but a quite distant relation with the customer, which is why it is more often used in price sensitive markets where the economy of scale is very important, adaptation costs are high and the cost of labor force is low (Tether et al., 2001).

As Sundbo (2002) defines customization means that every customer receives an individual service. He states that in the course of customization the service product is 'produced' in a concrete situation as an individual solution to a customer's specific problem. Customization is based on the fact that service product cannot be stored and that is why it has to be consumed in the moment of production, which makes the consumer a co-producer. It concentrated on the individual customer or guest there for called customization. However the rate of customization can be different. Customization means another type of logic, the logic of luxury only for those who can afford. Nowadays western economies are luxury economies, which mean that buyers of services can afford quality and they also expect it (Sundbo, 1994).

Table 2: Advantages of standardization and customization

Advantages of standardisation	Advantages of customization
Customer satisfaction	Customer satisfaction (unique product)
Zero failure	Ensures quality
Easy to steer the costs	Increase price and income
Increasing productivity	Easy to expand the sold man-hours
Systemised innovation (Sundbo, 1994)	Innovation is customer-near (Sundbo, 1994)

Source: own compilation

As it can be seen on Table 2 there are advantages of standardization and customization as well. Their application is based on the customers of the company. However some researchers think that these two dimensions should be used at the same time to mix the advantages and avoid disadvantages. They created some theory for this fact such as modulization (Sundbo, 1994), or in one of the authors' previous article a theory which says that customization is based on standardization and customization cannot work effectively without standardization as a basis (Gyurácz-Németh, Clarke, 2011)

4. Research Methodology

With the growing penetration of the Internet – also research activity has increased. Academic researchers mainly advocated the importance of assessing website effectiveness (Law et al, 2010), which is said to be best measured by webpage evaluation. As it is a newly emerging research area, it has no globally accepted definition yet, however it is mostly characterized as *the act of determining a correct and comprehensive set of user requirements, ensuring that a website provides useful content that meets user expectations and setting usability goals* (Law et al, 2010). In general, prior studies on website evaluation fall into two broad categories: quantitative and qualitative.

The research, shown in this paper, is a quantitative one – but not a traditional website evaluation. It was rather a supply-side approach: the main objective was to collect the characteristics of the homepages of Hungarian outbound agencies. Outbound and inbound agencies operate differently; of course they have different goals as well by developing a homepage. The reason why only outbound agencies were examined is very simple: they work on the 'same' market where at least the main economic, social, political, etc characteristics of the target groups are the same. The main research questions were:

- What are the web pages like?
- What points are typical regarding the content and the look of the homepages?
- Are there any characteristics that are common – as a standard?

The methodology of content analysis was applied: by a predefined check list the homepages of all the eligible travel agencies were examined. The steps of the research can be given as follows:

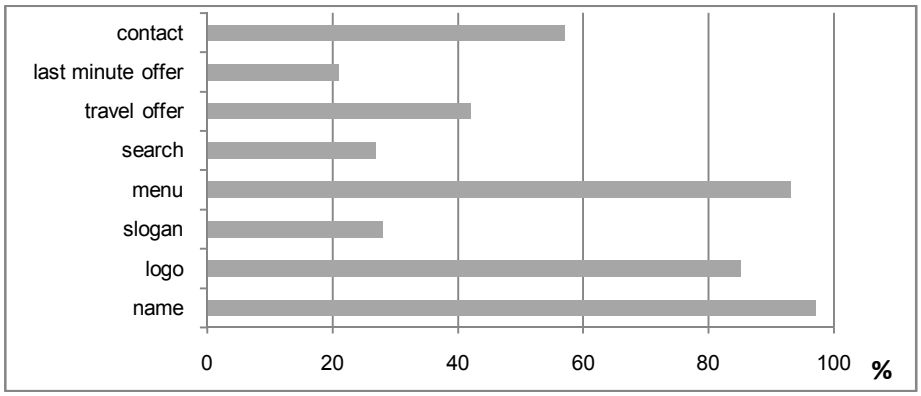
1. Collect all the outbound travel agencies. There are traditional agencies without a webpage, traditional agencies having an online surface beside their office and online travel agencies as well. The objective was to find all the *homepages* of the travel agencies, which have outbound programmes or only separate services.
2. Develop an evaluation sheet/check list for data collection. The so-called check list was needed to minimalize the subjective part of the evaluation process as much as possible. There were mostly closed and mainly 'yes-no' questions applied.
3. Tourism (BA) students were given the homepages and the sheets in excel form and they had to evaluate the online surface – according to the "check-list"-like evaluation sheet.
4. Gathered data were put together into one big sheet and analyzed by MS Excel.

Although the goal was to have the evaluation of every outbound travel agencies, it was hardly possible as unfortunately some of them was just under construction, out of order – or simply not existing. Finally 3 of the complete evaluations were not valid, so 437 of the existing travel agency-sites mean the research sample.

5. Research Findings

First of all the upper third of the travel agencies' webpage had to be evaluated. This part was chosen because the question was: "What can be seen at first sight?" As different computers and different browsers may show the sites differently – this restriction is supposed to be applicable.

Figure 1: Information types found in the upper third of the sites



Source: own compilation

Some agency prefers to have an 'intro' page, where the visitor has to choose language (8 cases), searched tourism product (9 cases) or something special to get to the main homepage. But most of the web pages (92%) has no 'intro': the starting page can be seen when opened.

As Figure 1 shows, basic information like the name and the logo of the travel agency can be found on the majority of the web pages – while (surprisingly) the slogan, the traveling offers or the contact information are not that important. The expectation was that contact information is still primary and can be well seen 'at first sight'. According to the changes of the consumer behavior and internet use e-mail address and chat possibilities are the most important contacts instead of the address of the 'real' office. As Figure 2 shows, indeed, the travel agencies find it important to put their e-mail contact on the web (69%). But giving chat opportunity to communicate interactively with the visitor (potential traveler) is really an unused possibility (only 18% of travel agencies have it).

Figure 2: Main contact information and frequency

Source: own compilation

Having chat service usually means using Skype: 85% of the agencies, which have chat possibility, use this service. The username is mainly the name of the travel agency, but in some cases also the person, who is just there to answer, is displayed. Of course online-offline mode can be seen – and the experience shows that in Hungary 24-hour availability is not typical; chat is *online*when the 'real' office is open.

The most important part of online presence should be the presentation of traveling offers. However it is interesting that 30% of the agencies have no 'hit' offer in the starting page. Of course the visitors can search, mainly by

- product (summer holiday, city break, etc.) (68%);
- destination (64%);
- services (type of travel, type of accommodation, etc.) (58%).

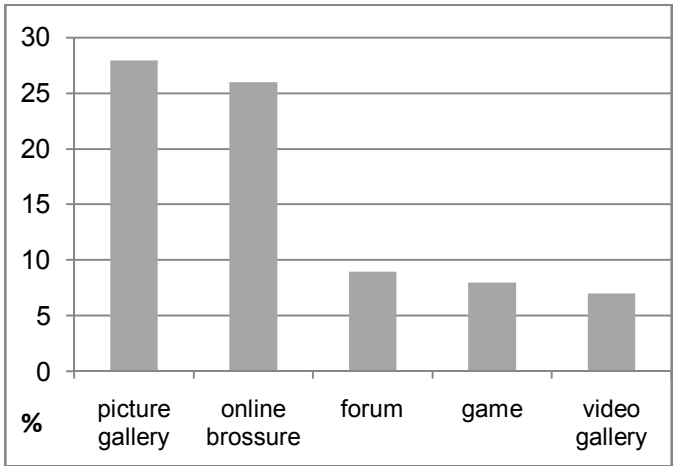
Very few, only 70 travel agencies (16%) find it important to have a site map helping web page orientation. Those who have 'hit' offer in the starting page, rarely choose to have a lot of, frequently changing offers (27%) – although it is a typical way of 'hit' offers– looking at other Hungarian web pages. Regarding the 120 agencies, which are changing offers frequently, they have an average 5 or 6 offers in the row with a slight deviation (the maximum an agency has is 40 offers).

While evaluating, the most of the offers had to be looked closer to answer the question if there was any offer out of date. The sad statement can be put here: travel agencies do not pay much attention to pick off the obsolete offers. Almost 20% of the examined sites contained old offers (an average 5 or 6 pieces) and 8 more web pages had uncountable many of these.

Another examined characteristic was the amount of "entertainment possibilities" – as it is called by the authors. These possibilities are not tightly connected to sales activity, but help to keep visitors in

touch and makes them recurring. Having a picture or video gallery, having a forum where experiences can be exchanged, offering various games (e. g. photo contest) or votes are all possibilities to make visitors come back to the homepage and see it again. There is no doubt about the usefulness of these – yet Hungarian travel agencies may not see too much potential advantage, as there are very few of them to provide any entertainment possibility. Figure 3 shows that best preferred is the picture gallery – but less than 30% of the agencies offer it on the web site.

Figure 3: 'Entertainment' possibilities



Source: own compilation

Effective online presence is greatly influenced by the atmosphere of the home page. Regarding the colors of the examined sites, undeniably the white-blue couple is the leading one. As the majority of the outbound travel agencies sell summer holidays, it is not surprising – and also evident that the third beloved color is yellow.

As students had the opportunity to outline their own opinion about the evaluated site in general – a little demand-side research was delivered as well. These opinions show that the easy-to-manage, simple web pages are the most successful, with few colors and many pictures.

6. Conclusions

The aim of the research was to make authors able to identify the standard elements of the tour operator and retail travel agency websites. These findings can help a new actor in the market to save the time and money, and make the website for their customers easier to handle by putting the standard characteristics on the new website. These standard elements are the followings:

- name,
- logo,
- contact (telephone, email and mail address as well) of the company on the upper third part of the website
- picture gallery and online brochure,
- 5-6 up-to-date offers presented on the website

On the other hand the results can make it possible for tour operators and travel agencies to differentiate themselves in other ways from their competitors, to customize their websites and create a unique product for the customer. The customization possibilities are the followings:

- 24 hour chat opportunity,
- site map placed on the upper third part of the website

- video gallery,
- game opportunities (photo contest) on the website.

The research was able to show the common elements and development possibilities of the tour operator and travel agency websites. The most important advice to give to these companies is that they have to improve their services and communication continuously, but they mustn't forget the standard requirements which make the websites easier to handle and reliable for their customers.

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Intention to Complain: Insights from the South African Restaurant Industry

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Abstract

The South African restaurant industry is fiercely competitive; with many restaurants either closing down or struggling to survive during recent difficult economic times. The industry is characterized by a wide range of restaurants ranging from fast food restaurants to sit-down restaurants that are either franchised or independently owned. As in most other industries, retaining a loyal customer base is paramount for survival in this industry irrespective of the form of ownership or business model followed.

Due to the high level of customer contact in the industry, restaurants are particularly prone to service failures that often result in unsatisfied customers. When a customer complains about a service failure to the restaurants staff it creates an opportunity for the staff to address the complaint by enforcing a service recovery strategy which aims to return the complaining customer to a state of satisfaction. In doing so, the likelihood that the customer could be retained increases while limiting the spreading of negative word-of mouth.

According to Velázquez *et al*. (2010) general and situation-specific factors influence the complaining behavior intentions of customers when unsatisfactory service has been experienced. General factors relate to consumers' general attitude towards complaining and the amount of information or experience they have. Situation-specific factors relate to the context within which the service failure has occurred and include: the customer's level of dissatisfaction with the particular service failure; the perceived importance of the situation within which the service failure has occurred; and the customer's perceived likelihood that the complaint will be successfully addressed once lodged (Velázquez *et al*., 2010).

This study focuses on investigating the general complaint behavior intentions and the strength of the relationship between these intentions as well as the situation-specific determining factors of complaint behavior in the South African restaurant industry. The general complaint behavior intentions of customers specifically relate to private and third party responses to complaints as well as how customers complain to the restaurant staff whilst the situation-specific determining factors include those stipulated in the preceding paragraph.

The study was quantitative in nature and a descriptive research design was followed. Convenience sampling was used to select respondents who have patronized (eaten or bought food at) a restaurant *and* who have experienced unsatisfactory service at any restaurant patronized during a six month period prior to the data collection. A self-administered questionnaire was used to collect

data from206 respondents. The constructs of interest to the study were measured on a 5-point unlabelled Likert-type scale. A demographic section was also included in the questionnaire to determine the profile of respondents. The items included in the measurements sets measuring the constructs of interest were adapted from a previous study and was found valid and reliable in this study(Velázquez *et al*., 2010).

Taking the unsatisfactory service experience at a restaurant into account, respondents indicated that they are most likely to undertake the following complaint behaviors: 'I would tell my friends and/or relations about my bad experience in that restaurant', 'I would discuss the problem with the restaurant manager' and 'I would comment on the problem at the restaurant so they can improve'. These complaint behavior intentions involve both a private response and complaining to restaurant employees themselves.

The study uncovered a significant positive linear relationship between the *level of dissatisfaction experienced* by respondents and the complaint behavior intentions that involve *private responses* such as 'I would not go back to the restaurant again', 'I would tell my friends and/or relatives about the bad experience in that restaurant', 'I would go to other restaurants from then on' and 'I would persuade my friends and/or relations not to visit that restaurant'. With regards to the *level of dissatisfaction experienced*, it was also found that a significant negative linear correlation exists between this variable and the *perceived likelihood* that the complaint will be successfully handled. Complaint behavior intentions that involve *third party responses* such as 'I would write a letter to a local newspaper describing my bad experience', 'I would tell a consumer protection body of my problem' and 'I would take legal action against the restaurant' furthermore exhibit a significant positive linear relationship with the *perceived importance of the situation*.

The results of the study indicate that when unsatisfactory service is experienced at a restaurant, customers rather engage in private responses (telling friends and not returning to the restaurant) before they complain to restaurant employees. Complaining to a third party is, however, viewed as a least likely response. Moreover, the study also uncovered that the higher the level of dissatisfaction restaurant customers experience, the more they are inclined to engage in private responses and the less likely they are to believe that the restaurant is able to deal with a complaint successfully. This is of particular concern since restaurants may thus not receive the complaints about serious service failures; instead the offended customers will simply switch to another restaurant and not return and will furthermore, spread negative word-of-mouth. Employees at South African restaurants should therefore put measures in place to elicit feedback and complaints from customers in order to get a chance at service recovery, especially when it comes to service failures customers consider especially dissatisfying.

The study also indicates that the more important respondents perceive the situation within which the unsatisfactory service was experienced, the more these customers tend to engage in third party complaint behavior. Restaurant employees therefore need to identify the reason why a customer or group of customers is patronizing the restaurant at a particular time, for example a table is booked to celebrate a wedding anniversary. By knowing why customers are patronizing the restaurant, restaurant employees will be able to focus on providing satisfactory service especially when the 'occasion' is of great importance to a customer.

The results of the study provide some insight into the complaint behavior intentions of restaurant customers in South Africa and could assist restaurant staff in understanding the importance of eliciting complaints from customers as an opportunity for service recovery which can lead to greater customer satisfaction. The study also highlights the role of the level of perceived dissatisfaction in

generating private responses and the role of the level of perceived importance of the situation in generating third party responses.

Keywords

Customer complaints, complaint behavior, restaurants, South Africa

Is Standardization a Risk Factor in Hungarian Health- and Wellness Hotels?

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Abstract

Introduction – Hungary's geothermal facilities are prominent, that manifest in about 600 thermal fountains, 213 certified mineral water, 218 certified medical/curative water, 74 medical spa and 169 health and wellness tourism related hotels. The Hungarian government has been assisting the development of health tourism and set the aim to be the worlds' leading health-tourism destination. The first assistance period started ten years ago, when actually wellness tourism begun to evolve in Hungary. The programme was called Széchenyi Plan. Nowadays, in the times of the New or the Second Széchenyi Plan, health tourism is an emphasised product not only in tourism, but in economic development as well. According to the Hungarian National Tourism Board Ltd's data, one third of the total income in hotel sector is realised by the health- and wellness tourism (HWT) related hotels, even though occupancy rates are not yet as not as high as expected.

Research questions – As a part of an extended study this paper is focusing on standardization as a risk factor. According to the model of the extended research, perception and management of risk factors are influenced by *external potential attributes* (like currency rate fluctuations or difficulties of assistance system); *internal potential attributes* (like trends or new competitors on the market); *enterprise attributes* (like size of the hotel, safety or quality insurance); and *personal attributes* (like gender, age or family status). Along two dimensions of a matrix, namely perception and management of risk factors, it is possible to differentiate the following range of attitudes: totally alarmed, acceptors and blinkered. Among the enterprise attributes standardization can be seen as an important tool of quality assurance in the hotel, like having/observing/missing external and/or internal standards in the hotel management.

Methodology – As the first step a qualitative survey was carried out among GMs of HWT related hotels to identify the themes of my research. With the help of the 6 deep interviews risk-definition, risk categories and risk factors were identified. The results of this qualitative research served to delimit especially the field of risk factors, because it is not possible to deal with all the factors. Based on the interviews and the literature a questionnaire has been devised and has been sent to the general managers of the Hungarian health-and wellness hotels that are members of the Hungarian Hotel Association. The SPSS software is going to be used to analyse the data.

The Competiveness of Estonian Business Sector Before, During and After the Economic Crisis[1]

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Abstract

The aim of this article is to analyze the competitiveness development of the Estonian business sector in the Baltic Sea region primarily the labor costs and productivity aspect before, during and after economic crisis. Theoretical literature about labor costs as a important factor in international competitiveness will be studied. Empirically the author analyses the size and dynamics of labor costs and productivity in Estonia at the national and sectoral level. Different sectors of economic activities in Estonia hold different positions in international competitiveness due to different level and development tendencies of labor costs and productivity. The analysis presented refers to the relation of relative employee and gross salary productivity to average productivity in whole economy. During the last two years, in Estonia a turnaround in development of total ULC as well as gross and net salary unit costs took place. The Estonian economy structure developed in direction to the pre-boom situation.

Keywords

International division of economic activities, international competitiveness, labor costs, labor productivity, sector productivity

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1. Introduction

The cornerstones of international economic competitiveness are low labor costs in comparison to the labor productivity level, especially in countries with labor intensive production. In Estonia we can detect different tendencies of labor costs and productivity developments before during and after the economic crises.

The aim of this article is to analyze the development tendencies of labor costs and labor productivity in Estonia as important factors of international competitiveness of the business sector. The following research tasks have been tackled:

- To analyze the importance of labor costs and productivity as a factor of international economic competitiveness on the base of scientific literature.
- To analyze empirically the general tendencies in ´labor costs and productivity between economic activities before, during and after the economic crisis

The first part of the article is based on various scientific literature sources. The empirical analysis presented in second part uses data from Eurostat and Statistic Estonia online databases.

2. The Labor Costs and Productivity as Factors of International Economic Competitiveness

The term "economic competitiveness" is an object for discussions, especially at the country level. Boltho's (1996: 1-2) assessment of 15 years ago is still relevant: there are no consistent definitions of competitiveness and the term seems to mean different things to different people. But at the same time most researchers evidently do not share Paul Krugman's (1994: 44) pessimistic view that the application of the term "competitiveness" at the country level is meaningless, wrong and dangerous. Attempts to understand the nature of "competitiveness" and quantitatively measure it have continued in various countries. Zanakis and Becerra-Fernandez (2005: 186) distinguish between cost-competitiveness, price-competitiveness and non-price competitiveness. A survey presented by Eckhard Siggel (2007) points out that different researchers accentuate different facets of competitiveness; for example, size and increase of market share, export performance, price ratios, cost competitiveness and so on. One of the most widespread approaches pointed out in the literature is the concept of unit labor costs (ULC) as the product of wage rate, labor productivity and exchange rate. (Siggel 2007: 8).

The wage and tax level in Estonia was relatively low compared to that of its Central European competitors. Therefore, remarkable growth was achieved in labor productivity, partly due to the flow of the labor force from low productivity economic sectors to high productivity ones (Laurson, Grawe 2004). A prognosis aimed at the entrepreneurs in advanced old EU member states forecast that despite this growth tendency, over 25 years the wage level in the new member states would only make up 75% of the old member states' wage level, due to the very low initial level (Alho et al. 2004). The cost level in Sweden is seven times higher than in Estonia and ten times higher than in Latvia. On the other hand, there were also skeptics who did not believe in the sustainability of the low wage based economic development strategy because economic growth inevitably brings pressure to increase wages (Ketels 2006).

Low wage level is undoubtedly attractive to businesses that exploit a low-skilled and low-paid labor force, but unions abroad tolerate outsourcing of intermediate production only so long as it does not become a threat and compete with the high-skilled and high-paid labor force at home. Therefore, in developing the Baltic economy, another precondition is often mentioned: the prevention of any kind of "friction" in the labor market (Svedberg 2005). Paavo Okko (2007) has explained that the convergence between the new EU countries with low wages and the old EU countries is a long term

and arduous process. At first the new EU countries are able to achieve quicker growth rates in wages (β-convergence), but the overall absolute differences in nominal wages remain (σ-convergence will not be achieved). If Estonia could have maintained an average 6.6% yearly growth in real GDP from 2008 to 2015 against Finland's 3.8% (average growth rates for these countries for 2000–2005), then the real GDP per capita in Estonia would have doubled while Finland's would have grown 1.5 times. At the same time, the difference in the level of nominal wages would rise by 70%. When the differences in wages between the Baltic states and highly developed countries is measured in 5 – 10 times, then a 10% rise in wages does not cause irreversible damage to the international competitiveness of the Baltic states. A relatively low level of average wages (in 2006 the average Estonian wage was only 25% of Germany's) is still (even after the economic crisis) an important factor of international competitiveness, although a high level of unemployment will characterize the Estonian economy for a while (Wiegert 2009).

In the case of low wages, another negative tendency often develops. Low wages negatively influence the labor force's qualifications, especially in technical fields, which are important for innovation-based development. Young people are not motivated to learn sophisticated technical subjects when finding a job in these fields is difficult and the wages are low in Estonia. Therefore, working abroad becomes an attractive opportunity for highly qualified young people.

Labor costs of production largely determine international price competitiveness, especially for less developed countries exporting labor intensive products. This article emphasizes a contradictory aspect of labor costs: while the producer wants to decrease the labor costs as an influential factor of price competition, the employee wants to achieve a rise in real income as the basis of living standards. That means a decrease in unit labor costs (ULC) has to be achieved through raising labor productivity and not through the reduction of real income. The rise in a country's competitiveness is often described through improved trade balance together with a rise in living standards (real income) (Global ... 1985; Hatsopoulos et al. 1988)

It is important to look at employee´s income level in a broader social context. Fagerberg (1988: 355) takes the need to raise the real income of employees and adds the need to guarantee general employment: a country's international competitiveness refers to the ability to implement central economic policy goals, especially achieving growth in real income and general employment levels, without causing problems to the balance of payments. "High wage countries are often concerned about the relatively high level of their labor costs in the production of particular goods and services compared to low wage countries, in particular to the extent that such lower labor costs are the result of lower taxation, smaller social security payments, lower expenses on high-skilled labor for R&D and innovation, and in some cases, lower labor standards" (van Ark et al. 2005: 3). Labor standards are seen as being one of the most important factors for a country's international competitiveness (Flanagan 2003), but these costs are difficult to point out and compare, leading to the frequent discussion of whether the WTO could introduce common standards in order to avoid distortions in the measurement of international competitiveness.

Labor costs integrate the income of employees with the expenditure of producers. Buckley et al (1988: 186) emphasize the paradox that the countries with the fastest growth in exports and in GDP have at the same time experienced much quicker growth in unit labor costs than other countries. That means that in developed countries with advanced economies, price competitiveness depends primarily on introducing qualitatively new (innovative) products and not on ULC. (Buckley et al., 1988: 189).

In the Ricardian two-country two-product international trade model only the labor costs are considered as a factor that determines the comparative advantage of a country. Dornbusch et. al. (1977) developed the n-product model but the labor costs remained the only factor determining the

international/relative competitiveness. The production of a product in one country is internationally competitive if the ratio of the domestic wage rate to the competitors' wage rate is lower in comparison to the ratio of domestic labor productivity to the competitors'.

In reality, the production of goods incorporates many more factors besides labor; therefore, other models have been developed, for example, the model of domestic resources costs and total unit costs (see Siggel 2007). Michael E. Porter (1990: 73) emphasizes that a country's competitiveness determines its prosperity, created through its industry's capacity to innovate and upgrade. He is critical of the prevailing thinking that labor costs, interest rates, exchange rates and economies of scale are the most powerful determinants of competitiveness (Porter 1990: 74). Porter developed what is referred to as the "diamond" of national competitive advantage. He offers a comprehensive new approach for the comparative analysis of competitiveness, comprising four parts: factor conditions, demand conditions, related and supporting industries, and firm strategy, structure and rivalry (Porter 1990: 77). Under factor conditions the first named is skilled labor. So the "diamond" of competitive advantage is directly related to classical approaches, insisting on the importance of labor costs for ensuring international competitiveness. Especially less developed countries have to compensate for disadvantages in other facets of the economic competitiveness "diamond" through lower labor costs. Low ULC are frequently seen as the most important current and future comparative advantage of Central and Eastern European countries (Havlik 1998: 13).

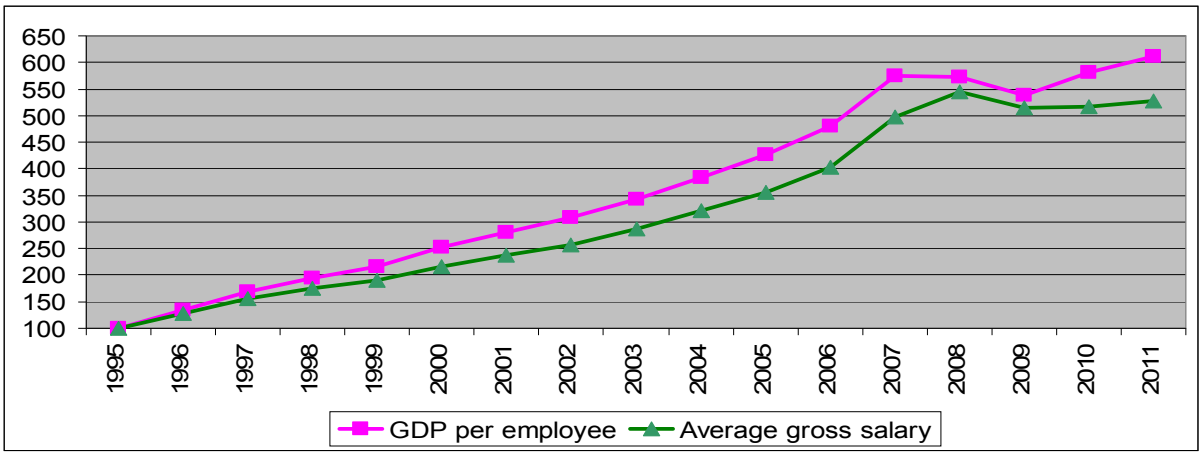
A country can apply different strategies to improve its international competitiveness (van Ark et al. 2005: 3). We have to distinguish short-run and long-run policies. In the short run a country can achieve success in the export sector by decreasing the labor costs per employee (the living standard of the population) but in an open economy this strategy is not effective. In the long run it is necessary to achieve growth in productivity (as the basis for the improvement of living standards), but this strategy can be developed only through a rise in investments.

3. The Development Tendencies of Labor Costs and Productivity in Estonia

From 1995 to 2003 the growth rate of nominal GDP exceeded the growth rate of the sum of gross wages in Estonia. Thereafter, for a couple of years the growth rates of both were equivalent. After Estonia's accession to the EU, the huge inflow of credit money sharply expanded demand for labor. As a result, the average level of gross wages climbed. In 2008, real GDP decreased and increased slightly nominally (only due to inflation). At the same time the growth of gross wages continued and outperformed productivity growth rate. The labor management of firms was not properly adapted. 2010 – 2011 the business sector in Estonia the labor policy growth rate exceeded the growth rate of salaries.

Chart 1 characterizes the development tendencies of the Estonian employees number, GDP per employee and average gross salary from 1995 to 2011. The employees number decreased from 1995 to 2000 11.7% in spite of economic growth, and stabilized on low level until 2004. 2005-2008 the number of employees increased rapidly and overtook in 2008 the level of 1995 2.7%. Deep crises lowered the number of employees 2010 nearly on the level of 2000. The economic growth recovered the labor market and the number of employees reached the level of 2005. The labor productivity (GDP per employee) rose quicker as the average gross salary and in 2007 was the growth rate 5.74 against 4.98. In 2008 the labor productivity stagnated while the average gross salary continued to increase and the proportion of the growth rates was 5.74 against 5.45. After the downturn in 2009 the labor productivity raised relatively quick whereas the increase in the average gross salary was small. Therefore, the difference between growth rates reached in 2011 the record – 6.1 against 5.27. In summary, in Estonia during the period 1995-2011 the labor productivity has risen quicker as the average gross salary of employees.

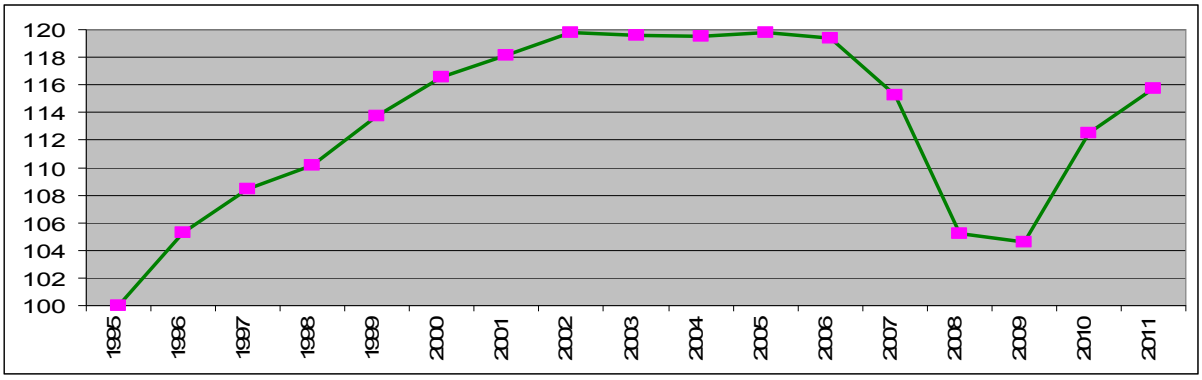
Figure 1: The dynamics of the Estonian GDP per employee and average gross salary from 1995 to 2011 (value of 1995 = 100), in %



Source: Statistics Estonia online database 2012, compiled and drafted by author

Chart 2 illustrates the development tendencies of GDP per gross salary unit in Estonia from 1995 to 2011. Until 2002 the "wage productivity" rose step-by-step and overcame 19.8% the level of 1995. After stabilization period until 2006 the GDP per gross salary unit has 2007-2008 fallen rapidly and stabilized for 2009 on the level less than 5% over the stand of 1995. In last years has been achieved rapid growth of the "wage productivity" and the results of the crises is nearby liquidated.

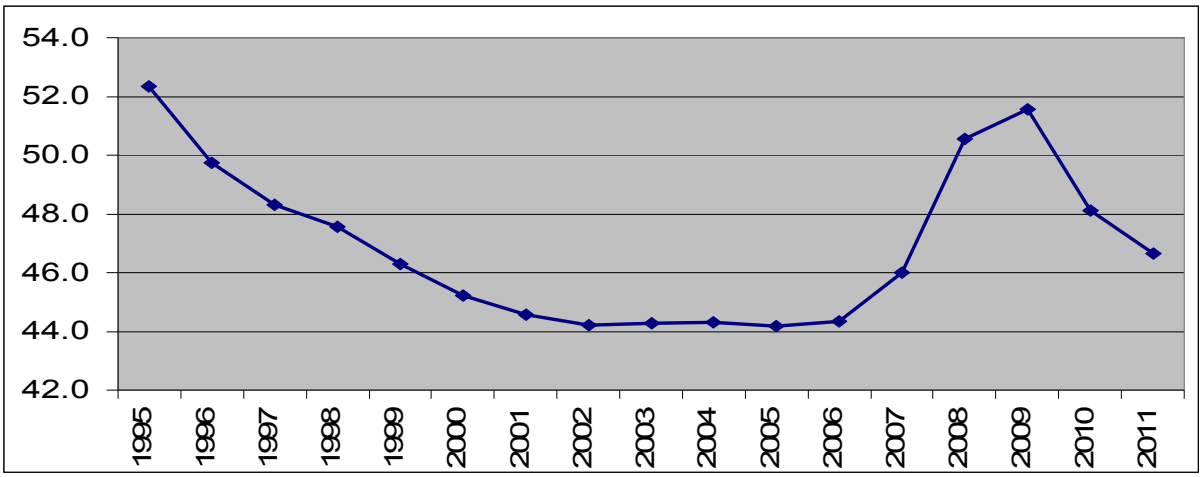
Figure 2: The dynamics of the Estonian GDP per gross salary unit from 1995 to 2011 (value of 1995 = 100), in %



Source: Statistics Estonia online database 2012, compiled and drafted by author

In an environment of high inflation (from 1995 to 2002) the growth of the total employee compensation sum fell behind the growth of the nominal GDP. The total ULC (total sum of labor related expenditure as a ratio to nominal GDP) reduced remarkably (see chart 3): from 52.4% in 1995 to 44.2% in 2002, which is more than 8% in seven years. By 2002 – 2006, total ULC had stabilized. The high demand for labor during the economic boom raised the total ULC to 51.2%, or by more than 7% in two years. In 2009 (amidst the crisis) the ratio rose to 51.6%, meaning the general level of the mid-1990s was once again achieved. In last years has been achieved a remarkable decrease of total ULC to 46.7% in 2011.

Figure 3: The total ULC per GDP unit in Estonia for 1995–2011, in %

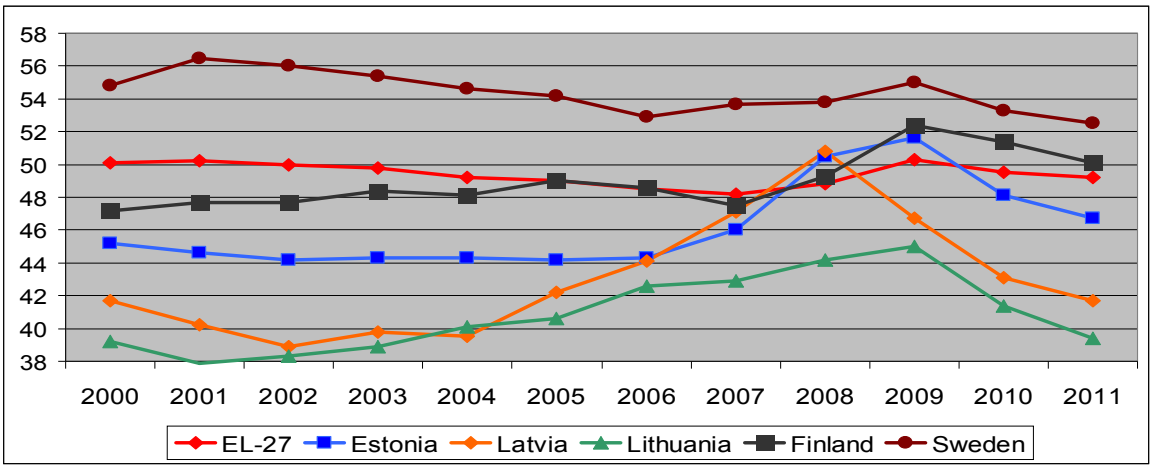


Source: Statistics Estonia online database 2012, compiled and drafted by author

The total ULC of nominal GDP may be considered as an important factor for international competitiveness. Chart 4 shows the total ULC of nominal GDP in Estonia, the EU (average), Latvia, Lithuania, Finland and Sweden. The period examined can be divided into three sub-periods:

- Until 2006, these countries show various tendencies. In the EU on average and in Sweden the total ULC decreased; in Finland and Estonia the total ULC was stable; in Latvia and Lithuania the total ULC rose.
- 2007–2009, the economic boom and the crisis generally raised the total ULC of nominal GDP: in Estonia and in Latvia very sharply (in 2008 the total ULC even exceeded the level of this indicator in Finland), moderately in Finland and Sweden, and relatively modestly in Lithuania.
- After the crisis the total ULC has decreased. One notices that generally the previous proportions across countries will be restored (although in Finland the total ULC has exceeded the EU average). Unusually, only Latvia managed to achieve a turnaround in the total ULC trend earlier than other countries, due to general wage reductions in 2009. Generally, in the EU (based on the average) and other countries the total ULC showed a slight tendency to decrease in last years.

Figure 4: The total ULC of the nominal GDP in Estonia compared to the EU average and neighbouring countries for 2000–2011, in %



Source: Eurostat online database 2012, compiled and drafted by author

The changes in unit labor cost levels during the economic boom and crisis have influenced Estonia's international competitiveness more than that of neighboring countries. In 2006, the ratio of employee compensation costs to GDP in Estonia was 2% down on Finland's and the EU average and 4% down on Sweden. Latvia and Lithuania came closer to the level of the total ULC in Estonia. In 2009, the examined ratio in Estonia was almost equal to the ratio in Finland and 2% higher than the EU average. Although Estonian ratio was 4% lower than Sweden, the ratio in Estonia was 4% higher than in Latvia and 7% higher than in Lithuania. During last years Estonia has restored its competitiveness position on the basis of total ULC to Finland and Sweden, but differences with Latvia and Lithuania have increased slightly. Obviously, Latvia and Lithuania are trying to maintain their reputation for being countries with low labor costs, meaning Estonia will have difficulties with its Baltic neighbors in the fierce competition for lower labor costs. Of course, nominal GDP and nominal labor expenditure are significantly lower than the EU average and especially in Finland and Sweden. According to Eurostat (2012), the GDP in current prices per person in 2011 was €11,900 in Estonia, €41,000 in Sweden and €35,600 in Finland. Therefore, compared to the Nordic countries, Estonia remains a source of cheap labor force and intermediate production. Compared to Latvia and Lithuania, Estonia has to work harder; this means being more productive and supplying higher quality service in order to compensate for its relatively higher wage levels compared to these countries.

Table 1 characterizes the productivity of employees by economic activities as a ratio to average productivity in whole economy.

Table 1: Value added per employee produced in Estonia according to economic activity (NACE-classification) for 1995, 2000, 2005 and 2008-2011, in % of average value added per employee in Estonian economy

	1995	2000	2005	2008	2009	2010	2011
Economic activities total	100	100	100	100	100	100	100
Agriculture, forestry and fishing	73.2	91.8	97.0	108.2	86.0	97.4	108.3
Mining and quarrying	111.9	82.2	91.6	104.7	98.7	104.0	126.3
Manufacturing	76.7	72.2	71.5	70.9	71.1	82.6	84.8
Electricity, gas, steam and air conditioning supply	136.5	118.9	151.9	193.2	252.1	241.9	251.0
Water supply; sewerage, waste management and remediation activities	163.3	118.2	112.9	253.4	232.0	239.3	144.9
Construction	118.8	84.0	113.2	82.1	73.6	70.7	69.5
Wholesale and retail trade; repair of motor vehicles and motorcycles	101.1	99.5	113.4	97.1	87.7	87.2	86.7
Transportation and storage	89.7	114.7	102.1	105.0	94.4	116.1	117.4
Accommodation and food service activities	53.5	43.2	48.4	39.3	37.5	31.0	36.9
Information and communication	254.9	243.5	182.1	193.7	222.0	222.1	175.1
Financial and insurance activities	189.1	262.7	291.8	257.9	187.7	200.5	196.6
Real estate activities	631.4	687.1	599.8	695.5	793.4	686.4	642.1
Professional-, scientific and technical activity	155.3	116.9	182.7	165.8	177.6	173.9	155.8
Administrative and support service activities	105.1	81.6	113.5	146.6	138.0	105.6	129.6
Public administration and defense; compulsory social security	95.4	90.4	80.9	100.5	116.7	95.0	94.9
Education	65.7	58.0	46.6	48.7	48.6	48.4	47.0
Human health and social work activities	57.9	58.0	52.8	70.4	70.2	59.2	59.8
Arts, entertainment and recreation	44.7	60.6	69.3	74.5	69.2	60.9	64.6
Other service activities	126.0	72.0	53.9	46.1	65.4	54.0	64.8

Source: Statistics Estonia online database 2012, compiled by author.

On the background of the general relatively quick increase of the average productivity per employee in Estonia (see Figure 1), the development of the productivity in different economic sectors shows quite various patterns:

- Value added per employee overcomes in real estate sector 6-8 times the average productivity in Estonian economy. From the lowest level in 2005 (599.8%) the economic boon has brought the relative productivity to highest level in 2009 (793.4%) and the economic crisis has caused the fall nearly back to the level of 1995 (642.1%).
- As monopolistic firms dominated the electricity, and gas etc. sector, its relative productivity level (from 136.5% in 1995 to 251% in 2011) has nearly doubled, mostly by increasing the product prices.
- The relative productivity in agriculture, forestry and fishing sector has considerable increased – from 73.2% in 1995 to 108.2% un 2008, and restored this level after the decrease during the crisis period.
- The manufacturing sector has lost about 10% of its relative productivity during the economic growth and boom period 1995-2008. It increased this level of relative productivity by about 20% in last three years, but stays in 2011 about 15% under the average productivity level.
- The lowest and decreasing relative productivity shows the accommodation and food service sector;
- Interestingly the information and communication sector has lost considerably its relative productivity level– from 254.9 in 1995 to 175.1% in 2011.
- The deepest fall of relative productivity level characterizes the construction sector – from 118.8% in 1995 to 69.5 in 2011.

Table 2 presents the value added per gross salary unit by economic activities as a ratio to average productivity in the whole economy. This table points out similarities, but also differences in position and development tendencies of economic sectors, compared to regularities demonstrated in Table 1:

Table 2: Value added per gross salary unit produced in Estonia according to economic activity (NACE-classification) for 1995, 2000, 2005 and 2008-2011, in % of average value added per gross salary unit in whole economy

	1995	2000	2005	2008	2009	2010	2011
Economic activities total	100	100	100	100	100	100	100
Agriculture, forestry and fishing	125.9	154.6	139.1	132.7	126.8	137.2	147.6
Mining and quarrying	81.4	70.4	92.9	108.2	110.8	112.3	110.6
Manufacturing	93.4	84.7	82.4	86.3	85.5	92.5	97.3
Electricity, gas, steam and air conditioning supply	90.1	109.7	186.4	192.9	226.6	245.3	234.0
Water supply; sewerage, waste management and remediation activities	102.6	112.4	125.1	136.0	146.7	148.2	144.8
Construction	95.1	106.2	103.5	90.9	81.6	78.3	85.3
Wholesale and retail trade; repair of motor vehicles and motorcycles	108.4	92.2	105.4	94.5	85.9	87.3	89.0
Transportation and storage	75.4	108.7	100.2	108.6	108.7	118.2	121.2
Accommodation and food service activities	81.5	86.1	79.5	64.8	59.7	53.5	56.1
Information and communication	148.5	129.2	122.1	115.3	111.4	95.5	91.9
Financial and insurance activities	88.0	125.9	120.5	142.1	115.3	113.7	113.7
Real estate activities	775.3	687.0	618.1	629.8	661.2	657.4	541.3
Professional-, scientific and technical activity	89.5	85.6	92.6	85.6	90.9	93.3	90.6
Administrative and support service activities	89.7	66.6	86.6	94.2	94.8	85.8	80.2
Public administration and defense; compulsory social security	66.2	65.3	64.0	74.2	85.3	81.3	78.1
Education	71.9	58.0	56.4	62.7	65.7	61.2	60.1
Human health and social work activities	67.0	57.7	59.3	66.2	68.1	62.4	61.6
Arts, entertainment and recreation	63.3	75.2	90.0	87.2	82.6	80.9	80.8

Source: Statistics Estonia online database 2012, compiled by author.

- The relative level of value added per gross salary unit is the highest in the Estonian economy, but has decreasing tendency – from 775.3% in 1995 to 541% in 2011.
- In electricity, gas etc. sector is the relative gross salary productivity lower than the relative employee productivity, but shows about the same growth rate.
- The relative gross salary productivity in agriculture, forestry and fishing sector is considerable higher than the relative employee productivity, but the difference is decreasing.
- In the manufacturing sector the relative gross salary productivity is modestly higher than the relative employee productivity and exhibits about the same development pattern.
- The relative gross salary productivity in accommodation and food service sector is higher than the relative employee productivity, but the difference is decreasing.
- One observes that the relative gross salary productivity has in construction sector the tendency to decrease, but much more modest than the relative employee productivity.

In direct international competition exporting firms of manufacturing, agriculture and fishing, transportation and communication sectors have to prove their competition capability. For attracting tourist the competing country should offer competitive services in accommodation and food services and transportation and communication sectors. After opening the market to direct international competition the electricity, gas etc. sector has to stand competition. Other sectors will influence the business environment, supporting or decreasing the competitiveness of exporting firms. So, the level and development tendencies of productivity are important for assuring the international economic competitiveness of a country. In Estonia the developments in labor costs and productivity are quite different and contradictory.

4. Summary

The Nordic countries in Baltic Sea region see Estonia only as an intermediate producer with cheap, but relatively high-skilled labor. EU accession did not stabilize Estonia's economic development. On the contrary, it initiated various destabilizing processes. The economic crisis resulted in a finance account deficit of balance of payment. The processes that at first supported Estonia's economic development have now reversed and will lead to serious hindrances. The deepness of the crisis highlighted and proved the non-sustainability of the chosen economic development strategy.

The remarkable backwardness of salaries compared to the general positive economic growth was concealed during the ten year period due to the relatively high inflation rate. As a result the share of business sector in GDP increased strongly. The massive inflow of foreign credit induced growth in labor force demand. The wage level increase at the start of the crisis re-established the 1995 proportions of GDP share between the business sector, households and public sector. But the business sector succeeded in re-establishing the advantageous position in GDP share it experienced at the start of the new millennium. Fifteen years have changed the economic structure of Estonia, this is designed to serve the interests of large multinationals and their policy of outsourcing cheap intermediate production to the Baltic states.

During the same period, the level of real income in Estonia has doubled. The low wage competition from Latvia and Lithuania has risen significantly. But there is a strong believe of Estonian policy makers. They presume that economic success can be achieved after the crisis by applying the same economic development policy and strategy. During last two years, in Estonia is achieved the turnaround in development of total ULC as well as gross and net salary unit costs. The structure of Estonian economic activities has achieved a development in direction to the pre-boom situation.

Different sectors of economic activities in Estonia have different positions in international competitiveness due to different level and development tendencies of labor costs and productivity in

terms of the relative employee and gross salary productivity to average productivity in whole economy.

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Public Debt Acceptability Evaluation in the Changing Economy

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Abstract

During the last decades many countries of the world faced rather strong tendency of the public debt increase. The level of a certain country's public debt is mostly determined by the general economic situation of the country and its perspectives. Trying to achieve more effective and faster economic development, the government usually borrows. The academic society discusses the role of the public debt in economics: how the borrowed funds should be used; how much can a government borrow? It is important to determine the place and role of the public debt in the countries economy and evaluate how borrowing effects the growth of the economy. The aim of this article is to determine the limits of the national debt acceptability, knowing the economic indicators. It is important to learn what level of the fiscal deficit is acceptable to the different states and how it could be managed under certain economic conditions.

Keywords

Public debt, public debt acceptability, economic indicators, relative indicators, debt management, government policy and regulation

1. Introduction

In today's situation public borrowing is inevitable, so its impact's analysis is very significant. Public debt is defined as the outstanding amount of the annual national budgets deficits. It shows country's debt, both, in domestic and foreign markets. Public debt acceptability is measured in accordance with formal fixed criteria. The closer public debt indexes are to the borrowing limits critical line, the higher risk comes to the country's economic situation. Public lending issues are widely analyzed in scientific literature, but there is no unanimous opinion what borrowing rate is tolerated. Most scientists say that in the growing economy, borrowing has a positive effect on economic development; controversy arises when it comes to the evaluation of effective use of borrowed funds. A number of general, economic and relative indexes are supplied which show country's current situation, trends and allow to make comparisons with other countries' borrowing situation. Naturally, the question arises to what extent country may borrow that debt burden wouldn't shade economic expansion. The main country debt acceptability evaluation criteria is indicated in the Maastricht Treaty, signed on February 7th in 1992, which states that country's borrowing rate cannot exceed 60 percent from GDP and budget deficit wouldn't exceed and approach to 3 percent from GDP. Twenty years passed from that contract signing during which countries joining the euro zone violated the treaty more than 60 times. Since violations of the Maastricht criteria were sufficiently large, stronger penalties were prevented as too large budget deficit may occur not only for the subjective, but for the objective reasons too. Aim of the Maastricht Treaty was to ensure euro zone members' sustainable growth, create criteria that would ensure price stability and exchange rates for the countries joining the euro zone, to keep low budget deficits and debt as well as the ability to maintain confidence in the financial markets. Some additional critical indicators for potential debt were defined by the International Monetary Fund and the World Bank. Public debt is treated as unacceptable if debt and export proportion exceeds 300 percent, as well as debt administrative costs and export proportion – 35 percent.

The paper conducted theoretical and empirical analysis of public debt which will help to respond to problematic issues – how public debt trends are formed in the world, what debt level is tolerated in the EU countries today and what main economic challenges countries are facing whose debt level exceeded the allowable lending criteria. Today there are cases when critical borrowing indicators are exceeded. Therefore timely and regular public debt analysis of absolute and relative indicators is necessary to reveal the impact to country's economic situation, assessing the formed situation and identifying underlying problems. The remaining risk is that public debt can become an unbearable burden for national budget and national economic development. By changing economic conditions new public debt management paradigm is being formed, allowing forming favorable borrowing conditions for the country, even exceeding the critical debt management indicators.

The research object – absolute and relative indicators of the public debt.

The article aim – to reveal national debt acceptability evaluation indicators, reaching to determine public debt level trends and emerging problems due to approach (or overrun) to the critical borrowing rates.

The aim is pursued by realization of set targets:

1. To reveal public debt acceptability evaluation indicators.
2. To perform different countries' public debt indicators 2003-2011 year's analysis, revealing formation trends of the borrowing.
3. To identify the main public debt problems as a result of critical approach to lending rates.

Research methods: scientific literature analysis, statistical classification, organization and analysis, statistical – mathematical methods and comparative analysis, graphical representation of results.

2. Public Debt Acceptability Evaluation Indicators

Recently, in many countries around the world, due to economic fluctuations, there is a spurring growth in public debt, which is becoming a serious problem. In economic downturn these problems become particularly bright and unavoidable. Growth of public spending influence the increase of budget deficit which has to be financed from borrowed resources. Country's borrowing is considered as a tool of socio – economic policy (Karazijienė, 2011). Economic theory states that government borrowing can lead to economic growth, but there is always risk how to maintain an optimal level of public debt, without burdening the budget and economic development. Public debt acceptability evaluation questions, in many different aspects, are analyzed by many Lithuanian (Janulytė 2011; Drakšaite 2011; Kurtinaityte and others 2011; Karazijienė 2009, 2011; Šimelytė 2010; Karazijienė, Sabonienė, 2009; Čiburienė, Povilaitis 2005; Levišauskaitė 2003, Budryte 2002) and foreign (Alesina, 2012; Egert, 2011; Cashell 2010; Nosbusch, 2008; Missale, Giavazzi, Benigno, 2002; Barro, 1999;) scientists in their performed studies. Along with increased public debt, its servicing costs are, also, rising. This factor stops economic growth and determines a lower standard of living for future generations (Janulytė, 2011). We agree with the authors (Karazijienė, 2011; Kurtinaitytė and others 2011) opinion that domestic borrowing is much more favorable, as the monetary resources remain within the country, which experiences fewer losses due to exchange rate differences. But such borrowing influences financial markets – it increases the interest rate and limits investment. However, often there are cases that domestic market feels the shortage of surplus resources; consequently it is necessary to borrow from foreign markets, thereby transferring the burden of debt for future generations.

Table 1: Public debt acceptability evaluation indicators

General indicators	Economic state indicators	Relative indicators
Public debt (domestic and foreign); Interest for public debt; Public debt per citizen.	GDP (gross domestic product); State budget expenditure; State export amount.	Public debt and GDP proportion; Interest for public debt and budget expenditure proportion ; Interest for public debt and GDP proportion; Foreign debt and public export proportion; Foreign debt and GDP proportion;

Source: Levisauskaitė, Ruskys 2003.

Scientific articles distinguish major economic indicators allowing revealing not only economic country's position, but political situation too. Authors focus on different indicators of public debt and their impact on country's situation. Mostly researches distinguish three types of public debt indicators: general, state economy and relative indicators (1 table). After the scientific analysis, it is possible to imply that there is no single, universal indicator describing public debt acceptability. For analysis it is purposeful to use absolute and relative indicators, which complement each other and extend the analyzed view.

3. Theoretical Approach to Public Debt in the Changing Economy

In today's economic environment major market factors are regulated by the market itself, although the role of state remains enormous. But the regulatory actions every time become more complex and have a direct dependence on already formed environment conditions. Before deciding on one or other regulatory measure, its likely impact and interventions must be evaluated and examined in detail. Large government borrowing is associated with certain risks that must be avoided or, at least, reduced. Janulytė (2011) excluded situations having a negative high debt impact on the economic

growth. Firstly, too large debt, over higher interest rate, negatively affects capital accumulation and growth, causing investment decline in private sector, but increasing taxes and inflation rate. Secondly, too large public debt may constrain fiscal policy trends by applying too strict cost reduction requirements. This author has, also, analyzed positive aspects of government borrowing, but only if the borrowing does not exceed its critical indicators and borrowed funds is used in areas that give a return on investment in the future. The most effective investment, according to Janulytė (2011) is available in human and physical capital: education, communication, and health care, transport and so on. Navickas and Štuopytė (2000) deduced that public debt affects country's monetary policy. Country loses its charges irreversibly (interest for debt servicing), there are changes in political decisions related with the country's fiscal policy, credit rating image is formed on the international market, and there is a threat of political dependence or a decline of influence in international positions. A carried out scientific analysis clearly shows that state can borrow only up to certain limits, because in a certain moment public debt can become uncontrolled phenomenon causing problems for entire country's economy and society. Therefore, it is essential that each state would form a clear strategic financial management model, which must be rational, purposeful, and appropriate for changing economic conditions and providing confidence for the society (Rėklaitis, 2009). We can agree with Kurtinaitytė and others (2011) approach that debt management effectiveness depends not on the strategy itself, but on its creators as well. It is important that these individuals not only share theoretical knowledge, but also have enough practice in the field, then strategies' quality is improving, but, the most importantly, decision reasonableness is increasing. Therefore, country's financial management should be conducted not only at the highest management level, as more responsibility on resource redistribution should be given for local governments' i.e. to pursue certain level's fiscal decentralization. Thus, state borrowing requirement would acquire more real reasoning and transparency.

Successfully functioning financial sector in each country is a condition for economic growth. But how, through what financial segments economic processes and their results are affected? What factors determine the impact? These are debatable questions, as each country's economy and financial system have specific characteristics for development (Karazijienė, Sabonienė, 2009). Such state's, which cannot form its own surplus budget, debt will increase every year, as well as debt servicing costs, so more and more taxpayers' money will have to be used for debt management. In this case, it's advisable, regularly, to analyze state budget's balance and formation of borrowing requirements, in different analysis periods and aspects. There is a real fiscal and financial crisis risk not managing to cope with budget deficit. Economists are tend to link public debt increase with declined possibilities to finance private investments from the borrowed funds, which leads to slower economic growth and a lower standard of living for future generations (Rėklaitis, 2009).

Noted critical public debt management level indicators generally emphasize the maximum debt limit, which is not a sufficient background to imply that public debt burden will be acceptable without exceeding an estimated limit. Each state has to create its own "government debt philosophy", taking into account real national economic and political situation. It is useful to borrow in economic upturn due to GDP growth as debt burden does not increase. You can see this from the relative debt indicator to GDP. But at the same time debt maintenance raises, which is covered by tax revenues and may negatively affect budget in the future periods. It's clear that debt will have to be returned some day. One source of public debt repayment is cuts on public spending, but it is unlikely that these means would be applied voluntarily by politicians who want to please the voters. The most real measures are tax increase or refinancing of debt. Barro (1999) presents economic theories corresponding, practical debt transfer to taxes situation.

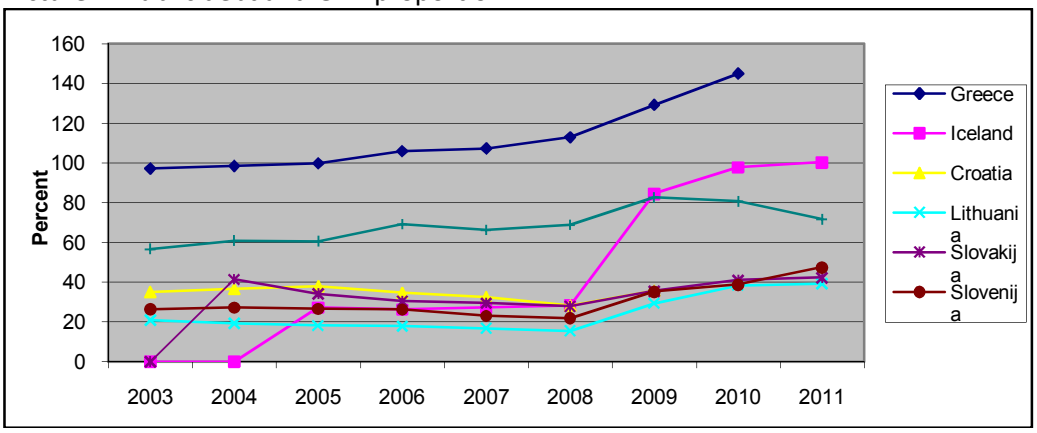
From an empirical and policy standpoint, the tax – smoothing approach generates two key implications. First, the government should run budget deficits at times of temporarily high public outlays. The classic situation is wartime deficit finance, as practiced, for example, by Britain from the

late 1600s through World War I. The high levels of spending during wars are paid mostly by borrowing, rather then current taxation. Then the future financing of the accumulated debt implies correspondingly higher taxes during the later peacetime periods. Thus, taxes are raised by roughly the same amount during and after war. Correspondingly, the government should run surpluses in peacetime. A similar situation arises for natural disasters, such as the recent hurricane in Central America, when public spending for infrastructure investment is temporarily high. These outlays should be financed mostly by public borrowing, unless a country can get some foreigners –such as United States or the World Bank – to pay for the emergency expenditures through foreign aid (Barro, 1999). The governmental borrowing does not cause damage to the economy if only the opportunities provided by debt are used in an optimal way.

4. Practical Public Debt Acceptability Evaluation in Different Countries

In today's global economic environment, all countries borrow and thus regulate their economies. Borrowing degree is different, just as borrowing needs are formed otherwise. Many countries of the world, long ago, surpassed the Maastricht criteria, however analysis of economic statistical data show the country's true economic situation. Seeking to show more real situation of borrowing countries, taking into account the generated product, received expenses, paid interest and export volumes – relative indicators are calculated. The analysis period is from 2002 to 2011. Primary analysis data is used from the Euro stat database. Seven different countries are analyzed: Greece, Iceland, Croatia, Lithuania, Slovakia, Slovenia and Hungary. For more detailed comparison of data in the scientific literature, it is recommended to use relative indicators. One of the most important indicators, which is indicated by the Maastricht Treaty, is a part of the public debt from country's GDP (see picture 1).

Picture 1: Public debt and GDP proportion

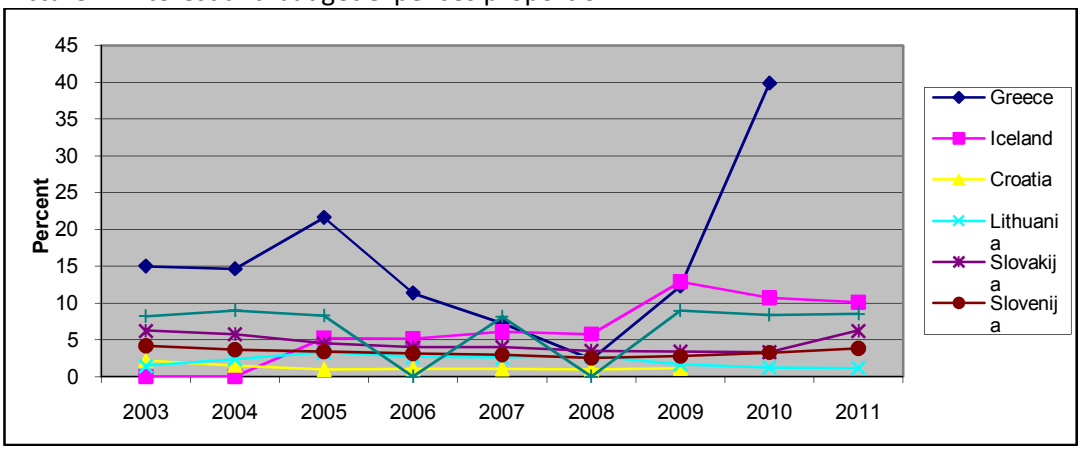


Iceland is not the euro zone country so this criterion does not concern it. Data about public debt is given from the year 2005 and was 27 percent from GDP. In 2011 the country's public debt level is the same as the size of the GDP, which means that borrowing is at the same extent as production, selling of goods and services over the year. Mostly this country borrowed in 2008-2009 as at that time country experienced banking sector crisis, which negatively caused country's economy. Meanwhile, Greece's, which is famous for borrowing and debt refinancing, amount of debt, since 2003, has been steadily increasing (it was 97 percent from GDP), while the biggest growth was seen in 2009-2010. In 2010 country's debt rose up to 145 percent GDP. This means that Greece borrows more than produces annual product. Hungarian government debt, in the analysis period, was in a critical area. At the beginning of analysis, public debt was 56 percent GDP, while at the end it had reached 72 percent GDP. Like all countries, Hungary increased its debt in 2009, but later this tendency decreased. Although it still exceeds the acceptable criteria.

Lithuania, Slovakia, Slovenia and Croatia have the least debt. These countries still have the potential to borrow, because they have never reached the critical limit of 60 percent. We can imply that according to public debt and GDP proportion, these countries' debt is acceptable.

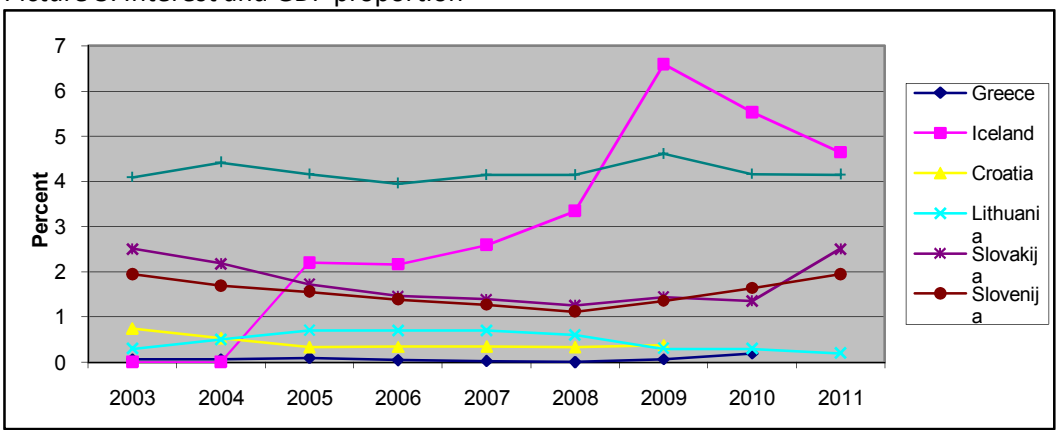
Each credit debt has its own cost, which consists of debt management and interest payments. However, countries' borrowing rates are different, so paid interest rates are different too. Next relative indicator showing how much, the country its budget expenses gives for public debt management is – public debt interest and budget cost percentage proportion (see picture 2).

Picture 2: Interest and budget expenses proportion



Economic theory suggests that the more debt country has the more interest it pays to its creditors. However, practice shows that it's not always true. Greece gets the maximum interest costs, as its debt is significantly higher than the other analyzed countries'. While Iceland and Hungary's public debt is also very high, their paid interest from budget is significantly smaller and tends to decline. This means that their borrowing costs are significantly lower than Greece. It shows Greece state level of credibility and low credit ratings. The lowest debt serving costs, which are not even two percent of the budget expenses, are in Lithuania and Croatia. Hungary's borrowing costs are 8 percent, and Iceland's – 10 percent of the state budget.

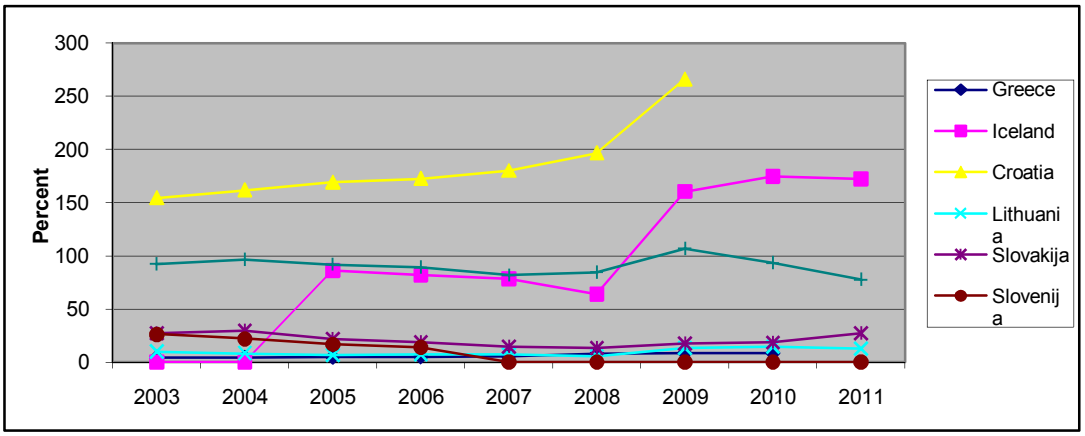
Picture 3: Interest and GDP proportion



A slightly different situation is seen among public debt interest and GDP proportion (see picture 3). From received GDP (in 2011) Iceland and Hungary paid the most interest. The least – Greece and Lithuania, which allows us to state that the cost of debt in these countries is covered by borrowed funds, not on the basis of population created product.

National and export proportion shows how much countries are able to cover public debts at the expense of exported production and how much of the borrowed fund is invested in the country's economy (see picture 4). In most cases countries borrow not for investment, but to cover running costs or to refinance older debts. From the given diagram you can see that Slovenia (0, 11 percent in 2011), Greece (8, 37 percent in 2010), Lithuania (12, 8 percent in 2011) and Slovakia (27, 3 percent in 2011) are not high extent export ountries. This means that borrowed funds will have to be returned with the help of new higher taxes. Although Slovenian and Lithuanian public debt in percentage of GDP are similar, but exports and public debt proportion differs significantly. We can assume that Slovenia invests more in its economy than Lithuania, therefore more rational use of borrowed funds is possible.

Picture 4: Public debt and export proportion



Iceland's government debt and export proportion (172 percent in 2011) shows that the country is much investing in the country's economy and export scopes show country's ability to return the debt. This explains country's lower borrowing costs. Meanwhile, Croatian public debt and export proportion (266, 35 percent in 2009) shows country's ability to manage borrowed funds effectively, to increase its investments and stimulate economic development.

The main factor leading countries to increased credit obligations is economic recession that began in 2008. There was a need to stabilize economic situation which required additional financial resources. However, the size of public debt and its management evolved differently. In many cases this was determined by government fiscal decisions to stabilize the economic situation in the country. Applied different measures brought different results, which will be felt in the future.

5. Findings

1. The main indicators supposing public debt acceptability are measured in absolute and relative proportions. Relative indicators more effectively reveals country's debt situation as they show state or foreign debt's ratio between generated product, debt servicing costs in the state budget and export volume in the economy. Country's borrowing needs are changing in different economic situation, but credit resources used for investments allow us to expect greater stability in commitments.
2. Presented analysis of economically different countries public debt revealed situation that there are countries that do not comply with the Maastricht Treaty's borrowing limit. Even though their debt exceeds critical indicators, their debt servicing costs are very different. It mostly depends on the country's economic situation and on effective usage of borrowed funds in the economy. Countries, which are investing their borrowed funds in high technologies, have a lower debt

burden, although their debt levels are high. However, there are countries whose public debt burden will be carried forward for tax payers, as country is borrowing more to refund state budget deficit which was caused by rising operating costs or is borrowed for debt refinancing. Countries, even if they have a relatively low public debt, which is presented euro zone countries' signed Maastricht Treaty, occurring debt refunding problems will be postponed for the future, thus transporting the burden on future generations.

3. Carried out public debt relative indicators analysis showed that the most problems because of increased need to borrow will have such countries as Greece, Lithuania and Slovakia. Iceland and Hungary borrows significantly more than allow critical borrowing rates, but most of the borrowed funds they invest into country's economy, so borrowing situation remains stable and debt refunding – manageable. Countries, forming financial management strategy, more flexibly adapt to the changing situation of public debt management. Therefore, there remains important human factor that can take competent management decisions, from which significantly depends and country's economic stability.

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The Relevance of Institutional Environment in Explaining Economic Growth Variation Across Countries in the Short Run

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Abstract

Many economists argue that definite institutional environment is the key precondition of economic development. A series of studies explored the positive link between institutional environment and economic performance. The institutional environment in these studies is measured through various indicators: Gastil's index of political rights and civil liberties, Economic Freedom of the World index, constructed by Fraser Institute, the Index of Economic Freedom, constructed by *The Wall Street Journal* and The Heritage Foundation, governance indicators, presented by the World Bank, and etc. While the measures of "institutions" vary across studies, the results are consistent: weak institutions (rule of law, bureaucratic quality, corruption, civil liberties and etc.) inhibit economic development while strong ones lead to prosperity. The empirical support for this statement is usually based on data in the long run. Due to globalization the recent global financial crisis had affected the entire world economy, with higher detriment in some countries than in others. This paper aims to analyze weather different consequences of recent economic crisis in the World countries can be explained by the quality of institutional environment in these countries.

The results confirm that quality of institutions is important determinant of economic development, but no evidence was found that it helps to respond to economic shocks and mitigate GDP's decline. Even contrary, negative relationship was observed that the better the institutional environment, the greater the decline in GDP per capita.

Keywords

Institutional environment, governance indicators, economic development, economic crisis

1. Introduction

Many economists argue that definite institutional environment is the key precondition of economic development. The series of studies by North (1990), Knack and Keefer (1995), Barro (1996), Knack (1996), Keefer and Knack (1997), Hall and Jones (1999), Acemoglu et al. (2001, 2003), Eicher et al. (2006), Eicher and Leukert (2009), Fabro and Aixala (2009) and more recent studies by Efendic, Pugh, and Adnett (2011), Stoever (2012) and many others explored the positive link between institutional environment and economic growth and development. Despite this we can find researches that doubt the effect of institutions on economic performance (Commander and Nikoloski, 2011; Vieira and Damasceno, 2011). The institutions in the studies are measured through various indicators: Gastil's index of political rights and civil liberties, Economic Freedom of the World index, constructed by Fraser Institute, the Index of Economic Freedom, constructed by *The Wall Street Journal* and The Heritage Foundation, governance indicators, presented by the World Bank, the subjective political risk ratings, compiled by various organizations, namely Business International, the International Country Risk Guide, and Business Environmental Risk Intelligence. While the measures of "institutions" vary across studies, the results are consistent: institutions help to explain the variation in per capita incomes across countries. There is a broad agreement in the literature that weak institutions (rule of law, bureaucratic quality, corruption, government repudiation of contracts, civil liberties and etc.) inhibit economic development while strong ones lead to prosperity.

Institutions are now widely believed to be important in explaining long-run economic performance, but only few attempts have been made to investigate whether countries with strong institutions performed better than countries with weak ones during recent economic crisis. According to Giannone, Lenza and Reichlin (2011) good governance should make countries more resilient to large shocks and therefore mitigate output losses associated with recessions. This assumption didn't prove out, as authors found that the set of policies that favor liberalization in credit markets (regulatory quality) had affected negatively countries' resilience to the recent recession as measured by the decline in output growth between 2009 and 2008. Johnson (2011) revealed that banks in less regulated countries performed better than banks in highly regulated countries during the market crisis of 2007–2009.

This paper aims to analyze weather different consequences of recent economic crisis in the world countries can be explained by the quality of institutional environment in these countries.

The countries' economic performance refers to 2007-2010 rate of change of GDP based on purchasing power parity (PPP). The measures of institutional environment are governance indicators, presented by the World Bank.

The paper is organized as follows. The next section deals with the definitional aspects of institutions and presents analytical and empirical findings on the relationship between institutions and economic performance. The second section introduces the data and methodology the analysis is based on. The third section presents the empirical analysis and discusses the results. The article ends with conclusions.

2. Institutions and Its Relationship With Economic Performance

According to Portes (2006), the interest to institutions in economic community has been particularly influenced by Nobel laureate in economics Douglass North. After North's declaration that "institutions matter," other analysts started to take them into account.

According to North (1990), "institutions are the humanly devised constraints that structure human interaction". They are made up of formal constraints (laws, constitutions) and informal constraints (taboos, customs, and traditions). Rodrik (2000) defines institutions as "a set of humanly devised behavioral rules that govern and shape the interactions of human beings, in part by helping them to form expectations of what other people will do." The term "institution" is often used as a synonym of "organization". Burki and Perry (1998) explain the difference, organizations are entities composed of people who act collectively in

pursuit of shared objectives and that actions are shaped by institutional structure defined by formal and informal rules and their enforcement mechanisms.

A series of studies support the positive link between various measures of institutions and economic growth: Knack and Keefer (1995), Barro (1996), Knack (1996), Keefer and Knack (1997), Acemoglu et al. (2001, 2003), Henisz (2000), Fabro and Aixala (2009) and development: North (1990), Hall and Jones (1999), Cavalcanti and Novo (2005), Eicher et al. (2006), Eicher and Leukert (2009), Efendic, Pugh, and Adnett (2011), Stoever (2012) and many others.

The impact of institutions on economic performance is indirect, as institutions don't produce goods or services. The main idea how institutions effect economic growth and development is that appropriate set of institutions define the incentives for individuals and organizations to invest in both physical and human capital, which are the proximate determinants of economic growth. Hall and Jones (1999) claim, that the differences in capital accumulation, productivity, and therefore output per worker are driven by differences in institutions. Eicher et al. (2006) results show that the largest impact of institutions is through its effect on the physical capital productivity. Cavalcanti and Novo (2005) revealed that 1% improvement in institutions (as they measure them) generates on average a 5 % increase in output per worker.

According to institutional approach, well defined institutions lower uncertainty, reduce transaction costs, reduce macroeconomic volatility and thus foster investments and innovation. Knack (2002) argues that there is greater technological progress and innovation in countries where institutions related to property rights are in place (in Bloch and Tang, 2004). A study by Tang et al. (2003) confirms that better institutional quality accelerates technical change, which enhances economic growth. Knack and Keefer (1995) find cross country econometric evidence to support the positive link between measures of institutional environment (particularly measures of property rights) and investments. The World Bank report 1997 presents the similar conclusion that investment and growth rate are higher in countries with stable government, clear and predictable law, protected property rights and reliable judiciary. Gwartney et al. (2004) reach the conclusion that the quality of a country's institutions exerts a strong impact on the rate of investment. Not only investment itself but also their impact on economic growth depends on institutional environment. Hall, Sobel and Crowley (2010) find that increases in physical and human capital lead to output growth only in countries with good institutions.

The researches on the impact of institutions on economic performance highlight the importance of the economic, politic and legal institutions. Lee (2010) undertakes a brief survey of three important strands of research on institutions and growth that have emerged in recent years, namely law and finance, new comparative economics, and politics and institutions. The author summarized that the main idea of the "Law and Finance Theory" is that international differences in financial development can be explained by differences in legal institutions. While examining the role of institutions in economic growth the „New comparative economics" focuses on legal environment and financial markets. The literature on "Politics and institutions" focuses on the importance of political institutions on long-run economic growth, investment and financial development.

In the literature the relationship between institutions and economic is clarified by using various indicators of institutions in various time span and different countries. Due to this reason the results are hardly comparable.

3. Data and Methodology

The measures of economic performance and institutions are taken from the World Bank databases. The countries' economic performance is measured by GDP per capita based on purchasing power parity (PPP). Data are in current international dollars [31]. The countries' resilience to the recent recession is measured by the percentage change in GDP per capita from 2007 to 2010. The countries that had negative annual

growth rates of GDP per capita during 2007s were omitted from the sample, because GDP decline in these countries had started before recent economic crisis.

As the measures of institutional environment governance indicators are used. Indicators are based on several hundred individual variables measuring perceptions of governance, drawn from 31 separate data sources. All scores lie between -2.5 and 2.5, with higher scores corresponding to better outcomes. For more detailed methodology used to construct the indicators see Kaufmann et al. (2010). The governance indicators measure the following six institutional dimensions of governance:

- *Voice and accountability*: the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, association and free media.
- *Political stability and absence of violence* refers to the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means.
- *Government effectiveness* captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.
- *Regulatory quality:* the ability of the government to formulate and implement policies and regulations which permit and promote private sector development.
- *Rule of law*: the extent to which agents have confidence in and abide by the rules of society, the police, and the courts, as well as the likelihood of crime and violence.
- *Control of corruption*: the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

In this paper, following Fabro and Aixala (2009), I defined an aggregate institutional quality index (AIQI) equal to the average of the six individual governance indicators for the years 2007-2010.

The empirical assessment of the relationship between economic performance and governance indicators is estimated using correlation analysis. I had carried out an analysis that divided the total sample into two sub-samples according to countries' AIQI: countries where AIQI was positive (64 countries) and where it was negative one (89 countries). These sub-samples were relatively named good and bad institutional environment samples respectively.

4. The Variation in Per Capita Income in Relation With Institutional Environment

Table 1 presents the data on GDP per capita change during 2007–2010 in three samples: (1) all countries; (2) countries where AIQI 2007–2010 average value was positive; (3) countries where AIQI 2007–2010 average value was negative.

Table 1: GDP per capita percentage change comparing 2010 to 2007

	N	Mean	Min	Max	Percentiles		
					25	50	75
All countries	153	5.1	-20.1	31.7	-1.3	4.2	11.2
Good institutional environment (GIE)	64	0.02	-20.4	23.4	-5.1	-0.7	4.3
Bad institutional environment (BIE)	89	8.8	-0.8	31.7	3.1	8.2	13.8

As we can see from Table 1, across 153 analyzed countries the GDP per capita change during 2007–2010 varied from -20.4 percent in Latvia to 31.7 percent in Myanmar. The GDP per capita from 2007 to 2010 on the average increased 5.1 percent. Surprising, that countries with bad institutional environment on the average performed better than those with good one. GDP per capita declined in more than 50 percent of countries in GIE sample and only in 1.1 percent of countries in BIE sample! GDP per capita on the average

increased 0.02 percent and 8.8 percent in countries with good and bad institutional environments respectively comparing 2010 to 2007. Giannone, Lenza and Reichlin (2011) suggest that good governance should make countries more resilient to large shocks and therefore mitigate output losses associated with recessions, but results of this research don't support this assumption. The explanation could be that institutional factors provide constrains which may inhibit policy makers efforts to respond to external shocks and quickly correct policy mistakes (Henisz, 2000). Another possible explanation can be drawn from O'Hara's (2012) conclusion that economic crisis had greatest impact on countries which were implementing major financial innovations and were open to international capital, what is typical for countries with good institutional environment.

It is well documented in the literature that GDP per capita differences across countries can be explained by the quality of institutions. Gwartney et al. (2004) conclude that institutions variable alone explains 63.2 percent variation in income across countries. The results of my previous research (Jankauskas and Seputiene, 2009) reveal that extent to which the variation in GDP per capita can be associated with the quality of institutional environment differs a lot between good and bad institutional environment samples. The results in good institutional environment sample come in line with series of studies in which strong and positive link between various measures of institutions and economic development was established. Contrary, in bad institutional environment sample no evidence was found that institutions mean a lot in respect with differences in GDP per capita. The results in Table 2 confirm that quality of institutions is important determinant of economic development, but no evidence was found that it helps to respond to economic shocks and mitigate GDP's decline.

Table 2: Correlation between economic performance and governance indicators

	Sample	N	VA	PS	GE	RQ	RL	CC	AIQI
GDP per capita percentage change (2007–2010)	ALL	153	-0.570**	-0.398**	-0.471**	-0.560**	-0.500**	-0.499**	-0.542**
	GIE	64	-0.420**	-0.187	-0.256*	-0.368**	-0.373**	-0.267*	-0.364**
	BIE	89	-0.348**	-0.079	-0.113	-0.348**	-0.075	-0.225*	-0.271*
GDP per capita average (2007–2010)	ALL	153	0.635**	0.591**	0.823**	0.789**	0.802**	0.794**	0.804**
	GIE	64	0.481**	0.323**	0.814**	0.775**	0.745**	0.691**	0.773**
	BIE	89	-0.068	0.203	0.180	0.162	0.086	0.013	0.136

** Correlation is significant at the 0.01 level (2-tailed).
* Correlation is significant at the 0.05 level (2-tailed).

The results show strong and positive link between various measures of institutions and economic development. All governance indicators positively correlate with GDP per capita and the strength of the relationship varies from moderate to strong. As in my previous research (Jankauskas and Seputiene, 2009) it can be concluded that institutions don't help to explain GDP per capita variation across countries with bad institutional environment. These results should not be interpreted that institutional environment is not important; rather the degree of "badness" makes no difference, but the degree of "goodness" means a lot.

The results come in line with Giannone, Lenza and Reichlin (2011) conclusion that regulatory quality has affected negatively countries' resilience to the recent recession. We can't neglect the meaning of institutions in economic development, but results show that in the short run good institutional environment doesn't help to respond to economic shocks, even contrary, in all cases negative relationship was observed, i. e. the better the institutional environment, the greater the decline in GDP per capita.

5. Discussion and Conclusions

The literature stresses the relationship between institutions and economic performance. According to institutional approach, well defined institutions lower uncertainty, reduce macroeconomic volatility, protect property rights and thus foster investments and innovation, which are the proximate determinants

of economic growth and development. The series of studies support the strong link between institutional environment (measured through property right, rule of law, corruption, bureaucratic quality and other institutional variables) and economic growth and development. A consensus has formed that institutions are important for economic growth and development in the long run, but recent economic crisis raised the question whether institutional environment is important in mitigating the consequences of economic shocks?

The advocates of economic globalization argue that countries get into economic crises because of unnecessary regulations and interventions in their economies and propose policies that lead to more economic liberalization. Giannone, Lenza and Reichlin (2011) raise the assumption that good governance should make countries more resilient to large shocks and therefore reduce output losses associated with recessions. But in their research authors find contrary results that regulatory quality has affected negatively countries' resilience to the recent recession. The results of this research also show that recent economic crisis has greater impact on countries with good institutional environment than on those with bad one. While GDP per capita decreased (comparing 2010 to 2007) in more than 50 percent (if to be more specific – 53 percent) of countries with good institutional environment, only 1 percent of countries with bad institutional environment experienced GDP per capita decline.

In general good institutional environment means that countries are open to international markets and encourage inflow and outflow of goods and capital so that made them more vulnerable to global economic crisis. Furthermore, institutions provide constraints on the action of government what might inhibit policy makers efforts quickly respond to external shocks and improve the situation in country in the face of a global crisis.

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The Use of Arbitration in the Administrative Contract: The Recommendation for Thailand

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Abstract

This paper aims to review arbitration laws and practices on administrative contracts in Thailand and some European countries in order to draw a comparison and then initiate some recommendations on the use of arbitration in Thailand.

After the Thai government's losses in several arbitration cases related to the administrative contract, the cabinet issued a resolution in 2009 to prohibit the inclusion of arbitration clauses in such contract. This regulation restrains international investment and has been criticized by foreign investors. Thus, reconsidering such regulation is necessary.

Interestingly, many countries in Europe have various practices on the use of arbitration in the administrative contract. Some prohibits it, unless allowed explicitly by law. Some do not have any restriction in this matter at all. From law and economic perspective, the reasons behind various practices shall be analyzed in the paper. Then, the inference would be made as the recommendation for Thailand.

Keywords

Arbitration clause, administrative contract, cabinet resolution, state intervention, Thailand

1. Introduction

1.1. Statement of the problem

For over half a century, Thailand has demonstrated that it is an "arbitration friendly state" by embracing and promoting arbitration as a method of resolving commercial disputes. Indeed, Thailand was among the earliest parties to adopt the 1958 New York Convention on the Uniform Enforcement of Arbitral Awards, adopting the New York Convention in December of 1959. Successive governments' policies and legislation have supported this internationally accepted method of dispute resolution.

It is widely acknowledged that those engaged in trade and investment often prefer to resolve their disputes by arbitration. Arbitration is considered to have many advantages compared to litigation, and businesses are therefore often more willing to trade with and invest in states where arbitration is supported as an effective procedure for resolving commercial disputes.

However, on July 28, 2009, the Thai Cabinet passed a Resolution expanding the 2004 Cabinet Resolution to restrict the use of arbitration in 'all' types of contracts- administrative contracts included, between a governmental organization and a Thai or foreign private entity, unless approved by the cabinet on a case by case basis.

The presence or absence of an arbitration clause is critical for investment decision-making and to engender and maintain confidence of investors and lenders. Given the current global economic situation, it is critical that Thailand, as a host country, has done everything possible to maintain investors' trust and confidence. Restricting the parties' freedom to contract how they will resolve private disputes operates to inhibit Thailand's efforts to promote trade and investment. As a result, it will make Thailand less competitive locally and in the international marketplace. Moreover, unintended consequences may otherwise result and could worsen the situation, such as dislocating commercial activities or deterring investment.

1.2. Significance of the study

As mentioned earlier, the author conducts this research paper in order to do the literature review about arbitration laws and practices on contracts between the state and foreign investors in Thailand and some European countries, trying to make the recommendation for Thailand in the end. Consequently, the study is conducted on the basis of documentary research-gathering, categorizing and analyzing information related to the topic.

It is worth further mention that the outcome of the paper would afterward belong to the author's master's degree thesis as a part of Thammasat International Trade Law and Economics programme in which the author is studying. For the author, the main purpose in this regard is how to logically and convincingly, analyze and criticize the congregate information from Law and Economic perspective, the area that is quite brand-new for most of academic and scholars in Thailand. So this paper is considered to be a very first step to accomplish the author's such prospective goal.

1.3. Synopsis

The substance of the paper starts from 'Validity of arbitration clauses in administrative contracts' in section 2, which mainly introduce the reader to the general view toward 'arbitrability' and 'non-arbitrability of administrative matters' in both international and domestic law. Then in section 3 and 4 are the exploration of arbitration laws and practices on administrative contract in Thailand and

some European countries, respectively. Finally, conclusion and recommendations will be presented in section 6, as a result of the analytical summary from Law and Economics perspective in section 5.

2. Validity of Arbitration Clauses in Administrative Contracts

2.1. Definition of terms

2.1.1. Administrative contract

One of the controversial issues regarding the validity of arbitration clauses in administrative contracts revolves around the definition of an administrative contract. The term of administrative contract is defined differently in each country; however, its essence is the same. Thailand's Act on Establishment of Administrative Court and Administrative Court Procedure, B.E. 2542 (1999), article 3, provides that "an administrative contract" includes an agreement:

1. in which at least one of the parties is an administrative agency or a person acting on behalf of the State; and
2. which exhibits the characteristics of
   a) a concession contract; or
   b) a public service contract; or
   c) a contract for the provision of public utilities; or
   d) a contract for the exploitation of natural resources.

In a word, administrative contracts shall be understood for the purposes of this paper; as contracts entered in to by public entities with private parties in connection with public interest matters- i.e. concession contracts relating to public utilities.

2.1.2. Arbitration clause

The arbitration agreement is defined as an agreement to submit present or future disputes to arbitration. This generic concept comprises two basic types:

a) A clause in a contract, by which the parties to a contract under take to submit to arbitration the disputes that may arise in relation to that contract (arbitration clause); or
b) An agreement by which the parties to a dispute that has already arisen submit the dispute to arbitration (submission agreement).

The arbitration clause therefore refers to disputes not existing when the agreement is executed. Such disputes, it must be noted, might never arise. (Caivano, 2005, pp. 3)

2.2. Disputes capable of being resolved by arbitration: "arbitrability"

The term "arbitrability" has a reasonably precise and limited meaning-whether specific classes of disputes are barred from arbitration because of national legislation or judicial authority. (Shore, 2009, pp.1)

Since arbitration is a private (non-state) process, with a large degree of autonomy and self-sufficiency. Court or other authorities entrusted with the protection of the public interest have only limited rights of interference. So countries have traditionally been reluctant to allow arbitration in spheres where there is a strong public interest at stake. Countries continued to distinguish between domains in which public interest and public control are relatively weak, and areas in which society (the state) has strong vested interests and policies. Disputes belonging to the first domain are arbitrable; lawsuits falling into the latter area are reserved for court and other state authorities.

The New York Convention impliedly and expressly acknowledges that non-arbitrability may defeat an arbitration agreement or prevent enforcement of an award, but not attempt to define the concept-in article II(1) provides that each contracting state shall recognize an arbitration agreement concerning "a subject matter capable of settlement by arbitration"; and in article V(2)(a) provides that an arbitral award may be refused recognition and enforcement if "the subject matter of the difference is not capable of settlement by arbitration" under the law of that country." (Várady, Barceló and Mehren, 2009)

The same is true of the UNCITRAL Model Law, which while advancing numerous uniform solutions in other areas, did not propose a definition of arbitrability. The Model Law does not directly lay out the requirement for arbitrability.(Caivano, 2005, pp. 22-23) Consequently, national decision-makers (legislatures or courts) have essentially been left to their own discretion in defining the disputes that can be settled by arbitration.

2.3. Non-arbitrability of administrative matters

The question of the validity of arbitration clauses in administrative contracts can arise in both topics of "*subjective* arbitrability or *capacity*" and "*objective* arbitrability". The first one deals with the legal ability of a person or entity to conclude an arbitration agreement. It is of particular concern in the case of states, local authorities and other public entities. The second one deals with the subject matter of disputes capable of being resolved by arbitration. In both civil-law and common-law courts, disputes in following areas have sometimes been found non-arbitrable: antitrust, securities law, intellectual property, damage from unilateral termination of exclusive distributorship agreements, political embargoes, damage to cargo carried under a bill of lading, bankruptcy, and administrative contracts. These areas are generally regulated by mandatory rules of law designed to protect important public interest and inappropriate to be resolved by arbitration.

Moreover; in other legal systems, arbitration agreements entered into by government or by various public bodies may be valid on condition that certain prior authorizations are obtained. (Gaillardand Savage, 1999) Despite many national laws contain limitations on the ability of state and public entities to settle disputes to which they are a party by means of arbitration, generally such limitations do not apply in international arbitration. Within the sphere of international law, it is now widely accepted that, a state cannot, in attempt to avoid arbitration pursuant to an arbitration agreement to which it is a party, invoke a provision of its own law that purport to prohibit arbitration with that state.(Fortier, 2005)

3. Arbitration Laws and Practices on Administrative Contracts in Thailand

3.1. The new Arbitration Act of Thailand (Okanurak and Yiamsamatha, 2004)

The new Arbitration act was enacted on 29 April 2002 and came into force on 30 April 2002. The new act replaced the Arbitration act B.E. 2530 (1987), which was criticized because it did not accord with the principles of the UNCITRAL Model Law on International Commercial Arbitration, which has been widely accepted and recognized as a prototype for international arbitration law. Therefore, a significant consideration behind the new Act was to adopt the UNCITRAL Model Law as a basis for the core development of the arbitration system in Thailand in order to keep pace with other developed economies.

The new law was also drafted for the explicit purpose of encouraging the settlement of disputes in international civil and commercial matters through the arbitration process. In this regard, the new

Arbitration act sets the same standard for enforcement of both domestic and international arbitrations, in order to promote investment at both domestic and international levels.

The question of arbitration clauses in administrative contracts, such as those in the ETA concession agreement, had been unsettled and open to debate. The new Arbitration Act resolves the question of whether arbitration clauses in administrative contracts are enforceable or not. The answer is affirmative: arbitration clauses in administrative contracts are valid and enforceable, and parties must comply with the awards as determined by the proper arbitral tribunals.

Section 15 of the Arbitration Act specifically provides that in an agreement between a governmental agency and a private party, the parties may agree to resolve any disputes pertaining to the agreement by means of arbitration, and that such arbitration agreement shall be binding upon the parties.

Another important effect of the new Act is that the arbitral awards may be revoked by the court on an application of the parties concerned. Equally significant is that disputes over the enforcement of arbitral awards in administrative contracts will now be under the jurisdiction of the Administrative Court, not the Court of Justice. Specifically, the Act provides that the appeal against an order or judgment under the Act must be made to the Supreme Court or the Supreme Administrative Court.

3.2. The cabinet resolution limiting the use of arbitration in Thai administrative contract

The boom years of the 90's construction and infrastructure investment led to a series of high profile arbitrations which went against several Government entities leading to large monetary awards. One of those is a highly controversial case regarding an arbitral agreement under the old Thai Arbitration Act. An arbitration panel awarded THB 6.2 Billion (approx. EUR 124 Mio.) in favor of a private foreign party on a concession contract concluded between the Expressway and Rapid Transit Authority (ETA) and a private consortium. Correspondingly, the Thai Attorney- General's office has put forward efforts to get such award revoked by the Administrative Court on the grounds that it would implicate the administrative law and was in conflict with the public order and his application was granted on appeal by the Supreme Court reasoning that the legal nature of the contract was administrative and therefore the execution by the governor of ETA was not in accordance with public law. Consequently, the Thai government resolved in January 2004 to outlaw arbitration in government administrative contracts unless prior Cabinet approval was obtained.(Lorenz & Partners, 2010)

The 2004 Cabinet resolution was passed even though Section 15 of the new Arbitration Act specifically provides that all contracts irrespective of the identity of parties involved may have an arbitration clause. Moreover, the 2009 Cabinet Resolution has widened the scope of the 2004 Cabinet Resolution to cover all contracts with government entities. The inclusion of an arbitration agreement in any contract with the Thai government remains subject to Cabinet approval on a case by case basis.

4. Arbitration Laws and Practices on Administrative Contracts in Some European Countries

4.1. International uniform laws

4.1.1. UNCITRAL model law on international commercial arbitration

The Arbitration Act in most of European countries is based on the Model Law. However, as mentioned above, the Model Law does not directly lay out the requirement for arbitrability. It merely mentioned in a footnote that the term commercial should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature, whether contractual or not. In

other words, the notion of commercial includes all kinds of economic transactions (excluding family and labor matters), irrespective of the private or public status of the parties involved or their categorization as merchants or non-merchants.

4.1.2. European Convention

Among European countries, a rule that states and state-owned entities cannot rely on restrictive provisions of their own law to challenge the validity of an arbitration agreement into which they unreservedly entered has been long established. It is found in European Convention on International Commercial Arbitration of 1961.Under the heading "Right of Legal Persons of Public Law to Resort to Arbitration", article II, paragraph 1 of such convention provides that:
"In cases referred to in Article I, paragraph 1, of this Convention [i.e. arbitration agreements and awards within the scope of the Convention], legal persons considered by the law which is applicable to them as "legal persons of public law" have theright to conclude valid arbitration agreements."

The convention lays down a substantive rule establishing the arbitrability of disputes involving such entities. However the convention does allow parties to make a reservation limiting the effect of this provision. Only Belgium has made that reservation, confining the impact of the rule to the state. (Gaillardand Savage, 1999)

4.2. Domestic laws

4.2.1. Preliminary observation

After exploring arbitration law and practice in some European countries, in respect of their use of arbitration in administrative contract, such laws and practices can be divided into two extreme cases: 'freely use of arbitration' and 'restricted use of arbitration'. The latter case has two different ways of restriction through their domestic law related to arbitration.(See table 1)

Table 1: the division of arbitration laws and practices on administrative contract in some European countries

1. freely use of arbitration	2. restricted use of arbitration	
	2.2 The law does not explicitly prohibit a public entity's recourse to arbitration. But administrative disputes must be referred to the national court, unless a different jurisdiction is provided by specific legal provisions.	2.3 The law explicitly forbids or limits a public entity's recourse to arbitration, or specifies administrative disputes as non-arbitrable disputes. But, there may be exceptions, by specific laws and decrees, to this rule.
England and Wales	Austria Germany Italy Netherland Poland Portugal Romania Russia Sweden Switzerland Turkey	Belgium France Lithuania Spain Ukraine

The division above is considered to be *Ex Ante* restriction toward the use of arbitration on administrative contracts. It is conducted by the legislature- via acts and the government- via decrees or emergency ordinances, in which the contracting party has to follow, in order to assure the validity of the arbitration clause in the administrative contract.

In addition to that, *Ex Post*'restricted use of arbitration' also exists. The *Ex Post* restriction is conducted by the national court of the state. Since the court is a critical player, determining the

validity of arbitrability issue; whether to enforce an arbitration clause or set aside the award, according to the law of the country.

4.2.2. Explanations

According to table 1, the domestic laws of England and Wales have no *Ex Ante*restriction on the use of arbitration in administrative contract. The law just clarifies that both contractual and non-contractual disputes may be submitted to arbitration and does not list or delimit matters which are not capable of settlement by arbitration. Matters that are deemed non-arbitrable under English law include only criminal and family law matters. (Jagusch and Dahlberg, 2012)Despite England and Wales have no statutes governing public services; n practice, there is a guideline issued for standardizing of Public Finance Initiative (PFI) contracts, including terms and conditions must have in the public service contracts. (H.M. Treasury, 2007)According to such standardization, public sector bodies are allowed to conclude an arbitration clause when drafting such contracts.

Consequently, the *Ex Ante* restrictions are found only in the domestic law of continental European countries. The restrictions are enacted in two ways differently, by two groups of countries. -In the first place, the law does not explicitly prohibit a public entity's recourse to arbitration. However, administrative disputes must be referred to the national court, unless a different jurisdiction is provided by specific legal provisions. The Romanian law governing public procurement contracts and works/services concession contracts –Government Emergency Ordinance 34/2006- confirms the jurisdiction of the national courts, specifying however that disputes over public procurement contracts must be referred to the commercial courts rather than to the administrative courts. However, such law does not apply to a certain number of public procurement and works/services concession contracts, for example, where the contracts in question were awarded pursuant to the procedures ofan international institution/organization. (Popa and Popescu, 2011, pp.103) In Portugal, 1986 Acton Voluntary Arbitration provides that the state and any other public legal entities may conclude arbitration agreements if they are authorized to do so by a special act. For instance, the Portuguese Administrative Procedure Code stipulates the inclusion of an arbitration clause in the administrative contracts and determines several categories of administrative disputes, such as the public construction contracts, which are subject to arbitration. (Center for Economic Development, 2007)

-In the second place; the law explicitly forbids a public entity's recourse to arbitration, or specifies administrative disputes as non-arbitrable disputes. The first part is a case of France Belgium and Spain law. Article 2060 of the French Civil Code provides that public entities cannot enter into arbitration agreements. There is, however, a series of exceptions to this rule. In Belgium, article 1676, paragraph 2 of the Civil Code provides that public legal entities can only conclude an arbitration agreement where the purpose of that agreement is to resolve disputes arising out of the preparation or performance of a contract.[1]Article 39 of the Spanish procurement law provides that only the entities of the public sector, lacking the status of Public Administrations, can use arbitration. (Dimitrijevich, 2010)The after part is a case of Lithuania and Ukraine law. In Lithonia, article 11 of the Law on Commercial Arbitration (LCA) sets out a list of non-arbitrable disputes including disputes arising from administrative legal relations.[2] (Audzevičius, Daujotas and Kozubovska, 2012) Article 12 of the Commercial Procedural Code of Ukraine contains restrictions on non-arbitrability of several

[1] The old provision provided that "anyone, except public law entities, with the power to enter into a settlement, may enter into an arbitration agreement. The state may enter into arbitration agreement when authorized by treatries". (Gaillard and Savage, 1999)

[2]However, public procurement contracts are not included in the list, according to the new LCA entered into force since 30 June 2012.

types of disputes including disputes arising out of conclusion, amendment, termination and performance of public procurement contracts. (Chernykh, 2012)

As for the *Ex Post* restriction, it is also found only in continental European countries in which the use of arbitration in administrative contract has to be allowed by a legal provision as an exception. This can be a case of Romanian recent court practice, denying arbitrability of disputes related to administrative contracts, even in cases where *the Government Emergency Ordinance 34/2006* in force at the time of their conclusion specifically allowed the recourse to arbitration. This is a result of the interpretation that the norm allowing arbitration was approved by means of a governmental decision, which has a lower statutory force than a law, cannot constitute a valid derogation to the provisions of Law554/2004on administrative disputes. Moreover, derogations to the jurisdiction of the administrative courts are possible only where other laws provide for a different 'judiciary' procedure, as opposed to an 'extra-judiciary' procedure like arbitration. This interpretation seems to be in line with the reasoning of the High Court and Cassation and Justice, which tends to follow a strict enforcement of the law on administrative disputes, wherever possible. (Ibid)

Another case of the *Ex Post* restriction is the court practice in France. Until now, a divergence existed between the *Cour de cassation* (the supreme court of justice) and the *Conseild'État* (the highest French administrative court) on the prohibition of arbitration for contracts entered into by public entities in international matters. While the Cour de cassation has consistently held, since its 1966 Galakis decision, that this prohibition did not apply to international contracts entered into for the purposes of, and in accordance with, the usages of international trade, the Conseild'État traditionally considered that there could be no choice of arbitration if the contract is of an administrative nature, irrespective of its international character. (Honlet, 2011)

5. Analytical Summary From Law And Economic Perspective

5.1. Nature of international law

In respect of section 2.2, 2.3 and 4.1; it is obvious that the international law on arbitration, either the New York Convention or the UNCITRALModel Law, does not elaborate a detailed list of the non-arbitrable issues and not ever mention about the *subjective* arbitrability. The Model Law only provides a general formula of *objective* arbitrability as: "what parties may compromise on or dispose", "any dispute involving property" or "any claim involving an economic interest". This is a result of considerable difficulties in reaching a worldwide consensus on such issues. Moreover; the formulation of international law usually faces a dilemma: the more general the formula, the greater the potential risk of divergent interpretation by courts of different states; and the more detailed the formula, the greater the risk of non-acceptance by States. Consequently, the issue of non-arbitrabiliy has been determined by law-makers of the states.

Nevertheless, there is an existence of a general principle of international arbitration that states and state-owned entities cannot rely on restrictive provisions of their own law to challenge the validity of an arbitration agreement. This rule is extracted from many sources of international law. In this place, the European Convention provides that legal persons of public law have the right to conclude valid arbitration agreements, whereas Belgium is the only one European country makes are servation to this provision. Thus, it implies that other European countries are bound to follow such provision. However, the preliminary observation of the study reveals that most of continental European countries still restrict the use of arbitration in administrative contracts through their domestic laws and the court decision. From legal perspective, this situation asserts the weak binding nature of international law due to a lack of enforcement mechanism in the international community. From economic perspective, however, it reflects self-interest behavior of the states, deciding to violate the international law when their interests are better served.

5.2. State intervention

In respect of section 4.2; England and Wales are considered as the representatives of common-law regime which use the single court system, while other continental European countries are as the representatives of civil-law regime which use the dual court system.

An outstanding result is that the use of arbitration in the administrative contract is very restricted in the civil-law countries where administrative jurisdiction is very well developed and plays an important role in the judicial system alongside the civil courts. It is different from the practice of the common-law countries which has allowed public entities concluding arbitration clauses in administrative contracts freely.

Focusing on 'restricted use of arbitration' in administrative contracts found in the civil-law countries, it is categorized into '*Ex Ante* restriction' and '*Ex Post* restriction'. From economic perspective, such restrictions are perceived as state intervention- the former is conducted by the legislature and the government, while the latter is conducted by the national court. This practice, on the one hand, reflects protectionist policy through domestic regulations and judicial review of the state. On the other hand, from legal perspective, it is in line with the concept of dual court system in which all the administrative disputes must be settled by the administrative court as it is the mandatory rule. Noting that in addition to protect public interest, the reason of having the administrative court is to balance unequal status of a state and a private party in the contract. Inquisition system[3]using in the administrative court is apparently created for private interest protection, different from accusation system using in the court of justice and arbitration that based on the equality of the contracting party.

5.3. Economics of contract

The state and its entities enter into international economic transactions, administrative contracts included, for a reason that is rooted in both law and economics: law, because they act in accordance with the legal regime governing their capacity; economics, because they enter into exchange arrangements with other private entities in order to satisfy their needs.

In a world of high transaction costs, contracts are often incomplete, not contingent on all relevant, in order to reduce such costs as much as possible. In practice, when two parties bargain over the agreement of a contract, they seek to include only substantial matters must have for the benefit of performances. Such is precisely the objective underlying the clauses of a contract, including its agreed system of dispute resolution. Therefore, a clause providing for dispute resolution through arbitration seems to fulfill such demand because it is concise and easy to conclude.

Mention again that the arbitration clause refers to disputes not existing when the agreement is executed and such disputes might never arise. So it is possible for the administration as the representative of the state to include an arbitration clause in the contract, although it may violatesthe state restrictions, if such contract is expected to aplenty benefit the contracting state. In respect of section 4.2.1; the *Ex Ante* restriction is divided into two ways of enactment, creating

[3] In the inquisitorial system, the presiding judge is not a passive recipient of information. Rather, the judge is primarily responsible for supervising the gathering of the evidence necessary to resolve the case. Thus,ifthe evidence is in the possession of the state, causing hardship for a private party to exhibit such evidence before court, the judge is able to call for such evidence in favor of the private one.

different environment for parties to draft the contract. If the law *Ex Ante* does not explicitly prohibit public entities recourse to arbitration in administrative contracts, it is easier for the party to conclude an arbitration clause and leave the issue of its validity to be justified by the court *Ex Post* when the disputes arise.

6. Recommendations for Thailand

In respect of section 3; the arbitration laws and practices on the administrative contracts in Thailand have its own history, different from many others .At first, the old 1987 Arbitration act did not expressly support the validity and enforceability of arbitration clauses in administrative contracts. Afterwards in 2002; despite the administrative court of Thailand had been instituted in 1999 creating its own jurisdiction over administrative disputes, section 15 was added in the new Arbitration act explicitly asserting that public entity are able to include arbitration clauses in such contracts, in order to promote the investment in the country. Recently, however, the cabinet issued a resolution in 2009 prohibiting public entities recourse to arbitration in such contracts with an exception of necessities, as a result of Thai government's losses in several arbitration cases.

Trying to draw a comparison between the arbitration laws and practices of Thailand and some European countries, some recommendations are initiated as follows:

a) Thailand is a civil law country which has a special jurisdiction of administrative court as same as countries in continental Europe. So it is not unexpected that Thailand restricts the use of arbitration in administrative contracts as well. However, the reason behind such restriction of Thailand is somewhat different. As to the use of arbitration in administrative contracts, the continental European countries seem to prohibit it firmly at the beginning and then slowly allow it through legal provisions as exceptions; while, Thailand has no restriction on it at first, then allows it explicitly by the arbitration act and turns back to prohibit it by the cabinet resolution at last. This observation reveals that the arbitration laws and practices in the continental European countries are keeping with the legal method of the dual court system, in which administrative disputes must be settled by the administrative court as a mandatory rule; while such laws and practices of Thailand are not accordance with such rule from the very beginning. On the contrary, the restriction has been prescribed recently because the Thai government did not want to be a losing side by arbitral awards anymore. This implies that the Thai government expects to always win the case by the administrative court, which is an inaccurate perception of having the administrative court- such court is not designed to judge a case in favor of the state. The recommendation here is that: if such expectation of the Thai government is truth, the administrative court practice in Thailand must be reconsidered; if not, it is the misunderstanding of the Thai government leading to such misdirection policy.

b) The cabinet resolution of the Thai government is seen as the *Ex Ante* restriction that explicitly forbids a public entity's recourse to arbitration. This way of restriction creates a lower opportunity to generate a contract than does not explicitly forbid a public entity's recourse to arbitration and leaves it to the *Ex Post* restriction by the court to decide the validity of an arbitration clause when disputes arise. So if Thailand wants to promote and create the investment contract, such *Ex Ante* restriction should be revised.

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Cross-cultural Leadership: A Roadmap for the Journey

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Abstract

In reflection of an upcoming trip to Kenya, a semester teaching in London, and recent engagements assisting consulting clients in understanding the intricacies of multiple cultures (at both the customer and supplier level), the current authors attempt to synergize research into guidelines for the challenges of cross-cultural leadership. As Gergen (2009) notes, developing leaders is a need shared throughout the world. Although the problems and solutions will differ, effective analysis, strategies and principles are largely universal when adapted to differing cultures. This research examines criteria for evaluating which leaders might be effective in crossing cultures.

Introduction

In order to apply leadership across cultures, it is important to establish our foundational position on the important role leadership plays in all organizations. Noted leadership scholars Neck and Manz (2013) posit that all who desire to improve leadership effectiveness must commit to a life-long journey of purposeful learning. Prior research reveals "mindsets" of effective leaders and the importance they place on the following key elements: 1) truth-truthfulness and trust-trustworthiness, 2) personal and group development, 3) curious flexibility, 4) incremental and revolutionary knowledge expansion, 5) personal and organizational innovativeness, 6) cross-cultural appropriateness, 7) balanced creative and practical problem solving for fitting solutions, 8) accountability and collaboration, 9) leveraging and applying knowledge, skills and abilities, and 10) seeking excellence through realization, reception, reflection and reproduction (Service and White, 2011; Shinn, 2011).

Our beliefs in leadership development are informed by the Oxford Tutorial method, where one reads, studies and digest as much as possible in order to reflect on newly gained “insights” thereby allowing one to make improvements. We believe that such a model applies nicely to developing leaders and de-mystifies the idea that leaders must be born with “it.” This development is advanced when an individual can be exposed to deeply collaborative learning, but it is possible to go it alone to a certain extent. Regardless, we must leverage all the knowledge in our heads and in as much of the extant literature as possible to reflectively probe, brain storm and scenario thought experiments in order to think by cycling through important problems and fitting solutions (Isaacson, 2007 and Service, 2009b).

We see leadership improvement starting with self knowledge directed toward enhancing leadership wisdom and quickly extending to a balanced understanding of followers and situations (Bisoux, 2011; Klopf and McCroskey, 2007; and Phan, 2011). Based on the work of Covey, Drucker and Mintzberg we offer several drivers of leadership development: Seek to know where you and the followers are in leadership development and then define clearly where all of us need to be personally and organizationally. Surround your study with these thoughts: 1) avoid developing and following “lists” instead learn to think, reflect and generalize; 2) leaders are nothing, leadership is everything; 3) you cannot predict the future, but you can help shape it; 4) leadership involves a) the leader, b) followers and c) situations; 5) enduring education is based on admitting ignorance, avoiding false dichotomies, truth, understandability, ownership and growing versus redistributing; 6) change under changeless principles; 7) all are constantly evaluated and judged, think about the perspectives of those judging; and lastly, 8) without action nothing is accomplished.

Management and Leadership Wisdom

While the authors attempt to expand an understanding of leadership in cross-cultural situations we also must acknowledge that our individual experiences are primarily as a result of living in American and Western European settings. There is much to be learned about leadership in differing contexts. The following section examines the role of wisdom in effectively developing leaders for cross cultural duties.

We all can gain wisdom, by properly reflecting on our mistakes and triumphs and not treating those two imposters the same. In leadership and management we must begin by differentiating wisdom from actions. Start by defining leadership as management done well. If you intend to be a good manager you will need to understand what it takes to be a good leader. The other non-leadership "parts” -if you will- of management are programmable and easily followed for efficiency. All too often we say management is doing things right and leadership is doing the right things; or

management is keeping people in the known and leadership is moving people into the unknown. Therefore, we need to develop people capable of exhibiting leadership as human influence through management, selection, relationships and creditability on appropriately balanced scales.

Leadership wisdom is circular. Effective leadership requires understanding of equifinality and multiplicity. Equifinality is a principle observed in open systems, and of course effective leadership is nothing if it is not an open system (Von Bertalanffy, 1968). Equifinality implies that individuals and organizations can obtain advantages and success in substantially different ways and that what worked or works for one may or may not work or apply for another at the same or another time. Multiplicity implies that every "thing" (all of which humans work with and for) becomes increasingly more complex, ambiguous and uncertain in depth and breadth, and there also become more "things" over time (Tyson, 2007). Finally, we see leadership wisdom is often useless if one selects the wrong issues to address (Davenport and Beck, 2001). The "worst" failed leadership and management are normally not related to effort or purposeful ethical lapses; they are caused by: 1) distrust- justified or not, 2) failing to act-no decision, and 3) selecting the wrong issues to address.

Motives and Contingency in Leadership

A better understanding of why leaders attempt to influence others is gleaned by knowing what the advice giver has to gain. Effective leaders and followers realize that influence is relationship based: mutual learning and trust; give and take; win and lose. Participants in leader-follower dyads can determine what *they* value versus what outsiders value and why and how in order to better meet today's newest challenges which are: 1) Leading travelling volunteers not managing employees. 2) Requiring new skills and understanding of self, others, and situations. 3) Managing in the known while leading into the unknown. 4) Handling lack of motivation and poor attitudes.

Leaders must be weary of propaganda disguised as truth. “No truth is without some mixture of error, and no error so false but that it possesses some elements of truth. . . . We must be sure though. . . . that we do not misapprehend what the facts really are (Wilber Wright in Tobin, 2003: p. 90).” Faced with a seemingly impossible task? Ignore the skeptics and just get on with *it* and *it* will improve (Smolin, 2001). So move to mindsets of: reflective, analytical, worldliness, collaborative and action (Mintzberg, 2004 and 2009). Then pick up these skills: 1) Extrospectionalism – nothing without reality. 2) Perspectivalism – nothing if "you" don’t see as "they" do. 3) Reflectionalism – nothing without application. 4) Generalizablism- nothing if it does not fit. 5) Introspectionalism – nothing without change (Service and Lockamy, 2008). Remember to watch your instincts: there are thousands of tells-tics, winces, flicks, looks, moves, inflections, etc.-every minute: be aware observe versus just look to pick them up (Brooks, 2011).

Much of our consulting work has revolved around the challenging tenet that 1) appropriate, 2) balance, 3) fit and 4) it depends answers everything. The challenge for leaders, regardless of cultural context, is in shifting thinking to understand what it depends on to become and remain appropriate, fitting and balanced in your actions as a leader. For indeed:

> The practice of management is characterized by its ambiguity. . . . leaves managers mostly with the messy stuff—the intractable problems, the complicated connections. . . . [Managers need] experience, intuition, judgment, and wisdom. . . . we need leaders with human skills, not professionals with academic credentials (Mintzberg, 2004: p. 18).

Douglas McGregor (Theory X and Y) simply found inadequate the models of human relations he taught when he studied organizational leadership.

> It took the direct experience of becoming a line executive . . . to teach me what no amount of observation of other people could have taught. . . . I hoped to duck the unpleasant

> necessity of making difficult decisions, of taking the responsibility for one course of action among many uncertain alternatives, of making mistakes and taking the consequences. I thought that maybe I could operate so that everyone would like me. . . . I couldn't have been more wrong (Wren and Bedeian, 2009: p. 430-432).

Leadership and Innovation across Cultures: GLQ-Global Leadership Quotient

After the above summary of background information on useful leadership concepts, we now come to the first focal point of this article and its resulting model. Service (2012) explains that international experience is a must for those seeking top executive and managerial level positions in most organizations of today (Mendenhall, et al, 2008). Service (2012) continues that global venture problems occur because of attitudes and lack of skills in relating "with" people in different cultures. "Integration of technologies, industries, nations, cultures, relationships, and interests continue to characterize the twenty-first century workplace (Potoker, 2011: p. xii)." Most researchers and practitioners are now saying that "[t]he leader of tomorrow is someone who can jump across boundaries and disciplines and analyze cultural and global differences (Shinn, 2011: p. 37)." "Leading across cultures requires specific skills, and organizations should provide formal training along with expatriate assignments to develop leaders who can achieve results in this demanding environment (Mathis and Jackson, 2013: p. 15)." Moreover, the required road to leadership understanding and improvement in a "flat" open world remains all too contradictory and unforgiving (Friedman, 2005 and 2008; and Tracy, 2010). These pronouncements indicate that few executives will succeed without worldly contextual adaptability skills and few organizations will succeed without global leaders (Mintzberg, 2009 and Service, 2006 and 2012). To address global leadership realities, contextually adaptive people who can lead must be developed (Service and Loudon, 2012).

All forms of adaptability require some level of self discovery. Yet, "we must admit that everyone else probably understands us better than we do ourselves (Jung, 1933: p. 77)." And, there are numerous models, frames, metaphors, and filters that we all use to make sense of our world. Moreover, "The fact is that people do not actually go empty-handed but take with them various frameworks. . . . [T]he choice is not between a framework and not taking one, but between taking one that is implicit and unconsidered, and one that is explicit and susceptible to conscious thought and challenge (Bate and Child, 1987; p.37)." Further, effective leadership, innovation, cultural awareness and so on, are about *commitment and necessity* directed toward accomplishment:

> A common series of . . . . processes seems required . . . sensing needs, amplifying understanding, building awareness, creating credibility, legitimizing viewpoints, generating partial solutions, broadening support, identifying zones of opposition and indifference, changing perceived risks, structuring needed flexibilities, putting forward trial concepts, creating pockets of commitment, eliminating undesired options, crystallizing focus and consensus, managing coalitions, . . . formalizing . . . commitments (Quinn, 1980: p. 146).

Figure out what sort of environment [we live] in and carve mental maps that would help [us] navigate it. . . . [developing] sophisticated models, which are then used to anticipate, interpret, and navigate through life (p. 46). . . . the essential feature of a human being, a culture, or a society (p. 108-109). . . . Cultures are emergent systems (Brooks, 2011: p. 110).

Cultural capital—tastes, opinions, cultural references, and conversational styles that will enable you to rise in polite society (p. 146). . . . We absorb ethnic cultures, institutional cultures, regional cultures, which do most of our thinking (p. 149). . . . Most relationships are bound by trust. . . . Trust reduces friction and lowers transaction costs (p. 155).

Klopf and McCroskey in *Intercultural Communication Encounters* (2007) said:

> [i]gnorance of another's culture is a major factor causing intercultural miscommunications (p. 9). . . . All cultures are characterized by distinctive attributes. We reviewed seven: [1] pervasiveness, [2] learned behavior, [2] shared behavior, [4] adaptability, [5] explicit/implicit behavior, [6] change and [7] ethnocentricity (p. 26).

Storti in *The Art of Crossing Cultures* (2001) says clearly that:

> cultural effectiveness comes at the cost of vigilance and sustained effort (p. 106). . . . it is difficult to imagine how they can succeed if they can't interact effectively with people from the local culture (p. xv). . . . Becoming culturally effective does not mean becoming a local; it means trying to see the world the way locals do and trying to imagine how they see you. . . . life is to know when to give way and when not to . . . So too the art of crossing cultures (p. 96). . . . Another advantage of being culturally aware is that the better you understand the local culture, the harder it is for the locals to hide behind it (p. 107). . . . The ability to see situations, problems, practices—the way we do things—from multiple perspectives, from the way other people see things, is a tremendous benefit to you and to your company when you get back home (p. 111).

Storti further warns that often you get sent abroad because you are bright and at the top of your game.

> [G]et beyond the temptation to withdraw from the local culture (p. 63). . . . cultural differences are not the only reason cross-cultural encounters some time go wrong. People from different cultures can fail to get along with each other for any number of reasons (p. 45). . . . The capacity of the average person to fully conceive of the "other" has always been greatly exaggerated (p. 70). . . . [for indeed] perceptual responses are influenced by the individual's expectations (p. 82). . . . Lists of do's and don'ts can't cover all contingencies, of course, and tend to greatly oversimplify cross-cultural effectiveness (2001: p. 87).

Dorner's treatment of *The Logic of FAILURE* (1996) said:

> Studying the consequences of our measures gives us excellent opportunities for correcting our incorrect behavioral tendencies and assumptions about reality. If our measures yield unexpected consequences, there must be reasons. By analyzing those reasons, we can learn what we should do better or differently (p. 177).

When faced with an unknown, especially about another culture or country, the first step is to "know what you don't know;" then read, study, focus, ask, and accept, to learn and then use what you have learned non-judgmentally. Seek first to understand before seeking to be understood (Covey, all dates). Famed management guru Peter F. Drucker (1998) said management is about human beings; and it is embedded in the cultures of organizations and societies.

As one's contextual intelligence grows, one moves from unconsciously incompetent to consciously incompetent, then to consciously competent before arriving at their final destination of unconsciously competent.

> It would be narrow-minded for us to believe that our picture of the world is the definitive one. . . . Experiments in psychology support the idea that people automatically assume their subjective experience to be a faithful representation of the real world. . . . Immanuel Kant postulated [in 1781] that the reality we experience is one that has been constructed and shaped by our minds, minds limited by our beliefs, feelings, experiences, and desires (Chopra and Mlodinow, 2011: p. 279).

Duane Elmer's 2002 *Cross-Cultural Connections: Stepping out and Fitting in Around the World,* is perhaps the best book on actually crossing cultures. Some other books have more research and broader thoughts, but Elmer, a professor and director of a Ph.D. program, provides the most direct

and useful advice. He has taught college courses in crossing cultures for 30 years. He continues to work with churches, educational institutions, missionaries and top companies in understanding how to be effective in different cultures. Elmer has worked or lived in over 75 countries. His principles start with skills of openness, acceptance and trust. For many the most meaningful concepts revolve around the often dichotomous views of right and wrong. Elmer allows that there should be a continuum as follows:

Wrong ----------just different----------Right

In sum, Elmer says it is a life long struggle to know where the lines are drawn on the right and wrong continuum. An awakening is often required for one to understand their personal narrow-mindedness (Punnett, 2012; Saba, 2011; and Thornton, 2012). Only continued epiphanies can provide a renewable evolving GLQ: remain open to the unexpected, new or different. The following GLQ model was developed from the literature, experience and a pilot study with some 50 individuals who have crossed cultures for business, teaching and learning (see Service and Loudon, 2012):

Figure 1: GLQ "Required Worldview" Strengths and Weaknesses (modified from original)

I. Strengths - advantages that are enablers in contextual adaptive development

A. Natural - more uncontrollable 'good' traits-key abilities and attitudes

1. Flexible-openness: equifinality
2. Dispassionate
3. Gender and gender orientations
4. Internal locus of control
5. Abilities under psychological hardiness
6. Attitudes & awareness-curiosity
7. Humility
8. Empathic listening
9. Time is theirs
10. Identificational-as different

B. Nurtured - more controllable 'good' traits-key knowledge and skills

1. Known "open" mindsets
2. High social/cultural intellect
3. Weak ethnocentricity
4. Observant
5. Knowledge/skills-job/tasks
6. High EQ
7. Patience
8. Cultural sensitivity
9. Preparation
10. Integrity

II. Weaknesses - disadvantages and derailers to leadership development

A. Natural - more uncontrollable 'bad' traits-key self-centered

1. Strong national affiliation
2. Narcissistic
3. Change avoidance
4. Large power distance
5. Cognitive simplicity
6. Psychological immaturity
7. Fix worldview
8. Blunt-dogmatic
9. Knows without study
10. Lacks moral compass-integrity

B. Nurtured - more controllable 'bad' traits-key avoidance

1. Disdaining other views
2. Confirming mindset
3. Learned behavior pervasiveness
4. Un-accepting of differences
5. Low EQ
6. Relationship challenged
7. Extractionist-to change worldview
8. Telling over discovering
9. Seeing as right or wrong
10. Holds to timeframes vs. events

The essence of the GLQ revolves around ***intentionality***: vigilant attention and sustained effort. While adequately describing this model goes beyond the scope of this manuscript (see Service and Loudon, 2012 for a full review) it does provide a launching point to propel our dialogue on cross-cultural leadership. Mendenhall, Osland, Bird, Oddou and Maznevski's (2008), *Global Leadership:*

Research, Practice and Development is perhaps the most complete global leadership "research review" book in the past 50 years. Their work offers several concepts that map nicely onto the GLQ:

> Today's world of global business requires that companies must "innovate by learning from the world" . . . transform individuals in ways that make them more valuable employees (p. 129). . . . today's leaderships will not be sufficient for the future, owing to the changing nature of global business (p. 50). . . . The passion to make a difference and the willingness to allow others to participate in creating it is more likely to lead to leadership success than simply acquiring and checking off a list of skills (p. 62).

Hall, (2011) said, "[W]hatever wisdom we manage to achieve derives from genes, nurture, mentorship, culture, and, perhaps most of all, an openness to the possibility of continual leaning and self-improvement (p. 225)." In Corbin and Strauss's (2008), we see an important quote regarding those that might say the above Model is too complex: "What is important is that research findings don't oversimplify phenomena, but rather capture some of the complexity of life. . . . *conditions/consequences do not exist in a vacuum* (p. 91)."

Difficult is Not Impossible

"Our premise is that many of the circumstances that seem to block us in our daily lives may only appear to do so based on a framework of assumptions we carry with us. Draw a different frame around the same set of circumstances and new pathways come into view (p. 1). . . . Our joint conviction is that much, much more is possible than people ordinarily think (p. 2)." We all seek confirming evidence based on our limited assumptions and frames and seldom really listen to or see dissenting views. For example, Picasso said about why he did not paint people "as they really are: show me a picture of her. Isn't she rather small and flat (Zander and Zander, 2000: p. 11)?"

From a *Business Week* book of the year we see a quote that can help us all understand more about why we should study such difficult concepts as leadership, culture and influence:

> All people have untapped leadership potential, just as all people have untapped athletic potential. There are clear differences due to nature and nurture . . . as to how much untapped potential there may be. Not everyone can be the CEO of a multibillion-dollar corporation. . . . but leadership is there in you (Tichy, 2002, p. 8).

Service and Kennedy (2012) offer additional input by stating that among others variables, mindsets and worldviews are touted as foundational to cross cultural success. "Nothing is more mysterious than another person's worldview. Each of us has one. We believe that our worldview expresses reality (Chopra and Mlodinow, 2011: p. xvii)." And, nothing influences success of leading across cultures more than one's worldview. An important work that more should review is illustrated by the following quotes:

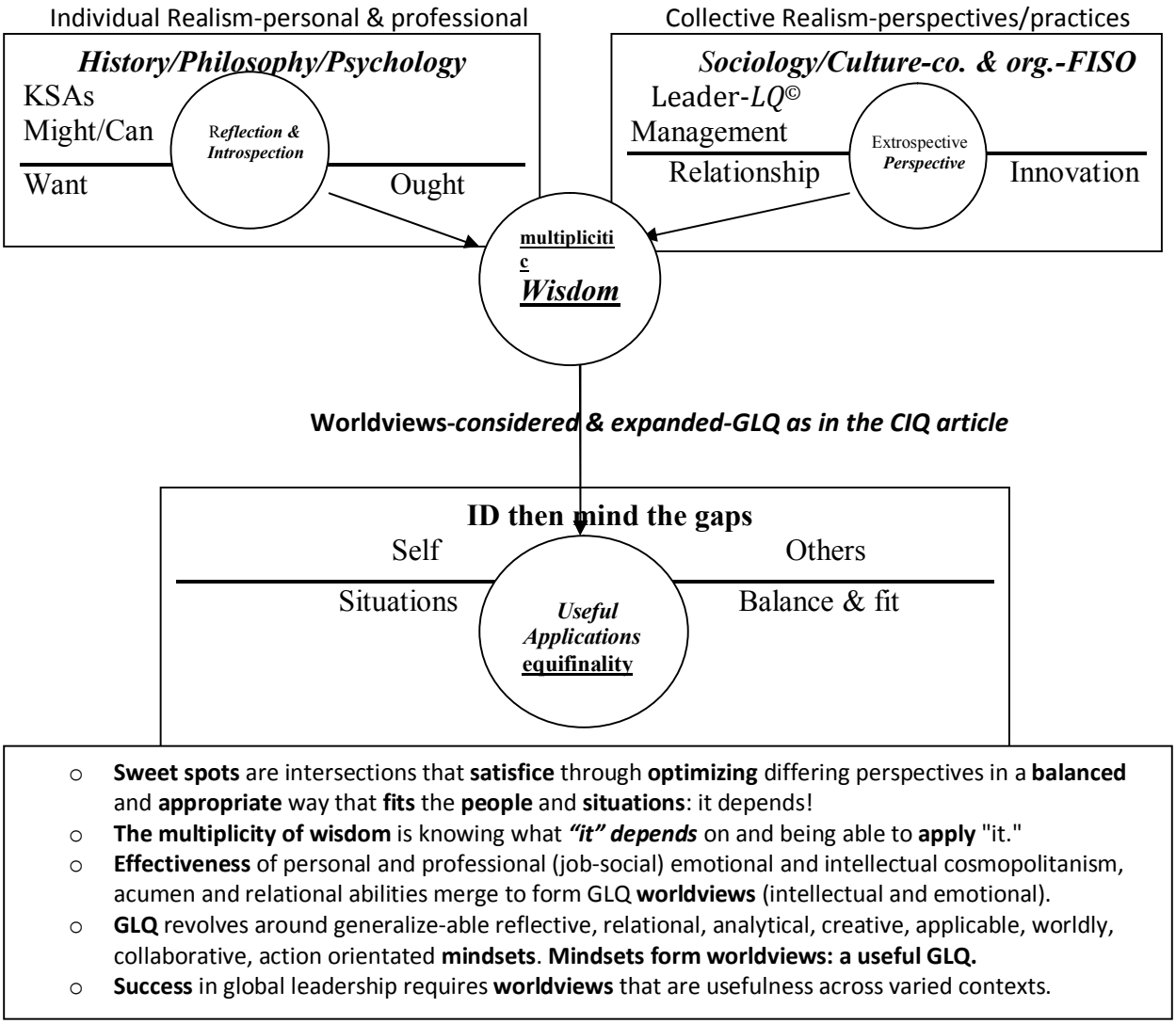
> <u>In order to communicate effectively with oral cultures, I am asking that we think differently than we have been taught to think, that we teach differently from the way we have been taught, and that we learn differently than the way we have learned</u> (underlining his: p. 50). . . . With above comparisons and explanations, I am in no way arguing that orality is better than literacy or vice versa (p. 29). . . . I simply do not have enough understanding to make any judgment in the matter (p.60)."

The discussion from this section leads us to the conclusion that for success in cross-cultural situations one must mind their worldview mind-sets.

Cross-Cultural Leadership for the Rest-of-us

The preceding pages have provided the groundwork for introducing the forthcoming model that addresses the many and varied complexities of cross-cultural leadership. The articles reviewed in this paper and Service and Arnott's book *Leadership Quotient-LQ*© (2006) which cites over 500 sources, uses 1,100 questionnaires, other empirical academic and popular press work, and 40 years of experience and research, are the base for Model 2 below. New research on a Contextual Intelligence Quotient (Service, 2012), GLQ (Service and Loudon, 2012) and a Rest-of-Us leadership model (Muczyk and Holt, 2008; and Service and White, 2011) move the leadership model forward to meet the complexity and ambiguity of global leadership. The new Model represented here moves us to a comprehensive view of what it takes to be a more effective global leader. Remember that non empirical research can be an innovative direction setter. And, as the great Peter F. Drucker came to realize leadership improvement is necessary and possible if it becomes a life-long self-development activity (Cohen, 2010).

Figure 2: Global Leadership Effectiveness Model



- **Sweet spots** are intersections that **satisfice** through **optimizing** differing perspectives in a **balanced** and **appropriate** way that **fits** the **people** and **situations**: it depends!
- **The multiplicity of wisdom** is knowing what ***"it" depends*** on and being able to **apply** "it."
- **Effectiveness** of personal and professional (job-social) emotional and intellectual cosmopolitanism, acumen and relational abilities merge to form GLQ **worldviews** (intellectual and emotional).
- **GLQ** revolves around generalize-able reflective, relational, analytical, creative, applicable, worldly, collaborative, action orientated **mindsets**. **Mindsets form worldviews: a useful GLQ.**
- **Success** in global leadership requires **worldviews** that are usefulness across varied contexts.

The Model

In examining Figure 2 it is important to note that the amalgamation of sweet-spots of leadership effectiveness is "Wisdom." This "Wisdom," as described earlier in this manuscript, balances combinations and permutations of circumstances that fit the involved people at the appropriate time in the proper manner. Wisdom is not only knowledge but more importantly how and when to use the appropriate knowledge. Focus on analyzing yourself, others and situations and apply new-found knowledge to improve leadership effectiveness in complex contexts (Hall, 2011; Sternberg, 2003; and Tichy and Bennis, 2007).

Individual Realism-Personal and Professional

History: Few doubt that every individual is a product of all that has ever happened to them as well as their genetic make-up. Who one interacts with, and what one sees, hears and reads as well as all that has happened to mankind, particularly one's own ancestors, make us all who we are. "[N]one of us exists, self-made, in isolation from it (Brooks, 2011: p. 32)." The Model precepts within the heart of this sub-model have been discovered and cultivated, as the current authors have dissected historical accounts of leadership events with an eye toward discovering underlying variables (Corbin and Strauss, 2008). The objective of this sub-model centers on reflection and introspection through "thought experiments" where you mentally practice leadership precepts (Csikszentmihalyi, 1990; Gopnik, 2012; Isaacson, 2007; Service, 2009 a and b; and Service and Carson, 2010).

Might-Can-Want-Ought

Since leadership is a needed and improvable form of human influence that moves people into the unknown, philosophical and psychological understandings are needed: introspection that results in work. *Might* represents the possible market for a given leader. *Can* rests on one's abilities and knowledge. *Want* is desire. Finally, we see ought as the ethics and values of doing something and how one does it. When one contemplates introspectively the variables about themselves they are being philosophical; but when they help others, they use psychological skills of influencing through reflective questioning and listening. Sadly in some cultures gender, political or religious persuasion may make "might" very difficult if not impossible for some: prefer truth over politically correct (Blair, 2010; Covey all dates; Kouzes and Postner, 2010; Levitt and Dubner, 2005 and 2009; Peters, 2003; Service, 2012; and Thornton, 2012).

Collective Realism – Perspectives and Practices

Collective humanistic influence gets to the nature of leadership as it crosses into the realm of sociology where leaders determine what it takes to motivate and move "groups" of people. Understanding cultural norms underlies required leadership styles and methods that have any chance for success in major contextual changes (Yukl, 2013).

Leader-perspectives: After years of searching and wishing one finds that there are simply no magic solutions or secrets. True human influence revolves around the foundational understandings of leaders, followers, and all levels of environments, and how they interact as leadership occurs (all Service-LQ). All of us want direction, inspiration, validation, and relationships (Charan, 2007). Also we want leadership that will guide us to the next level. "Leadership is a combination of strategy and character. If you must be without one, be without the strategy (Schwarzkopf in Corsini, 2006: p. 33)."

Follower-perspectives: Followers stirred to act proves leadership. Without followers there are no leaders. Goleman's Emotional Quotient (EQ) is a trademark of what it takes to be a great follower (Goleman, all). Followers must be persuadable and capable if they are to follow successfully. They must have IQ and EQ appropriate to the mission and needs. Leaders can move people to where they would not normally go, but they cannot change the core make-up of intellect, emotions and physical capacities. All successful global leaders must understand the cultural orientations of those they wish to make into followers (Collins, 2001; Service and Carson, 2009; and Yukl, 2013).

Situation-perspectives: Situational awareness-analysis directed toward understanding situations as they arise provide the foundation for strategic intelligence (Service, 2009b). Strategic intelligence is required because strategy is a journey of planning, implementing, evaluating and adjusting while paying attention and focusing on the right things: current and desired situations. Successful strategy is about understanding the situation that encompass the people for it is through people (leaders, followers, customers, stakeholders, and the public at large-societies and their cultures) that goals get accomplished (Hunger and Wheelen, 2011). An answer to Colin Powell's question, "Why would you follow somebody around a corner?" defines a successful leader's situational analysis, strategy and leadership (Harari, 2002 P: 203).

Contextual-perspectives: Humans are unable to understand total reality (Gladwell, 2008; Levitt and Dubner, 2009; and Pink, 2009). However, one can move their perception closer to reality and manage the others involved to move them to enact the situations one wants and needs. First, consider the sampling of the complexities of cultural subsystems of: 1) Psychological systems of individuality. 2) Subsistence methods system-how we make a living. 3) Cultural, religious or man-made systems aspects of interrelated life.4) Social systems-define interactions, roles, and laws.5) Ecological systems-all aspects of differing physical environments.6) Inter-individual side-sociology. 7) Projective aspects of myths, fantasies, and religion. Second, realize that there are other "thinking framework" descriptors which include: ecosystems, demographics, economic systems and conditions, international communities, resource availability, political and governmental issues, legal, competitive flatters and accelerators, family, technological and organizational cultures. Third, realize these "classifications" overlap the seven cultural subsystems above, but taken together allow for many combinations and permutations of complexity that form a realistic view of our complicated contextual worlds (Barney, 1995; Friedman, 2005 and 2008; Gardner, 2006; Pinker, 2002; Service and Ledlow, 2007; and Sternberg, all dates). And, finally, we can conclude that with so many varied viewpoints to choose from, it is amazing that there is any agreed-upon version of contextual reality). Those differing "ways" must focus on followers' cultures and contexts: not that simple.

Do not be limited by your frames or filters. Do not ignore arguments that do not fit your mental models. Most of us seek confirming evidence and seek only models and frames that fit our opinions and preferences. Global leadership improvement is not just about solving problems, but more about being open to new ideas and views (Blair, 2010; Charan, 2007; Collins, 2003; Drucker, 1967; Mintzberg, 2004; Service, 2009a; and White and Lean, 2008).

Collective Realism - Practices

This is where collective wisdom starts for in one situation "management"(that is primarily doing things right or more efficiently in a systematic manner) is called for; or the situation might call for "relationship building;" or it might require "innovation" (doing something new and different); or it might require "leadership" to move people into new and different directions. The correct choice requires combining "extrospection" with the perspectives noted in the previous section. The manage-lead-relate-innovate wisdom revolves around when it is time to do what. Normally true

leadership requires going through each of these actions as one leads people into the next wave; they must manage them through relationships and innovate as new situations arise.

In this area one decides to lead, manage, build relationships or innovate; often it is a combination, i.e. lead and innovate through relationship building.

Leadership-practices-overview: Leaders influence followers in new desired directions. They use many styles and ways to accomplish this difficult influence (McIntosh, 2011; and Monarth, 2010). But, leadership wisdom only comes when one knows when to tell, sell, ask, collaborate, back off, jump in, shoot from the hip, do research, become a follower, create or enact a new situation, recruit different followers, return to the old followers, jump up and down and shout, be still and quiet, and so on. Regardless of actions the one thing leaders must avoid is inaction for as Churchill said, "I should have made nothing had I not made mistakes."

Today's pop psychology theories and secrets of leadership are simply a leadership lottery for those that do not realize that leadership development is tough, mentally challenging work. Wishing it were easy does not make it so. We often equate leadership fads to dieting fads, most work, but all have a cost. In dieting, most help for a while and do not hurt much and some are deadly; but most of them simply delay the real needed change, and produced roller-coaster effects. Leadership development is like weight control: at some point you have to forget the fads and practice the basics. Then in both diet and leadership one must continue to practice the fundamentals in a new lifestyle. To be successful in personal leadership development, you have to learn the basics with a *balanced* perspective; and then practice and refine them. There are no simple answers. There exists only *balanced* hard work and discipline behind one becoming an effective global leader that can *fit* the *leaders, followers,* and *environments* facing them in order to *stand out* as an effective leader who has honor and lasting respect (Service and White, 2011).

Leadership-practices-LQ©: "The leader must be able to self-diagnose and have a high degree of self-awareness. . . . the leader must be an expert observer of others. . . . the leader must be able and willing to intervene, coach, and influence. . . [the] leader's ultimate task is to build organizational competence (Runde and Flanagan, 2007: p. 83)." In global organizations today for success a simple *LQ©* principle must be applied: FISO-Fit In before you Stand Out. We see FISO as a concept that is a foundational truism in all cultures and contexts.

Previously, Service (2009b) proposed combining the *Leadership Quotient's* (LQ©) and thought experiments as a framework for leadership and management. The point was to define leadership more completely than had been done in the past in order that one would have a better benchmark. The research question in the 2009 article was; how can one understand (for application) the good and bad qualities they have, and the influence of those precepts in order to become a more effective leader? This difficult task was met with due diligence and effort through application of Einstein's thought experiment concept merged with the LQ© (Service, 2009a and b; and Service and Arnott, 2009). The resulting frameworks provide a comprehensive system for studying and improving leadership. That stream of research concluded that measuring one's self against precepts related to the occurrence of good and bad leadership with the mind's eye toward maximizing strengths and minimizing weaknesses can result in a thought experiment that improves leadership effectiveness.

***Management-practices*:** Leadership is management done well and there are more than enough management primers out there so this section will be brief. Most primers start with the truism of "Knowing thyself—and being ready for reinvention (Lublin, 2010: p. D4)." Management functions center on planning, organizing, directing-leading, controlling, and most importantly staffing. Get the people right and other issues matter much less (Service and Cockerham, 2007). One issue that must

be addressed is that most business writings are more descriptive than prescriptive. You need to understand the prescripts for doing the right things right. Drucker's 1973 classic *Management*, and Wren and Bedeian's 2009 *History of Management Thought* bring together what it takes to be an effective manager. These requirements are further revealed through the words of famed management professor and writer Henry Mintzberg:

> The practice of management is characterized by its ambiguity. . . . That leaves the managers mostly with the messy stuff—the intractable problems, the complicated connections. And that is what makes the practice of management so fundamentally 'soft' and why labels such as experience, intuition, judgment, and wisdom are so commonly used for it (2004: p. 13). . . .Managing thus means engaging based on judgment, **rooted in context** (p. 275).

In global organizations management success is a prerequisite for the chance to lead (Service and Carson, 2010).

Relationship-practices: Relationships form the center of humanness and enduring ones must be based on mutual benefit and mutual trust (Covey, 1991). A successful leader, think win-win-win . . . and always ask but be willing to give before they take. Start by building as many relationships as possible and remember you are no stronger than your weakest relationships (Drucker, 2001).

Innovation-practices: The management guru of gurus, Peter F. Drucker, continually stressed "to not innovate is to die." And, Friedman in his 2005 and 2008 books clarifies "new" competitive worlds that require an innovate or die mindset. Friedman identifies our world as flat because we are now competing against everyone in the world. He says that we should not build walls, but dig our way out by acting small if we are big and acting big if we are small. Additionally, Friedman and Mandelbaum (2011) rightly proclaim, "Continuous innovation is not a luxury anymore—it is becoming a necessity. In the hyper-connected world, wherever can be done, will be done (p. 96)."

Freakonomics and *SuperFreakonomics* (Levitt and Dubner, 2005 and 2009) also present entertaining, yet eminently useful, findings. Both *Freaks'* six innovative themes are instructive for our Model: 1) Realizing that what we value, and how we value it, is not necessarily related to what others value or how they value it. 2) Recognizing that common sense has become uncommon. 3) Understanding that there are many simple explanations that are wrong. 4) Looking at what an advice giver has to gain. 5) Measuring something most often makes it improve—be sure what "it" is. 6) Knowing that unintended consequences run ramped regardless of "righteousness "of intentions.

Cohen's *Drucker on Leadership: New Lessons from the Father of Modern Management* (2010), does not sugar coat the fact that becoming a more effective leader is difficult and requires a lifetime of "innovation" coupled with energy and effort focused more on "doing than dash." Likewise, Collins and Hansen's *Great by Choice* (2011) which follows on to Collin's 2001, *Good to Great* can help the reader in discovering management and leadership principles starting and ending with innovation of self and one's organizations.

Wisdom: From Philosophy to Neuroscience (Hall, 2010) is an excellent book that rehashes research about neuroscience, and human success and wisdom as it has developed over the past 20 years. It ends with the challenge for us to dare to be wise. The need to become and remain innovative is laced throughout this book. "Balance is a persistent theme in the literature of wisdom (p. 203). . . . People do have the capacity to overcome emotional responses (p. 205)."

Robert J. Sternberg has written hundreds of articles and scores of books; and his *Wisdom, Intelligence, and Creativity Synthesized* (2003) adds must to the understanding of leadership wisdom (also see: Barney, 1995; Blanchard, et al, 2002; Drucker, 1985 and 1998; Porter, all; Service, 2010; and Tichy and Bennis, 2007). The key point here is to decide when to lead, when to manage, when

to form or enhance relationships and when to innovate: all informed by the central feature of our model – wisdom.

How can we apply, the so what?

In this sub-model we see applying all parts of the other two sub-models by using relevant earned and learned relational, management and leadership "wisdoms." Years of research, application, thought and work show that these "wisdoms" can NOT be reduced to principles or secrets presented by the rich and famous (Gladwell, 2008). Additionally, wisdom indicates that limited empirical evidence of limited principles cannot enable one to improve someone else's or their own global leadership effectiveness. Our new Model uses as much as possible from the useful but limited "principles and secrets" and combines that with solid research and experience to drive home the point that leadership effectiveness, especially at a global level, is a lifetime commitment or it is harmful. The leadership "wisdom" objective must be continuous improvement.

Effective learners can see wisdom revolves around: 1) understanding self, others and situations; 2) balancing goal achievements from many and varied perspectives; and 3) seeking "the common good through balancing of intrapersonal, interpersonal and extrapersonal interests over the short and long terms (Sternberg, 2003: p. 188)." Our Global Leadership Effectiveness Model (Figure 2) provides a roadmap towards becoming a cross-cultural leader capable of understanding the wisdom sweet-spot of varied reflections, perspectives and extro-and-introspections.

Conclusion

Everyone wants to feel needed and appreciated and they want something to build their lives around. Leaders have to give them those things and more importantly remember: "What people want in leaders today, more than ever before, is integrity—walking their talk, (p. xvii). . . . I have come to understand the truth behind the saying 'leaders aren't born, they are made (first unnumbered introductory page: Despain and Converse, 2003). This book is based on a lifetime of experiences and espouses that the key is values defined with shared beliefs coupled with standards for workplace behaviors. "Leadership is about others and not about self (p. xxii). . . . I give people freedom to handle work their own way, I listen more than I talk, I work with ever employee to create a development plan, and I say something positive to every employee in my group every day (p. 148)." Indeed, leaders must move from a control-based leadership to a values-based-leadership model.

Yes, leaders need enough intellect to handle the tasks, but they also must motivate, guide, inspire, listen, know how to gain consensus, teach and learn, innovate, anticipate and analyze. Leaders must ultimately move and act because beyond talent and principles lay all the usual words: discipline, endurance, love and luck. Life and its close subset, leadership are truly tests and they do not come with clear exact directions. The principles outlined within our Model can lead to a shift toward a more effective way of leveraging leadership in cross-cultural settings.

The long and winding road to leadership understanding and improvement has been crooked, crowded, rough, and bumpy; but the tough road unquestionably has led us to a greater understanding that allows for freedom of choice in striving for opportunity of success through fulfillment as a leader. The Models presented in this research help smooth the journey of navigating cross-cultural leadership challenges.

From Model 1 the reader should see precepts to develop and improve as well as measure leadership within cross-cultural contexts. Figure 2 reveals the three blocks of overall leadership effectiveness and their individual sweet-spots of: 1) reflection and introspection; 2) Extrospection and perspective; and 3) useful application resulting in a multiplicitic wisdom that is truly a wisdom which changes with who you are, who they are and with differing cross-cultural situations. As leaders, followers, and markets become more diverse it is imperative that effective cross-cultural leadership emerge as rule and not the exception. Without organizational investment in developing a new generation of leaders that understand the complexities of managing across cultures, success in the new global economy is virtually impossible. However, organizations that embrace the challenge of cross-cultural leadership will be poised for a bright future.

Though much work has yet to be done and there are weaknesses in this current research, please do not fail to use insights you might glean from this work.

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Online Optimization by Safeguarding Brand Domain Names for European Tourism Destination Countries

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Abstract

While country destinations have web addresses relating to publicity in the global marketplace, utilization processes from countries' geographic names to be registered in English with certain unrestricted generic top-level domain extensions is a considerable posture not only for both online effectiveness but also serves as a safeguard for protecting their destination brand names. As such, in this paper we undergo a research on the European Union countries' names (both members and candidates) within the scope of exploring the differences on the level of online optimization by safeguarding destination brand names. Moreover, we conduct a research of the reverse relation between the online effectiveness and relative economic size of various countries. The findings prove that some EU destination countries seem to be profoundly unsuccessful when it comes to safeguarding their online destination brand names. With reference to the results, we pinpoint the possible reasons, and thus, hopefully this study will provide a basis to further studies focusing on the speculation of brand names.

Keywords

Destination, optimization, online branding, domain, European Union

1. Introduction

Online branding literature underlines that many organizations use a corporate brand web site (Leitch and Richardson, 2003) in terms of the opportunity for building enhanced trust and relationships (Xie and Boggs, 2006). Accordingly, from our point of view, destination countries with unique, touristic, historical and cultural diversity should match their web addresses (URLs) with own brand name as part of a mainstay to their online branding strategy. Investing in brand names offers an opportunity to extend the brand over a wide range of relative merits, and is therefore more efficient.

Having the best web addresses/URLs' portfolio is possible by ownership (i.e. registering or buying in the domain aftermarket) of all available unrestricted domain extensions. This can increase the likelihood of locating the brand web sites. Failure to acquire the domain names leaves the brand's equity susceptible to sabotage by competitors, adversaries and proactive entrepreneurs (Hanson, 2000; Ries and Ries, 2000).

Indeed, the consistency between a destination's web domain names and brand name lies in its widespread recognition. This realization can employ an online success even though the domain names can be registered by any individual, company and governmental or non-governmental organizations.

We encounter extreme and different prices in the domain speculation market (aftermarket) as seen from the examples in RealTimeDomains.com's reports (2012) regarding to the country names such as Israel.com (sold for 5.88 million USD) and Zimbabwe.com (sold for 130.000 USD). When "zimbabwe.com" is taken into consideration, it is observed that the portal serves its own country tourism, whereas "Israel.com" is still inactive, possibly because the portal is held by a competitor or another domain speculator.

In exploring online optimization measurement today, the destinations need to be sensitive to two basic components which lie in the following:

- How successfully and efficiently can destination countries establish online presence and spread their own accurate images to the intended target net surfers in the global marketplace?
- Which domain addresses could be more useful for drawing attention of the surfers and provide online brand loyalty?

Taking the components above into a consideration the research question progresses. Indeed "on which domain extensions should the destination countries focus for online optimization in order to protect online brand names?" As such, this paper is the outcome of this research question that focuses on the destinations' response to brand domain names.

2. Literature Review

In order to perform research questions and research design in the study, the literature review contents were categorized into two categories, namely, destination branding in the online platform and organizational optimization.

2.1. Destination branding in the online platform

A tourism destination including tourism products such as support services and attractions and tourist resources has physical and administrative boundaries defining its management, and images and perceptions defining its market competitiveness (UNWTO, 2007). It is evident that a unique combination of tangible and intangible characteristics with values represents the brand. Morgan et al. (2003) stress that a brand is one of the most powerful marketing 'weapons' that a destination protector can use to influence potential tourists.

The UNWTO (2007) indicates that as a point of departure, destination brands provide a range of benefits which circle stimulating destination awareness, also, demand creation and transaction; generate customer loyalty; serve as a basis to co-ordinate private sector initiatives; act as a tool to encourage seamless marketing tools and assist by being an image enhancement tool for other economic sectors in any destination (Tourism KwaZulu-Natal, 2008).

Harris and Goode (2004), state that trust is essential for online brand loyalty. In relation to this, Ibeh et al. (2005) argue that the trust is as expected more significant in the virtual world as compared to the real world. Doney and Cannon (1997) emphasize that the notion of trust is applicable in condition of uncertainty. Subsequently, consumers feel comfortable when faced with trusted brands because trust increases their confidence level in an uncertain environment (Chaudhuri and Holbrook, 2001).

Aaker (1996) declares that brand trust goes beyond the consumer's satisfaction by way of functional performance of the product and its attributes. Matzler et al. (2008), on the other hand, emphasizes that brand trust is the key variable to maintain evolving relationships with customers, which sequentially lead to brand loyalty. In addition, trust is often conceptualized as encompassing perceptions of honesty/integrity, reliability/dependability, responsibility, and positive motives/intentions (Smith, 1997).

In brief, trust is as anticipate more significant in the virtual world where the web has become one of the most effective and direct delivery medium for external communication. Both Argenti (2003) and Goodman (2004) state that a proper website benefits an organization in the way of coherent identity, positioning, culture, and corporate citizenship. In this situation, websites serve as a distinctive feature of relationships in influencing consumers' interaction with a brand. However, web domain names provide a notable difference in a website's success (Lawson, 2000). Moreover, the semantic dimension allows web domain names to act not only as unique addresses, but also as slogans, billboards, or brand names (Burk, 1995). Indeed, as is indicated in Hashim and Murphy' study (2007), offline, and even more so online, brands are important to consumers; online consumers substitute brand names for product information (Ward & Lee, 2000). In their view, branded websites increase online familiarity and confidence. Besides, Murphy, Raffa, & Mizerski's study (2003) that highlights the importance of using branded domain names, Murphy, Olaru, Schegg, & Frey (2003) and Murphy & Tan (2003) suggest that their use may reflect advanced Internet adoption.

An effective online strategy allows existing or potential visitors remember or guess the correct website address (Ilfeld & Winer, 2002). Indeed, some well-known companies and destinations (i.e. www.panasonic.net, www.dell.com, www.finland.com, and www.spain.info) supply their own names in web addresses, so there is no need to search for the address in a search engine.

According to Leng (2010), choosing the right keyword for a domain name is vital as it leads to search engine optimization (SEO). Recent research by Cutrell & Guan (2007) found that users spent between 22% and 25% of their time viewing the domain name in search engine results. Nielsen

(1999) asserts that users are interested in domain names when assessing the credibility of a destination.

2.2. Organizational optimization

Effective positioning on the internet is a goal for destinations to be successful in relation of organizational effectiveness in today's competitive world. In the optimization literature, as a broad term, organizational effectiveness is the extent to which an organization has encountered its stated goals and objectives and how well it is performed in the process (Yankey & McClellan, 2003). It can be perceived from the literature that the *"Goal Approach"* theory, based on the purposive-rational approach by Pfeffer (1982) and the managed systems idea by Elmore (1978) represent the basic model of effectiveness. The theory is based on the accepted idea which implies that all organizations possess goals which in themselves shift to criteria to be used to measure effectiveness. Needless to say that, this popular theory has its limitations. Some argue that people, not organizations, have goals. Others state that goals lack specificity, prioritization, and ignore unofficial, but essential, goals. As a result, the "*Goal Approach"* theory is fit and proper to assess a destination's organizational effectiveness in the context of online effectiveness. On the other hand, as is procured from Herman & Renz's studies (1997; 2004) most organizations can utilize more specific and current theories when assessing effectiveness.

3. Online Optimization by Protecting Brand Domain Names

If the goal is just to be seen online and establish online presence, there are many ways to do so. To name a few, placing ads and promotions, setting up or participating in online communities, and using e-mail and also creating a website (Armstrong & Kotler, 2008). As a popular social networking and micro blogging service, Twitter can be used to broadcast the destination's latest news and blog posts, interact with its customers, or to enable easy internal collaboration and group communication. In this sense, destinations do not need a domain name to go online. Namely, websites such as Yahoo, Lycos and Geocities offer free, albeit limited space, for hosting websites. Yet, a website address from these free services, such as "http://dir.yahoo.com/countries/turkey/", is difficult to type and hard to remember. Furthermore, when compared with "www.turkey.com", the free website address inspires less trust.

Registering a domain name is the starting point when procuring a website. In other words, it is the first step towards establishing an ''online presence' by creating a website (German, 2010; Leng, 2010). A domain name is a unique text-based internet address and the pointer to a website. Hence, it is essential to select the right domain name. A good example of a country domain name would be "www.belgium.com", where www stands for "World Wide Web", "Belgium" is the actual domain name, and ".com" is the extension. In brief, a domain name enables people to easily find a site without having to memorize a complicated number combination (*Internet Protocol*-IP address).

In short, the likely benefits of these top-level domains—ranging from new branding and destination introduction and marketing opportunities to enhanced brand name protect—are substantial providers.

3.1. Unrestricted generic Top-Level Domains (gTLDs)

The right domain name is prime "virtual" real estate that can leverage a destination country's visibility. When introducing the gTLDs which is accessible to everyone we can say that information

regarding to the existing gTLDs such as ".COM" appears in the IANA Root Zone Database. There are 323 top-level domain names directly under the domain name system root (IANA, 2011). Top-level domains are categorized further as either Country Code Top-Level Domains (ccTLDs) or gTLDs; of which there are sponsored top-level domains and unsponsored top-level domains. Table 1 refers to the comprehensive list of top-level domain names excluding the internationalized domain names (IDNs) which appear in the reserved stage for testing.

Table 1: List of top-level domains (TLDs)

Top-Level Domains		
Country Code TLDs	**Sponsored TLDs**	**Generic and generic-restricted TLDs**
.ac .ad .ae .af .ag .ai .al .am .an .ao .aq .ar .as .at .au .aw .ax .az .ba .bb .bd .be .bf .bg .bh .bi .bj .bm .bn .bo .br .bs .bt .bv .bw .by .bz .ca .cat .cc .cd .cf .cg .ch .ci .ck .cl .cm .cn .co .cr .cu .cv .cx .cy .cz .de .dj .dk .dm .do .dz .ec .ee .eg .er .es .et .eu .fi .fj .fk .fm .fo .fr .ga .gb .gd .ge .gf .gg .gh .gi .gl .gm .gn .gp .gq .gr .gs .gt .gu .gw .gy .hk .hm .hn .hr .ht .hu .id .ie .il .im .in .io .iq .ir .is .it .je .jm .jo .jp .ke .kg .kh .ki .km .kn .kp .kr .kw .ky .kz .la .lb .lc .li .lk .lr .ls .lt .lu .lv .ly .ma .mc .md .me .mg .mh .mk .ml .mm .mn .mo .mp .mq .mr .ms .mt .mu .mv .mw .mx .my .mz .na .nc .ne .nf .ng .ni .nl .no .np .nr .nu .nz .om .pa .pe .pf .pg .ph .pk .pl .pm .pn .pr .ps .pt .pw .py .qa .re .ro .rs .ru .rw .sa .sb .sc .sd .se .sg .sh .si .sj .sk .sl .sm .sn .so .sr .st .su .sv .sy .sz .tc .td .tf .tg .th .tj .tk .tl .tm .tn .to .tp .tr .tt .tv .tw .tz .ua .ug .uk .um .us .uy .uz .va .vc .ve .vg .vi .vn .vu .wf .ws .ye .yt .yu .za .zm .zw	.aero .asia .cat .coop .edu .gov .int .jobs .mil .mobi .museum .tel .travel .xxx	Arpa (infrastructure) .biz (ge-restricted) .com (generic) .info (generic) .name (ge-restricted) .net (generic) .org (generic) .pro (ge-restricted)

As seen in table 1 the domain extension/suffixes, the last 2 or 3 letters trailing a domain name refer to the location or status of the registrant. The extensions are used for multiple purposes: commercial ".COM", ".NET", organizations ".ORG", informational ".INFO", and business ".BIZ". Some gTLD such as ".TRAVEL", are reserved for entities whose primary area of activity is in the travel industry. Country Code Top-Level domains (ccTLDs) are two-letter top-level domains especially designated for a particular country or autonomous territory implemented to service their community (IANA, 2011). For example, the .FR ccTLD is an extension that represents France. Individuals and companies located in France can register ".FR" domain names. As is widely acknowledged, a ccTLD is an internet top-level domain generally used or reserved for individuals, companies, corporation or organizations of a country.

However, registration of some country domains is open to everyone worldwide following a basic procedure. For example, although the ".TV" ccTLD is an extension that represents Tuvalu, there are no local presence limitations for the registration and anyone can register on a first-come, first-served basis. Namely, the .TV was originally the ccTLD for the island of Tuvalu. It is now more commonly used for domains related to video, television broadcasting and webTV. The ".EU" as a ccTLD is eligible for any individual or organization residing within the European Union. The ".EU" domain names are available on a first-come, first-served basis. Although many ".EU" names are available, sometimes a name is unavailable. For example, a name could has been blocked or reserved by the European institutions, EU Member States, EU Candidate or Members of the European Environment Agency.

The Internet Corporation for Assigned Names and Numbers (ICANN) has announced a plan on 16 June 2008 which will allow for a virtually unlimited number of new gTLDs (Talley, 2011). Apparently, the new system will expand popular domains such as ".com", ".net" and ".org" to include new generic, brand, geographic, ethnic, community, and specialized domain name extensions. It would be possible to have domain name extensions such as ".london", ".peace", ".panasonic", and ".hotel". New domain suffixes would also include Arabic, Chinese, Spanish and other scripts.

Applications for the first round were available from January 12, 2012 and will close on April 12, 2012. However, if an applicant has applied for a gTLD string that is a geographic name (country or territory names), the applicant will not be approved, as country or territory names are not available under the new gTLDs program in this application round. As is emphasized in ICANN's new gTLD Applicant Guidebook (2011), country and territory names are excluded from the process based on the advice from the Governmental Advisory Committee. It is apparent that, ICANN's new gTLDs program doesn't provide any purpose for the destination countries within the context of protected brand or new extension options.

In conclusion, for destination countries, having an ideal domains portfolio by ownership (by registering or buying in domain aftermarket) of all available unrestricted domain extensions offers a good start of online optimization by protecting destination brand online which in itself is a desirable feature. Failure to defensive registrations leaves the brand's equity susceptible to sabotage by third parties.

In the tourism literature, no research is available that supports online optimization of any destination countries by protecting brand domain names. This paper aims to fill this gap by developing a scale model of online optimization based on available domain extensions. While drawing attention to the certain domain extensions, notably we aim to employ this paper as a basis for further studies on brand domain name speculation, and also adopt different approaches on effective positioning on the Internet.

4. Methodology

It is quite clear that if the goal of destination countries is online effectiveness by creating websites, they should have own brand domain names with available domain name extensions. The most popular ones to register with simple procedure domain extensions out of the countries' own country-code Top-Level Domains (ccTLDs) like ".PL" (Poland) and ".IT" (Italy), in order of popularity, are ".COM", ".TRAVEL", ".ORG", ".INFO", ".EU", ".BIZ", ".NET", ".TV", and ".CO". Considering the relevant usage of EU countries' domain names in English with the above-stated popular domain extensions, we aim to reach some findings to secure the attention of each destination's protectors such as public tourist organizations or destination management organizations (DMOs).

To be able to achieve a score of assessing on online optimization by creating web sites for European Union destination countries (EUCs), we assign a point to each domain extensions according to their usage majority as the suffixes of the web addresses including the brand names. As stated in table 2, ".COM" is the most preferred and popular domain extension whereas ".CO" is the exact opposite, and also ".TV" is not frequently favoured. When a country enjoys active websites relevant to the country with these ten domain extensions, the total effectiveness success is 100 % with 55p. The relative share of each extension of favorable outcome is also given in the table. With a five-point scale, the points are labeled as (01 to 11p) *miserable*, (12 to 22p) *worthless,* (23 to 33p) *mediocre*, (34 to 44p) *good*, and (45 to 55p) *very good*.

Table 2: The ten popular TLDs' consisted scores

Popular gTLD extensions	.com	ccTLDs	.travel	.org	.info	.eu	.biz	.net	.tv	.co	TOTAL
Scoring	***10p***	***9p***	***8p***	***7p***	***6p***	***5p***	***4p***	***3p***	***2p***	***1p***	***55p***
	18%	***16%***	***15%***	***13%***	***11%***	***9%***	***7%***	***5%***	***4%***	***2%***	***100%***

On the other hand, as it is detailed below, Google performance is also calculated with the same scoring method within the context of the first page projecting results of the EUCs' names (Italy, France etc.) search.

4.1. Scoring of online optimization

To carry our research within 31 EUCs we typed all EUCs' names in English with ten extensions directly to the browser (Internet Explorer) as seen in Italy sample *(www.italy.com, www.italy.org, www.italy.travel, www.italy.ne, www.italy.eu, www.italy.biz, www.italy.info, www.italy.tv, www.italy.co, www.italy.it)* and checked whether they are active with relevant content for online tourism publicity. At this juncture, since this study's aim is not a comprehensive content analysis of the websites, we only had a brief look at their homepages containing certain elements to capture visitors' interest promptly. As a result, we created table 4 which is relevant to the success levels of the countries in effective online positioning.

4.2. Scoring of Google performance

Inarguably, Google is the market leader for web search in most (Western) countries (Beel at al., 2010). Taking the United Kingdom (UK) as an example for EUCs, Google dominates 91.02 percent share of searches, while Yahoo in third position captures 2.79 percent of searches in the country. Besides, in the U.S.A., Google grew by 65.6 percent, Yahoo fell to 15.2 percent, whereas Bing grew by 14.8 percent, Ask fell to 2.9 percent and AOL held steady at 1.5 percent (Goodwin, 2011). All this reveals that Google's performance in EU countries, namely, in order to determine which countries are shown on Google's first page, we type on Google search box the country names in English. Thus table 5 was created to expose actual Google performance of the countries, and also to see the domain name attributes of the destination country websites on Google's first page periodically.

4.3. Cross-sectional analyses of the destination countries

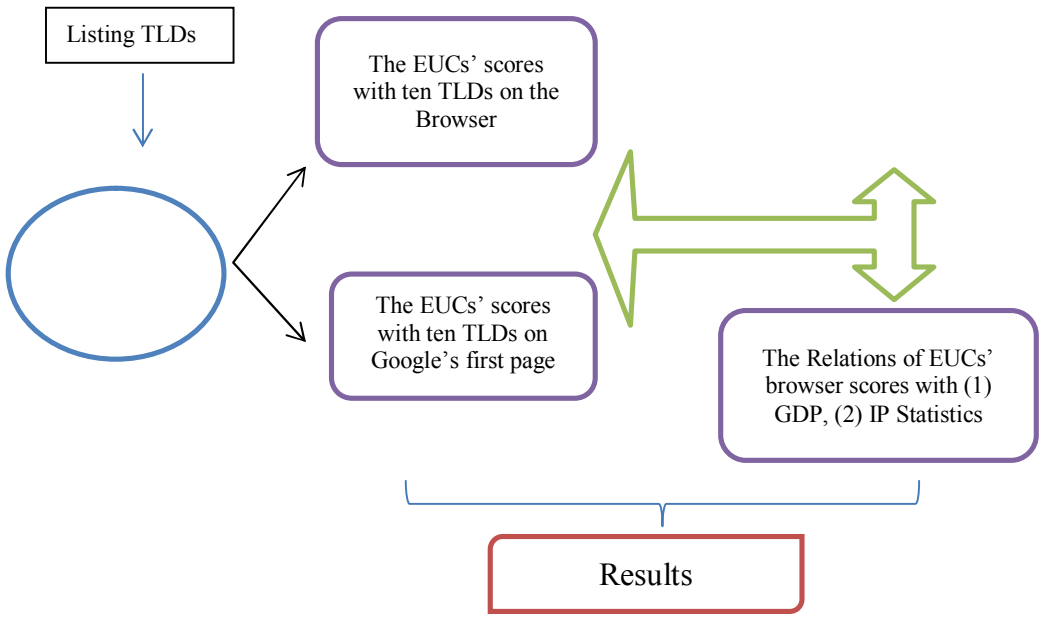
To gain a theoretical standpoint to the online optimization searches depending brand equity of generic domain names, we assert that more developed EUCs are unsuccessful to assure optimum presence online by protecting own brand domain names within the framework of destination's organizational success. It could be claimed that a speculative interest on country domain names is not independent from their socio-economic size.

To test this assumption we search the relation among the online optimization of the brand domain names (countries) and Gross Domestic Product of the countries (GDP) and also Internet Penetration (IP) by using cross-sectional data. It is widely recognized in the literature that heteroscedasticity often arises in the analysis of cross-sectional data. There are several methods of testing for this presence and one of the most common is the White's General Test (White, 1980). In short, the heteroscedasticity problems are searched by using White's General Test. White Heteroscedasticity Consistent standard errors & Covariance is selected for the regression estimation in order to eliminate possible distortion. On the other hand, the variables and values used for the White's General Test are demonstrated in table 3 and the steps of the research process are summarized in frame 1. For the analysis, Eviews 7 statistical software is used and the results are shown in table 7.

Table 3: GDP and IP statistics of 31 EUCs

Member and Candidate Countries of the EU	**GDP (US$ billion)**	**Internet Penetration (% 2010 Est.)**
Austria	405681	74
Belgium	499397	77
Bulgaria	52996	47
Cyprus	25022	43
Czech Republic	218363	65
Denmark	337811	85
Estonia	20325	75
Finland	260382	85
France	2751000	69
Germany	3519000	79
Greece	310365	46
Hungary	133677	61
Ireland	212792	65
Italy	2181000	49
Latvia	26141	68
Lithuania	40333	59
Luxembourg	61580	84
Malta	8985	58
Netherlands	823160	88
Poland	497976	58
Portugal	236146	48
Romania	174429	35
Slovakia	95177	74
Slovenia	50698	64
Spain	1485000	62
Sweden	544716	92
United Kingdom	2472000	82
Croatia	65137	50
Macedonia	10113	50
Iceland	13815	97
Turkey	795605	44

Frame 1: Steps of the research process



5. Findings

The popular domain extensions such as ".COM", ".TRAVEL", ".ORG", ".INFO", ".EU", ".BIZ", ".NET", ".TV", and ".CO" with the countries' own online codes (ccTLDs) should be registered on a first-come, first - served basis in order to establish online optimization by protecting brand domains. Acquiring each of them can help the destination countries to receive position at segmented visitor base or to direct them all to the same website to maintain brand consistency.

There are also unrestricted extensions which are not limited with the above mentioned, such as ".CC", ".ME", ".TK", ".TW", ".VG", ".WS", and ".ES". Although these extensions are not as popular as before, it could be better to acquire also these extensions to prevent abuse of third parties. Tourist destination countries, such as Turkey, acquiring ".ES" extension, can create for example "www.turquia.es" and can take advantage in the Spanish tourism market.

As can be seen from table 4, many EUCs don't possess the brand names when taking ten domain extensions into a consideration. The score of online optimization as an average of EUCs is "*worthless".* On the other hand, table 4 also shows that the most successful countries when it comes to domain extensions are respectively Denmark, Poland, Austria and Finland.

Table 4: The EUCs' scores with 10 TLDs on the browser

Popular gTLDs extensions →	.com	ccTLDs		.travel	.org	.info	.eu	.biz	.net	.tv	.co	TOTAL		
	10p	***9p***		***8p***	***7p***	***6p***	***5p***	***4p***	***3p***	***2p***	***1p***	***55p***		***100%***
Austria	+	*au*	+	+	+							4	31p	56%
Belgium		*be*		+				+				3	19p	35%
Bulgaria		*bg*										1	9p	16%
Cyprus	+	*cy*	+				+					3	22p	40%
Czech Republic	+	*cz*	+									3	27p	49%
Denmark	+	*dk*	+	+	+			+				6	43p	78%
Estonia		*ee*				+						1	5p	09%
Finland	+	*fi*		+		+						4	31p	56%
France		*fr*										1	9p	16%
Germany		*de*	+		+	+						3	19p	35%
Greece	+	*gr*										1	10p	18%
Hungary	+	*hu*		+								3	26p	47%
Ireland	+	*ie*	+									3	27p	49%
Italy		*it*										1	9p	16%
Latvia		*lv*	+									2	17p	31%
Lithuania		*li*	+									2	17p	31%
Luxembourg	+	*lu*				+						3	24p	44%
Malta	+	*mt*					+	+				3	17p	31%
Netherlands	+	*nl*										2	19p	35%
Poland	+	*pl*	+			+	+					5	36p	65%
Portugal	+	*pt*	+	+								3	25p	45%
Romania		*ro*	+	+								2	15p	27%
Slovakia	+	*sk*	+	+								3	25p	45%
Slovenia		*sl*			+	+			+			3	13p	24%
Spain	+	*es*			+		+					4	29p	53%
Sweden		*se*			+							2	15p	27%
England/UK	+	*uk*										1	10p	18%
Croatia	+	*hr*	+									3	27p	49%
Macedonia	+	*mk*		+	+							3	23p	42%
Iceland		*is*	+	+								3	24p	44%
Turkey		*tr*										-	-	-
TOTAL/MEAN	***18***	***18***		***14***	***10***	***7***	***6***	***4***	***3***	***1***	***0***	***8 1***	***20p***	***36%***

As a result, this paper projects that many destination country names are not actively participated in the online marketplace although all of them have been already registered almost two decades ago (e.g. ".COM" extension, www.turkey.com, Created on: 18 May 1995, www.italy.com, Created on: 15 July 1998).

According to the results regarding Google performance of the EUCs with brand domain names demonstrated in table 5, the score as an average appearing on Google's first page is *"miserable"*.

Table 5: The EUCs' scores with 10 TLDs on Google's first page

Popular gTLDs extensions →	.com	ccTLDs		.travel	.org	.info	.eu	.biz	.net	.tv	.co	TOTAL		
	10p	***9p***		***8p***	***7p***	***6p***	***5p***	***4p***	***3p***	***2p***	***1p***	*55p*		*100%*
Austria		*au*			+	+						2	13p	24%
Belgium		*be*	+									1	9p	16%
Bulgaria		*bg*										-	-	-
Cyprus	+	*cy*										1	10p	18%
Czech Republic		*cz*	+									1	9p	16%
Denmark		*dk*	+		+							2	16p	29%
Estonia		*ee*					+					1	5p	09%
Finland	+	*fi*	+		+							3	26p	47%
France		*fr*										-	-	-
Germany		*de*		+		+						2	14p	25%
Greece	+	*gr*										1	10p	18%
Hungary	+	*hu*										1	10p	18%
Ireland	+	*ie*										1	10p	18%
Italy		*it*										-	-	-
Latvia		*lv*		+								1	8p	15%
Lithuania		*li*										-	-	
Luxembourg	+	*lu*										1	10p	18%
Malta	+	*mt*										1	10p	18%
Netherlands		*nl*										-	-	-
Poland	+	*pl*	+	+								3	27p	49%
Portugal	+	*pt*			+							2	17p	31%
Romania		*ro*			+							1	7p	13%
Slovakia	+	*sk*		+	+							3	25p	45%
Slovenia		*sl*				+						1	6p	11%
Spain		*es*				+						1	6p	11%
Sweden		*se*	+									1	9p	16%
England/UK		*uk*										-	-	-
Croatia		*hr*	+									1	9p	16%
Macedonia	+	*mk*			+							2	17p	31%
Iceland		*is*	+									1	9p	16%
Turkey		*tr*										-	-	-
TOTAL/MEAN	11	8		4	7	4	1	0	0	0	0	35	8p	***17%***

Table 6 reflects a view on the domain name compositions as keyword or descriptive domains. The EUCs secured 10 keyword domain names and 21 descriptive domains in 2010, while they had 8 descriptive domain names and 23 keyword domains in 2011. Taking these changes into

consideration it could be claimed that branded keyword domains have become more popular in the progress.

Table 6: Googles' access in comparing EUCs keyword websites and descriptive ones

EUCountries	**Web Adresses (may 2010)**	**Domain Attributes**	**Web Adresses (September 2011)**	**Domain Attributes**
Austria	www.austria.info	Keyword	www.austria.org	Keyword
Belgium	www.visitbelgium.com	Descriptive	www.belgium.be	Keyword
Bulgaria	www.bulgariatravel.org	Descriptive	www.bulgariatravel.org	Descriptive
Cyprus	www.visitcyprus.com	Descriptive	www.cyprus.com	Keyword
Czech Republic	www.czechtourism.com	Descriptive	www.czechrepublic.cz	Keyword
Denmark	www.visitdenmark.com	Descriptive	www.visitdenmark.com	Descriptive
Estonia	www.visitestonia.com	Descriptive	www.estonia.eu	Keyword
Finland	www.visitfinland.com	Descriptive	www.finland.com	Keyword
France	www.france.com	Keyword	www.franceguide.com	Descriptive
Germany	www.germany-tourism.de	Descriptive	www.germany.travel	Keyword
Greece	www.gnto.gr	Descriptive	www.greece.com	Keyword
Hungary	www.hungary.com	Keyword	www.hungary.com	Keyword
Ireland	www.tourismireland.com	Descriptive	www.ireland.com	Keyword
Italy	www.italiantourism.com	Descriptive	www.italiantourism.com	Descriptive
Latvia	www.latviatourism.lv	Descriptive	www.latvia.travel	Keyword
Lithuania	www.visitlithuania.net	Descriptive	www.visitlithuania.net	Descriptive
Luxembourg	www.visitluxembourg.com	Descriptive	www.luxembourg.com	Keyword
Malta	www.visitmalta.com	Descriptive	www.malta.com	Keyword
Netherlands	www.holland.com	Keyword	www.holland.com	Keyword
Poland	www.poland.pl	Keyword	www.poland.com	Keyword
Portugal	www.portugal.org	Keyword	www.portugal.com	Keyword
Romania	www.romaniatourism.com	Descriptive	www.romania.org	Keyword
Slovakia	www.slovakia.com	Keyword	www.slovakia.com	Keyword
Slovenia	www.slovenia.info	Keyword	www.slovenia.info	Keyword
Spain	www.spain.info	Keyword	www.spain.info	Keyword
Sweden	www.visitsweden.com	Descriptive	www.sweden.se	Keyword
England/UK	www.visitengland.com	Descriptive	www.visitengland.com	Descriptive
Croatia	www.croatia.hr	Keyword	www.croatia.hr	Keyword
Macedonia	www.exploringmacedonia.com	Descriptive	www.macedonia.com	Descriptive
Iceland	www.icetourist.is	Descriptive	www.iceland.is	Keyword
Turkey	www.tourismturkey.org	Descriptive	www.tourismturkey.org	Descriptive

Table 7 demonstrates that there is a reverse relation between the online optimization by protecting brand names and the relative economic size of the countries. The findings based on the cross sectional analyses prove statistically that more developed countries (GDP based) profoundly failed to protect their online brand names. On the other hand, despite of this significant but inversely relation statistically, the relation between the IP (Internet penetration) of the countries and their online optimization scores are not significant as it stands at 5% level.

Table 7: The White's General Test results of the relations of EUCs' browser scores with their GDP and IP statistics

Method: Least Squares
Sample: 1 31
Included observations: 31
White heteroscedasticity-consistent standard errors & covariance

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	102.3809	63.42057	1.614316	0.1177
GDP	-3.19E-05	1.40E-05	-2.279705	*0.0304
IP	1.791271	0.987982	1.813059	0.0806

R-squared	0.159108	Mean dependent var	200.9677
Adjusted R-squared	0.099044	S.D. dependent var	94.91592
S.E. of regression	90.09296	Akaike info criterion	11.93133
Sum squared resid	227268.7	Schwarz criterion	12.07010
Log likelihood	-181.9356	Hannan-Quinn criter.	11.97656
F-statistic	2.648984	Durbin-Watson stat	2.354372
Prob(F-statistic)	0.088382		

** Significant at 0.05 level*

6. Conclusion and Implications

More and more people view the web as a means of attaining tourism destination information. Websites provide instant information for today's researching consumers regardless of their geographic location. A keyword (memorable and as short as possible) domain name such as a country name has more chance to gain recognition because it sums up everything the country is, says, and does. Another major advantage of keyword based domain names is that the website including the keyword could drive a substantial part of search engine traffic. Creating a country domain with some popular extensions increases the trust and loyalty of visitors and that is the underlying principle of generating more tourist income.

According to the research findings regarding to the differences in the level of the effective online positioning by creating websites within the scope of EUCs, relevant usage of country names in English with certain gTLDs as web addresses (URL) is unproductive. On the other hand, the Google performance of the countries is miserable. The findings also reflecting the EU average that the organizational success of the countries as tourism destinations in online optimization should be reviewed by other researchers. When reverse relation between the online optimization and relative economic size of the countries are considered, the findings prove that some developed countries failed to protect their online destination brand names.

The picture of EUCs in this study should be considered as an indicator of the success referring to organizational destination effectiveness for decision makers of each country. This paper can also be employed as a model in the same way for destinations in different geographical dimensions (country, region, city, tourist routes, and attractions) consistent with an ever-growing newly established domain extensions which are open to everyone worldwide.

Naturally, this study is not without its limitations. Firstly, instead of including all unrestricted domain extensions, only 10 gTLDs were analyzed in the study. Secondly, existing but not activated domains for country promotions haven't been researched as to whether these domains were owed by

domain speculators. As such, how much money the speculators require for the domains and what the secondary domain market is like were not examined. In the future, such a study would give fresh insights to test a secondary domain market price which at this point in time is completely virgin territory in the literature.

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Globalization as a Driver for Innovation

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Abstract

This paper examines the critical role of globalization as a driver for innovation.The introduction of the global strategy quadruple model truly links the three known strategy perspectives (namely: industry competition, resources and institution views) and performance. The model could assist in advancing the cause of sustainable competitive advantages.

This study could assist scholars in addressing the important three research questions: (1) Why are some firms are more innovative than others? (2) What effect does product, firm, industry and market innovativeness have on business performance? (3) Does the link between innovativeness and business performance depend on all or some of the innovativeness factors of product, firm industry and market?

The presented set of four propositions, when tested,will result in a greater understanding of the links and relationship between a firm's global strategy,innovativeness and business performance. The quadruple model presented can be used to examine these relationships in general and in the context of innovation. It is anticipated that this work will assist researchers, business management and analysts in developing global innovation strategies.

Keywords

Strategy, innovativeness, product innovativeness, firm innovativeness, industry innovativeness , market innovativeness

Introduction

Globalization has become a phenomenon that brings the world closer through the exchange of goods and products, information, knowledge and culture. Over the last few decades, the pace of Globalization has become much faster and more dramatic because of unprecedented advances in technology, communications, science, transport and industry. Globalization has also been a catalyst or driver of advances resulting from innovation, that have required adjustments in strategy from competing firms and created significant challenges in the business environment. Clearly, management needs to understand the impact of globalization on innovation so that it can deal with the challenges more appropriately.

The literature refers to Levitt (1983), as the first scholar who used the term 'global' which has now become a mainstream term in the 1980s resulting in many firms transforming into 'global firms'. However, in 1985, Hamel and Prahalad (1985) developed a global competitive framework which pointed to a link between globalization and competition.

It is worth noting that the intensity of competition has been fuelled by the rise in globalization and has led to a marked increase in competitive challenges. Some of those challenges are concerned, to some extent, with getting products and/or services to the right place at the right time at the lowest possible cost. This surge in competitive intensity has been accompanied with an increase in the number of organizations that have realized that it is not enough to improve organizational efficiencies, but to explore the role of innovation in global sustainable competitive advantages.

Competitive advantages through intensive technological innovations have been noted by Yeung (1999) who proposed a link between competition and innovation. This means the link between competition and globalization proposed by (Hamel and Prahalad, 1985) together with link between competition and innovation proposed by Yeung (1999) should point to globalization as a possible driver for innovation. Firms embark on globalization in order to expand into foreign markets to enhance their innovative culture for a superior performance (Knight et. al., 2004). In other words, globalization has led to changes in the competitive environment in which firms operate.

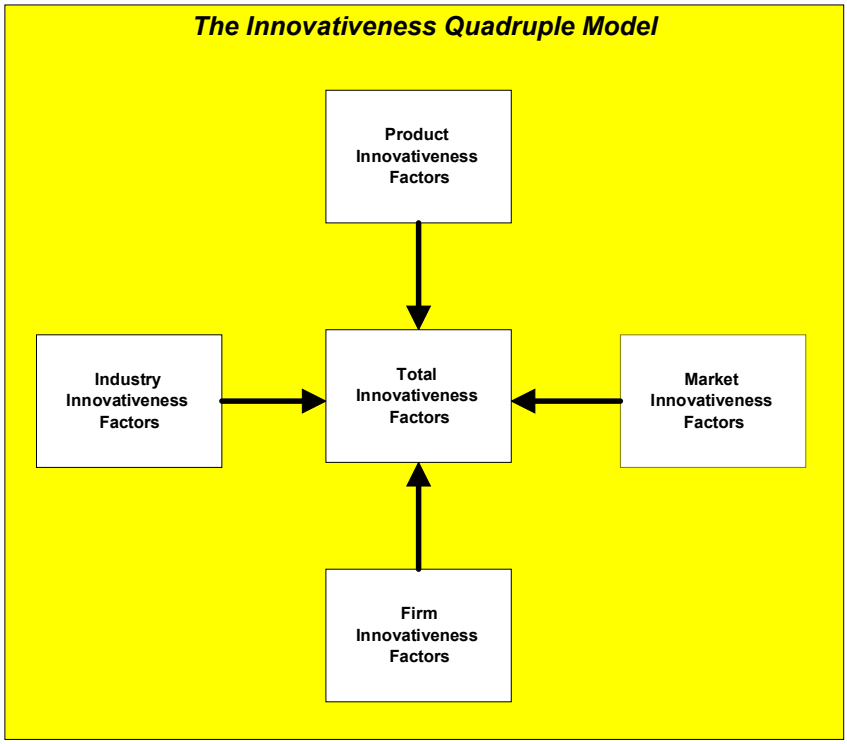
It is widely accepted that in the 21stcentury, globalization will be highlighted by rapid proliferation and diffusion of innovative technologies, products, and services, and the increasingly important role of innovation in catalyzing, shaping, and driving competitiveness.

However, the literature has focused on some aspects of innovation driven by competition, but ignored the role of globalization as a driver of innovation. Thus, the focus of this paper is the role of globalization as a driver of innovation. Innovations/ innovativeness is seen though two complementary viewpoints, namely *Competiveness* and *Globalisation*. The paper will also identify the critical factors and forces that fuel innovativeness.

Although culture is considered a part of international business research, it has not penetrated through to the global strategy of core research because of the reasons proposed by (Kogut and Singh, 1988; Shenkar 2001; Tihanyiet. al.,2005;Singh, 2007). It is important to mention that (Scott 1995) points to institutional issues, being broadly encompassed as cultural differences, through various aspects of institutional environments including innovativeness environments. Furthermore, other innovativeness issues such as product and firm innovativeness must also play a key role in forming the total environment of innovativeness. In other words the set of innovativeness factors must be interdependent on at least four sub innovativeness factors, namely: product, firm, industry and market innovativeness factors. It should be noted that the Porter diamond model (1990, 1998) refers to the firm's competitive advantage that is dependable on an important set of four environmental factors, namely, factors related to: a) Firm strategy, structure, and rivalry within one

country, b) Natural and human resource repertoires in a country, c) Related and supporting industries and 4) Domestic demand. However, in this research the total innovativeness factors are dependable on an important set of four innovativeness factors, namely, product, firm, industry and market innovativeness. The relationship between those four sets of sub innovativeness factors and the innovativeness factors may be described by the following diagram (Figure 1).

Figure 1: The Innovativeness Quadruple model.



In recent time, the institution-based view of global strategy has emerged suggesting that global strategy should incorporate a culture of innovativeness (Lee et. al. 2007; Meyer and Peng 2005; Peng 2002, 2003, 2007;Peng and Khoury 2008; Penget. al. 2008;Wright et al. 2005).

Various studies about the role of institutions in global competition suggest that the ability of the innovative firm to operate effectively inthe host market decreases (Gomez-Mejia and Palich 1997; Hennart and Larimo 1998). This may be due to an institutions distance in regards to innovation practices. However, there are other views that suggest that the innovativeness of the industry and the market could also contribute significantly to the uncertainty for managerial decision-making, which increases managerial risk due to innovation (Shane et. al. 1995). In contrast Soliman (2011a, 20011b) provided evidence that the process of innovation is a chain that encompasses three stages, knowledge management, learning organization and innovation management and that innovation is driven by competition.

This paper examines the environmental factors that could impact on the role of globalization as driver of innovation.

The Innovativeness Quadruple model

There is no universal agreement on the meaning of innovativeness and most authors consider innovativeness as a trait that is still under question. Subramaniam and Nilakanta (1996) defined

innovativeness as "*enduring organizational traits*" while Ettlie et. al. (1984) defined innovativeness as "*the propensity for a firm to innovate or develop new products*".

Innovativeness can be defined as the ability to create new products or services or management practices that bring about sound renewals and changes. In other words, innovativeness could refer to the organization's overall capability of introducing new product or service to the market, and or opening up new markets, through combining strategic orientation with innovative strategies and process (Wang and Ahmed, 2004). Hult, et. al. (2004) also defined innovativeness "*as postulate by the firm's capacity to engage in innovation*". Hult, et. al.(2004) have pointed out that most of the drivers of innovativeness still remain unknown. However, according to Verhees and Meulenberg (2004), innovativeness could also mean "*a willingness of the firm to learn about and to adopt innovations*". While most research in the field of innovation has been focusing on various aspects of innovation such as: Definitions, Measurement, Dimensions, Sources and Types, Influencing Factors and Competitive Advantages of innovation, the literature appears to have ignored the role of globalization as a driver for innovativeness (Hashim, et. al., 2003 and Mohamed and Rickards, 1996).

The fact that innovation is viewed as an element of competition is not a recent finding. Indeed Solo (1951) and Schumpeter (1982) are some of the earlier researchers who pointed to innovation as a competitive advantage of organizations. Recently, Das and Joshi (2007) also observed that the capacity of a company to innovate may lead to a competitive advantage. It should be noted that innovation requires resources for transforming the organization into an innovative firm. Therefore, the essential company's activities, such as innovativeness must also be assessed on the basis of the available resources for innovation.

In addition consumer behavior has been considered by many researchers as a force that could impact on the innovative behavior which ultimately could impact on the overall innovativeness of the firm (Roehrich, 2004). However, customers alone cannot drive innovativeness unless the firm and the industry and the market environments are supportive of innovation. In other words, if the innovativeness of the firm and the industry and the market are absent, the innovated product or the service is likely to face difficulty at the consumer level. The significance of the link between innovativeness and firm performance has been addressed recently by Rubera and Kirca (2012) who argued that "*innovativeness has direct positive effects on financial position and firm value*" and that innovation is increasingly seen as the key to unlocking competitive advantage, as much for countries as for companies.

It should be noted that innovation is in general a risky investment and that innovation is an element of competition for the company (Solo, 1951). In addition Lundvall, et. al. (1997), pointed to the link between innovation and competition and stated "*innovation is an instrument of competition for a company, that innovation could be influenced by competition*". This implies that changes in the competitive environments of a firm are likely to influence changes in its capacity to innovate. Lundvall, et. al. (1997) also argue that "*firms experiencing an intensified competition are much more prone to develop new products*". This could mean that changes in the intensity of competition of the environment could also impact on the firm's propensity to innovate. In other words, globalization which is widely been accepted as a driver for competition could also be a driver for innovation.

Therefore, it is proposed that the necessary innovation environments should also encompass the product innovativeness, firm innovativeness, industry innovativeness and market innovativeness. This article attempts to address the issue of innovativeness as a driver of innovation, which in turn drives globalization.

Product Innovativeness Factors

Daneels and Kleinsmith (2001) defined product innovativeness as ''*product that possesses newness or a degree of newness*". There is no consensus on either the definition of innovativeness or its roots. However innovation is generally regarded to relate to products and processes. Product innovation appears to be particularly important for international competition and economic growth. Accordingly, product innovation may be considered as "the development of new products, changes in design of established products, or use of new materials or components in the manufacture of established products".

The innovation based view of the firm, is that the firm's ability to develop a new or improved product may be affected by the availability of state of the art processes and equipment for the creation and production of the product newness. Therefore product innovativeness also presents opportunities for lowering costs and or enhanced quality and reliability of the new products. This could lead to enhancing, and possibly sustaining, the firm's competitive advantage.

According to White et. al. (1988), "Product innovativeness is the development of new products, changes in design of established products, or use of new materials or components in the manufacture of established products". White et. al. (1988) suggest that product innovation can be divided into two categories of innovation: development of new products, and improvement of existing products. Furthermore, the process of product innovativeness and the product development including bringing a new product or service to market has been described by White et. al. (1988) as "*a process that consists of two parallel sub-processes; namely idea generation and product design that involves detail engineering and market research and marketing analysis*". The process of product innovation could also be a process of launching or improving products to meet user needs. White et. al. (1988) consider improvement of existing products as also improvements in functional characteristics, technical abilities, or ease of use.

On the other hand, Kleinschmidt and Cooper (1991) argue that "*product innovativeness does not have a major impact on the rate of success in the marketplace*". They demonstrated that the relationship between product innovativeness and commercial success is U-shaped. They believe that "*both high and low innovativeness products are more likely to be more successful than those in-between*". Accordingly, past research has shown that moderately innovative, middle-of-the-road products are less likely to succeed when measured by a number of performance criteria.

It should be noted that product innovation implies difference and uniqueness while an improvement of existing product could be about meaningful differentiation of product. If the differentiation features are minor adjustments or small, it is referred to as "incremental" improvements rather than innovation. In contrast, new products or product innovation infers that the product newness creates or defines a category that meets consumer needs whether it is for new features or for insubstantial features, such as resalable or clear packaging.

Product innovation is considered by most scholars as a key component of many companies strategies. On one hand product innovation could lead to significant value creation as well as offering an opportunity for the firm to be the first mover in the market thus resulting in benefits to the firm. Additional benefits of product innovation could be through increasing the degree of differentiation with other competitors' products. Therefore, product innovativeness enhances the firm's competitive advantages. On the other hand it is often a risky endeavor. Accordingly, it possible to propose that innovativeness is related to product innovativeness as follows:

Proposition 1:

P[1]: It is proposed that innovativeness is interdependent on product innovativeness factors, which in turn are dependent on whether the product innovativeness conditions are either favourable or unfavorable.

Firm Innovativeness Factors

A number of authors have defined firm's innovativeness as being "*an organization's tendency to engage in and support new ideas, novelty, experimentation, and creative processes that may result in new products, services, or technological processes*" (Lumpkin and Dess, 1996). In recent time Jambulingamtet. al. (2005) noted that "*the concept of firm's innovativeness reflects an important way in which organizations treat and direct new opportunities*". However, it is possible to refer to a firm's innovativeness as the capacity of the firm to innovate or to maintain the capacity for organizational innovation.

According to Tidd, et. al. (2005), the competitive environment in which the company operates includes the internal resources and capabilities of the firm. However Das and Joshi (2007) pointed out that those resources and capabilities of the firm must facilitate innovation, which is considered a key competitive priority. Various other researchers such as Hurley and Hult (1998) have defined firm innovativeness as the firm's ability to develop and launch new products or services at a fast rate. Other researchers including Daneels and Kleinsmith (2001) defined product or service innovativeness as"*the degree of newness of a product or service*". While consumer innovativeness is defined by Midgley and Dowling (1978) as the tendency to buy new products or services more often and more quickly than other people. This implies, according to Rubera and Kirca (2012), that firm innovativeness indirectly affects firm value through its effects on market position and financial position. However, the characteristics of the firm in relation to external factors have been addressed by (Cavusgil et. al., 1993; Johnson and Arunthanes, 1995; Leonidou et. al., 2002; Menguc, 1997). Many researchers argue that a firm's international strategy should lead to sales growth (Johnson and Arunthanes, 1995; Leonidou et. al., 2002). In other words, this implies that most multinationals should consider their strategy as a facilitator for sales growth which ultimately should translate into higher return on investment as a result of expansion in global markets (Zou and Cavusgil, 2002). It should be also pointed out that a number of researchers including (Cavusgil and Zou, 1994; Johnson and Arunthanes, 1995; Leonidou et. al., 2002; Zou and Cavusgil, 2002) have argued that the firm's product strategy, including the product innovative strategy, affect the overall firm global strategy and ultimately the firm performance. This implies that the firm innovativeness factors could impact on the firm's overall global strategy. However, the firm innovativeness strategy may also be dependent on whether the firm innovativeness factors are favorable. Thus it is possible to propose the following:

Proposition 2:

P[2]: It is proposed that innovativeness is interdependent on firm innovativeness factors which in turn are dependent on whether the firm innovativeness conditions are either favorable or unfavorable.

Industry Innovativeness Factors

Cho and Pucik (2005) argued that innovation is a competitive alternative since the capacity of the firm to promote innovation is itself a competitive advantage. Furthermore, Cho and Pucik (2005) have considered the capacity of the firm to innovate as an intangible resource that is difficult to

imitate, and hence they considered innovation a sustainable competitive advantage. The findings of Cho and Pucik is consistent with similar findings in a large body of the literature that point to value, rarity, inimitability and use of the company's internal resources as pre-requisites for a sustainable competitive advantage (Barney, 1991; Grant, 1991; Peteraf, 1993). Other studies support the notion that the organizations should possess resources that the competitors cannot easily copy, acquire or buy since it could lead to obtaining a competitive advantage. Various other studies emphasized the importance of the resources and capabilities related to innovation inside the companies (Hamel and Prahalad, 1994; Tidd, et. al. 2005). In all of the studies mentioned, the resources and the company's capabilities for innovation have been shown to be essential elements of the generation of innovations.

According to Facó and Csillag (2010) "*some works sought to analyze the sources of innovations, or even innovative stimulus external to companies*". In this regards, Hippel (1988) identified three distinct sources of innovation: users, suppliers and manufacturing companies. Hippel (2007) has considered a "*user-driven innovation and knowledge diffusion"* line as a central activities for firm innovativeness. However, more recent refinements of Hippel's proposal (1988, 2007) points to exchange of knowledge between the innovative firm and the supplier and, and between the innovative firm and the user, as the key attribute of good innovations.

Another research study conducted by Abecassis-Moedas (2006) points to the influence of the firm innovativeness on other members of the innovation chain. In other words the industry innovativeness may linked to or dependant on the firm innovativeness. Accordingly, it is possible to propose the following:

Proposition 3:

P^3: It is proposed that innovativeness is interdependent on industry innovativeness factors which in turn are dependent on whether the industry innovativeness conditions are either favorable or unfavorable.

Market Innovativeness factors:

According to Hilmi (2008) and Schumpeter, (1942), "*Market innovativeness is highly connected to product innovativeness, and often studied as product-market innovativeness*". Other studies also refer to market innovativeness as "*the newness of approaches that companies adopt to enter and exploit the targeted market with emphasizes on the novelty of market oriented approaches*" (Ali, et. al., 1995). Furthermore, Ali,et. al. (1995) consider innovativeness as a "*market based construct and define innovativeness as the uniqueness or novelty of the product to the market*". While Andrews and Smith (1996) consider market innovativeness as innovation activities that is related to market research, and identification of new market opportunities. In this research, market innovativeness is considered as the newness of approaches that firms adopt to enter and exploit new markets. In other words, the product innovativeness could focus on product newness while the market innovativeness emphasizes the newness of marketing approaches. Therefore, it is accepted that innovativeness is difficult to operationalize due to inconsistencies in the definition of innovativeness by various scholars (Li, et. al., 2006; and Wang and Ahmed, 2004).

Increased international trade implies higher competitive pressure in the domestic market. This pressure may force firms to improve their efficiency or to switch to products in which they have a competitive advantage. However, greater economic openness also creates new business opportunities in foreign markets. With improved access to the international markets, firms can raise their sales and expand their production capacity to benefit from economies of scale, or explore new

product markets with better prospects. To analyze the impact of increasing globalization, we include a number of variables capturing various aspects of international trade.

Several contributions point to the importance of the effect of market innovativeness on business performance. For instance, Hilmi (2008) and Hult, et. al. (2004) noted that "*market innovativeness is an important determinant of business performance*". Their finding is consistent with earlier studies which confirm innovativeness as an important determinant of business performance.

It should be noted that, if market innovativeness is important for organizational performance, then it is imperative that firms' management should design and implement an organizational culture that embodies market innovativeness.

Proposition 4:

P[4]: It is proposed that innovativeness is interdependent on market innovativeness factors which in turn are dependent on whether the market innovativeness conditions are either favorable or unfavorable.

The Global Strategy perspectives

The influence of the "environment" in developing the firm strategy has long been featured in the literature (Lawrence and Lorsch, 1969). However, strategy research appears to focus primarily on economic variables such as market demand and technological change (Dessand Beard, 1984). In recent time researchers began exploring the interactions among institutions, organizations, and strategic choices (Peng, et. al. 2009; Narayanan and Fahey, 2005). Accordingly, a market-based institutional framework has been taken as a main feature of this strategy research. This means the impact of formal and informal institutional factors have been to some extent ignored or belittled. However the increasing need for firms to explore a range of strategic choices including innovation, means that strategy research is now considered one of the key four component of strategy. Accordingly, the development of global strategy should also include an innovation-based view as well as the other three views proposed by Peng, et. al (2009); namely industry based view, resource-based views and the institution-based view.

Global Strategy from Innovation perspectives

To some extent, innovationstrategies differs from other types of business strategies due to uncertainty. Uncertainty usually occurs as a result of inability to predict the impact of the innovation. Therefore many common approaches used to develop a business strategy are inappropriate for innovative businesses. Furthermore, innovative strategy guides decisions on how resources, including intangibles, are to be used to meet a firm's objectives for innovation, and thereby deliver value and build competitive advantages. Innovative strategy is regarded as strategic since it includes analysis of a company's competitive and technological environment; assessment of its external challenges and opportunities; and analysis of where its distinctive advantages lie. In other words, innovation strategies involve prioritizing and developing the right technological innovations by ensuring the appropriate resources, capabilities and processes are used to their best effect in delivering value.

Global Strategy from Industry competition perspectives

According to Soliman (2011a and 2011b), globalization has driven industry competition to new heights. The Porter model of 1980s has led to many management theories and in particular competition to be modified. One such model that has sprung out of globalization growth era of the 1980 is the Porter five forces of competition (1980). It is arguable that the five forces model has been the most widely used to assist firms in establishing competitive advantages. However, these theories were substantially modified over time. For example, the Adam smith Model of 1776 (Edwin Cannan, 1904) was followed by the Industrial Organization of 1930 (Hoskisson et. al, 1999). The Porter Five forces model of the 1980 (Porter, 1980) replaced the formers theories as more appropriate method for evaluating competition at that time. In recent times, Soliman, (2011a, 2011b)has shown that the competitive models need to incorporate the innovativeness of the firm. However this study proposes that analysis of the innovativeness ofa firm must be accompanied by analysis of the innovativeness of the industry where the firm belongs and the market where the innovated product will be released.

Clearly, the emergence of the porter model in 1980 signified a shift of policy makers' focus from understanding competition into making competition work. However as competition intensifies and the emergence of more advances in technology tools and processes coupled with advances in management research, it has become almost imperative for companies survival that they need to be innovative in order to sustain competitive advantage.

Some businesses consider moves and reacting to changes on the basis of competitor analysis should lead to several key decisions in strategic planning such as innovation. Davidson (1997) described how the sources of competitor information can be grouped into three data categories which was named by Davidson asa) recorded data, b) observable data and c) opportunistic data. In addition the resources and institutional issues ought to be considered almost at same time as the assessment of the competitiveness of the firm.

Global Strategy from Resources perspectives

A recent study conducted by Cho and Pucik (2005) characterised the capacity of a firm to promote innovation and creativity as a competitive advantage. Cho and Pucik defined the capacity of a firm to innovate as an intangible resource that is difficult to imitate. Furthermore innovativeness is, by definition, rare and possibly costly to imitate and is valuable. In other words, innovativeness could result in a sustainable competitive advantage (Barney, 1991; Grant, 1991; Peteraf, 1993).This means, firms are in facta mixed portfolio of products and resources and thus a firm's financials are directly related to its resources (Penrose, 1955; Rubin, 1973 and Wernerfelt, 1984). Therefore, it is possible to suggest that the greater the resources and distinctive capabilities that a company possesses, the better its performance will be.

A firm can be considered as more than an administrative unit, but a combination of productive resources(Penrose, 1995, p.61). The relationship between resources and the firm's innovativeness has been shown by a number of scholars, suggesting that for organizations to obtain a competitive advantage, they should possess resources that the competitors cannot easily copy, acquire or buy including resources and capabilities related to innovation inside the companies (Hamel and Prahalad, 1994; Tidd,et. al. 2005). The resources and the company's capabilities for innovation are essential elements for the generation of innovations and sustaining a competitive advantage.

Global Strategy from Institutional perspectives

According to Peng, et. al. (2009), "*the institution-based view is a third leading perspective in strategic management in addition to the industry-based and resource-based views*". Therefore, the institution-basedview in strategy complements the industry based and resource-based views.

While we discuss research one merging economies, we also point out the equally important ramifications of the institution-based view for research on developed economies. Combining the articulation of the two core propositions andthe efforts to address the four fundamental questions will be the first-time contribution this article makes to enrich the strategic management literature.

Peng et. al. (2009) propose that institutions matter. In addition, the institution-based view has also grown in response to scholars criticisms of the industry-based and resource-based views' as inadequate to define global strategy. The industry-based view, which deals largely with industry competition, has been criticized for ignoring histories and institutions (Narayanan and Fahey, 2005) and instead it focuses on the Porter's five forces, interfirm rivalry, and its prescription for a cost leadership strategy.

Similarly, the resource-based view has been criticized for failing to recognize that innovation, which is by definition valuable, rare, and hard-to-imitate, should be considered a key strategic choice for some firms. This means the rise of innovation in this global economy has attracted scholarly attention in strategy to focus on how innovation matters. The emergence of innovativeness as a key component in global strategy is similar to the emergence of the institution-based view in 2009 (Peng, et. al. 2009).

By arguing that the innovation-based view has emerged as the fourth component in the strategy development as proposed by the quadruple model, this article makes important contributions to strategy development of firms.

Conclusions

The rise of the innovation-based view can be viewed as a further development of the global strategy field that needs to embrace the proposition that innovation matter. The introduction of the global strategy quadruple model is truly a link between the three known strategy perspectives (namely, industry competition, resources and institution views) and performance, which will help advance the cause of sustainable competitive advantages.

This paper provides new evidence on the link between globalization and innovativeness, contributing to the literature in two important respects:

First, this paper is a study of the innovativeness factors that could impact on the development of the global strategy.

Second, the quadruple model could be used to analyze the innovativeness factors thus taking into account the dynamics of the competitive forces affecting the innovation.

This study could assist scholars in addressing the important three research questions: (1) Why are some firms are more innovative than others? (2) What effect does product, firm industry and market innovativeness have on business performance? (3) Does the linkage between innovativeness and business performance depend on all or some of the innovativeness factors of product, firm industry and market?.

The presented set of four propositions, when tested, will result in a greater understanding of the link and relationship between the firm's global strategy, innovativeness and business performance. The quadruple model presented can be used to examine these relationships in general and in the context of innovation. It is anticipated that this work will assist researchers, business management and analysts in developing global innovation strategies.

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Are Codes of Ethics Standardized? - A Comparative and Content Focused Analysis of Corporate Codes of Ethics of Hungarian Large Corporations

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Abstract

Codes of ethics set down ethic values, norms, principles and behavior rules. They contribute to clarifying what is considered as legitimate and responsible regarding the everyday corporate business life. After a revision of technical literature regarding the role of codes of ethics, this article examines some examples available on the internet of the first 50 companies from Hungary with the highest revenue. The content related comparison covers the Hungarian, American and Indian practice as well. The analysis can be thought-provoking for companies planning to conduct an institutionalization of ethics.

Keywords

Business ethics, corporate ethics, ethics management, ethics institutionalization, code of ethics

Introduction

A cardinal aspect of business ethics, more closely corporate ethics are the changes in corporate environment. They have induced certain processes as a result of which 'good companies' today are not only the ones that are successful in business, but the ones that are authentic and ethical, aiming to meet social expectations. Thus, optimizing the company's effects on those concerned and minimizing the harmful effects of its activities (*Epstein*, 2006).

Ethical behavior within an organization is affected by individual features on the one hand and organizational aspects on the (*Hassink-de Vries-Bollen*, 2007). Organizations can encourage ethical behavior either by a moral screening of their employees or by maintaining an environment which reduces the possibility of unethical (*Trevino*, 1986). Codes of ethics are the best known tools of developing moral environment and institutionalizing corporate ethics. According to some authors, they are an obvious feature of modern business organizations (*Cowton-Thompson*, 2000). A code of ethics is the public declaration of the principles and rules that determine business practices within and outside companies. It serves a guideline for both present and future behavior, it determines the ethical values and responsibilities of employees regarding each other and other stakeholders as well (*Kaptein and Schwartz*, 2008). Typically, it encourages self-regulation (*Schwartz*, 2001). The main challenge of codes of ethics lies in the process of creation, much rather than in recorded results. (*Newton*, 1995; *Ulrich-Lunau-Weber*, 1996).

The role of corporate codes of ethics

Kaptein és Schwartz (2008) have summarized different (often contradictory) opinions about the role and effect of corporate codes of ethics in their work which deals with the effectiveness of codes of ethics. According to some researchers, companies should have codes of ethics simply because it is right to do so (*L'Etang*, 1992), or because it is a way of declaring and managing their moral responsibility, in this way contributing to the solution of social problems (*Logsdon-Wood*, 2005).

Others, however, emphasize that a company can benefit from having a code of ethics. According to some early empiric surveys, the vast majority of managers asked believed that such codes have a positive effect on decision-making and corporate behavior. However, opinions regarding the extent of this effect differed (*Becker- Frietzsche*, 1987). *Singhapakdi and Vitel* (1990) examined employees dealing with marketing and found that those who had to adhere to a code of ethics were much more sensitive to ethical problems and often chose ethical solutions when making a decision. Codes of ethics maintain and improve the reputation of a company (*Bowie*, 1990), reduce the penalties given for breaking the law (*Pitt-Groskaufmanis*,1990), encourage courts to loosen regulations and control (*Clark*, 1980), increase organizational effectiveness (*Mezher-Jamali-Zreik*, 2002), and improve work atmosphere (*Manley*, 1991). Codes of ethics take responsibility off from simple individuals (*Schwartz*, 2000). They often make employees feel better and safer at their company, while customers and other stakeholders show a greater trust towards the company (*Wood*, 2000). Those who judge them positively believe that codes of ethics are necessary (*Rezaee, Z., Elmore, R. and Szendi*, 2001), important (*Cooper*, 1990), valuable (*Wood-Rimmer*, 2003), essential (*Coughlan*, 2005), invaluable (*Sethi*, 2002), and successful (*Dobson*, 2005).

There are some, however, who are quite critical regarding the values in codes of corporate ethics. *Matthews* (1990) believes that there is no significant relationship between responsible behavior and the existence of such codes, and that they were written in protection of corporate interests against employees. In many cases they only force the value system of the leadership of a company on others, and they encourage immoral, rather than moral deeds. In areas not covered by the code, it is 'free for all'. Any act that reduces profits is forbidden (for example embezzlement), while others that

result in gains or savings (for example environment pollution or violating safety norms) are not mentioned in the code (*Cressey and Moore*, 1983). Business codes lessen the employees' responsibility. Besides, they are humiliating, threatening and accusing (*Raiborn-Payne*, 1990). They make shareholders more suspicious, cynical and incredulous (*Dobel*, 1993), they cost more than what they are worth (*Hess-McWhorter-Fort*, 2006), and are less effective than branch codes or laws (*McClintock*, 1999).

Regarding the practical role of codes of ethics, on the basis of (*Schwartz*, 2001)'s metaphors we have identified the following main types (*Szegedi*, 2011):

1. ***„A shop window article"*** **–** According to some critics, codes of ethics are often like shop window articles (*White- Montgomery,* 1980; *Weaver-Trevino-Cochran*, 1999), they do not have a real role, it is only important that the company should have such a thing. Such codes give confusing answers to questions regarding corporate ethics (*Warren*, 1993), and fail to have any practical effect (*Norberg*, 2009). Moreover, they can be even harmful, because employees can feel this shop window nature. After the scandal the code of ethics of Enron was on sale on the internet under the label of 'a barely used code' (*Warner*, 2001). Publishing on the case highlighted that the code was paired with a 'cowboy' culture. It means that they regularly broke the rules and rewarded aggressive, individualistic behavior (*Stevens*, 2008).
2. ***„A set of rules"*** **–** A code of ethics can contain rules – in this sense it can be identified as a set of rules. However, a great majority of them contains values. Moreover, they can be specifically value-oriented. If this is the case, the term 'a set of rules' is not appropriate. It can be used in a negative sense of the word, which may imply that the company means to regulate its employees with the help of the code.
3. ***„A mirror"*** **–** The term refers to the phenomenon that a code of ethics can strengthen acceptable behavior. Naturally, it can contain certain norms that are not yet part of the corporate culture the company aims to include them. A code of ethics is a clear sign of the fact that the company is well aware of the necessity of ethical behavior and expects its employees to be committed to it (*O'Dwyer-Madden*, 2006).
4. ***„An indicator"*** **–** A code of ethics shows what counts as right and wrong behavior. The employees of a company can come from different cultures and societies and can carry different ethic norms. The code can serve as an indicator for them showing what kind of behavior is expected from them in the course of corporate life. It states clear requirements (*Schwartz*, 2001). It serves as a guide for employees to follow corporate values and norms (*LRN*, 2010).
5. ***„A shield"*** **–** A code of ethics can act as a shield for companies because it can protect them from wrong behavior and encourage right deeds (*Cleek-Leonard*, 1998). In many countries codes of ethics are backed up by laws in order to prevent offences.
6. ***„Help"*** **–** A code can provide help in several senses of the word. On the one hand, it can aim to restore confidence after a scandal, on the other hand, it can help preserve and improve company's reputation as well as prevent criticism from the public (*Bondy-Matten-Moon*, 2004). Ethical dilemmas can place a pressure on employees, so a code of ethics can help individual decision-making.
7. ***„A smoke signal"*** **–** Codes of ethics can be defined as smoke signals because they provide a chance to prevent unethical behavior *(Schwartz*, 2001).
8. ***„A base"*** **–**Many authors see codes of ethics as a base of an ethic program (*Murphy*, 1988), because the codification of certain ethic norms can serve as a basis for further implementations.
9. ***„The first step"*** **–** A code of ethics is the first step of building corporate culture (*Wood-Rimmer*, 2003). It is the first step of just an ethical program because it cannot ensure ethical behavior without making employees aware of values and accepted behavior (*Ross-Benson*, 1995).

Kaptein and Schwartz (2008) examined almost 80 studies on codes of ethics in their work which deals with the effectiveness of codes of ethics. 35 % of them evaluated codes positively, that is, they found

them efficient. According to 16 %, the relationship is weak, 33% thinks there is no significant relationship between the existence of a code and the ethical nature of the company. 14 % showed mixed results and only on one occasion was it demonstrated that a code evoked the opposite of what it had meant to achieve. *Kaptein and Wempe* (1998:853.) emphasize: *'a code is nothing, coding is everything'*. Several researches state the importance of repeated evaluation and correction. At the same time, they highlight that a code should become a living document. Besides, voluntary commitment can be effective only if the declaration of will is followed by actual deeds.

Codes of ethics at big corporations in Hungary

The aim of this research is to compare the content of the codes of ethics of big corporations in Hungary. Samples were taken from the first 50 companies in Hungary that have the most revenue (*HVG*, 2011) and have some kind of ethics-related documents available on the internet. The analysis also dealt with the features of these codes as well as what kind of similarities and differences can be detected between them. There is no 'good' or 'bad' practice because the nature and effectiveness of codes and other ethic institutions depend on the branch of industry, the corporate culture of the company in question and on other corporate features. Ethical documentation of 14 companies were compared in the study which are the following: Mol Plc., Nokia Komárom Ltd., E.ON Földgáz Trade Company Ltd., Magyar Telekom Plc., Tiszai Vegyi Kombinát Plc., TIGÁZ Tiszántúli Gázszolgáltató Company Ltd., Richter Gedeon Vegyészeti Gyár Plc., Shell Hungary Kereskedelmi Company Ltd., OMV Hungária Ásványolaj Ltd., Mol Energiakereskedő Company Ltd., Borsodchem Company Ltd., Metro Kereskedelmi Ltd., Szerencsejáték Company Ltd., Telenor Magyarország Company Ltd.

The sample cannot be considered as representative. The statements are applied only within this given circle, they cannot be generalised for the whole of big corporations in Hungary. Table 1 contains the main features of the companies and codes examined. The analysis relies exclusively on the ethical documentation that could be found on company homepages at the time of the study. (*Mol Group*, 2012; *Nokia*, 2011; *E.ON Földgáz Trade Company Ltd.,* 2012; Magyar Telekom Plc., 2011; *TIGÁZ Tiszántúli Gázszolgáltató Company Ltd.,* 2008; *Richter Gedeon Vegyészeti Gyár Plc.*, 2009; *Shell*, 2006; *OMV*, 2009; *Mol Energiakereskedő Company Ltd.*, 2012; *BorsodChem Csoport*, 2008; *Metro*, 2012; *Szerencsejáték Company Ltd.*, 2010; *Telenor*, 2010).

There are several **terms** for codes that present the ethical values and norms of the companies in special technical literature and corporate practice as well. At the majority (79%) of the companies examined the name of the ethical document was 'code of ethics'. There were some cases where it was called 'behavior code' (Nokia), 'operational code' (Magyar Telekom) or 'business principles' (Metro). I will use 'code of ethics' for reasons of simplicity. There are considerable differences in the **extent of the codes**. The shortest one is 2 pages (Mol Energiakereskedő Company Ltd.), the longest one 80 pages (Shell), the average is 20 pages. Some 60 % of the codes analysed provides a detailed elaboration of the topics involved (MOL, EON Földgáz Trade, Magyar Telekom, TIGÁZ, Shell, OMV, Borsodchem, Szerencsejáték).

The extent of detailedness is in connection with the orientation, that is, how much principle- and rule-oriented the code is. The practice of the world's big corporations shows that a relatively small part (13%) of companies apply a code that is only rule-oriented. 35% use a principle-oriented code and the majority of the codes (52%) show a mixed nature, that is, both principles and rules are present in them (*KPMG*, 2008).

This tendency is even more enforced in the analyzed codes because 70% of them represent both principles and rules and only 30% is principle-oriented. The majority of mixed codes (77%) is more rule-oriented and just a smaller part (23%) is more principle-oriented. Experience shows that the

terminology of the codes also reflects its rule- or principle-orientation. Namely, if the code is principle-oriented, it tends to use the term 'we', while in the case of rule-orientation the term 'you' is more frequent (*KPMG*, 2008). The codes examined largely support this statement. Principle-oriented codes used first person plural, while rule-oriented codes talk about the company's employees in general. Two analyzed codes use informal forms, even these only in imperatives: *„You are not alone. If it is difficult to make a decision, or simply you are worried about a problem, consult your boss or the personnel manager"* (Nokia, 2011:7). *„When in doubt ask!"* (Metro, 2012:3).

Among the analyzed companies, one of the most important **reasons for creating a code of ethics** is to provide a guideline and help for employees regarding everyday behavior. 93% of the companies emphasized this aim, with only Mol Energiakereskedő Company Ltd. not planning out about the aim of the code. At 86% of the companies taking corporate responsibility was present in a way that goes beyond the traditional sense of the word. Only Richter and Telenor did not highlight this in their codes. According to 64% of the companies, taking corporate responsibility and ethical behavior is the key to long term economic success and competitive advantage. (MOL, TVK, Nokia, EON Földgáz Trade, Magyar Telekom, TIGÁZ, OMV, Shell, Metro). 64% of the companies set improvement of corporate culture as an aim, and 57% aimed at protecting the company's good reputation.

Apart from accountability, honesty and respect also appear as **ethical values** in all of the examined codes. Further values include cooperation (93%), open mindedness (79%), transparency (71%), fairness (64%), trust (64%), correctness (57%), and equity (57%).

To provide an overview the **topics of the codes** examined I used *LeFebvre* (2011)'s classification. It includes three main areas, namely, protection of the company, meeting social expectations and personal accountability. Within protection of the company you will find personal gain at the company's expense and company assets. Within meeting social expectations there are honesty, human rights and legal adequacy. Similarly, within personal accountability there are the subtopics of accountability for oneself and for others. I have supplemented *LeFebvre* (2011)'s topics with specific areas that occur in the codes examined by me. Figure 1 presents the main topics that occur in the examined codes. The percentages show frequency respectively. On the basis of frequency, the more frequent a topic is, the darker the background in the figure.

On the basis of the analysis, the most frequent topics of the examined codes are conflict of interests (100%), gifts and entertainment (100%), discrimination/harassment (100%), and adherence to law (100%). In most codes you will find use of company assets (86%), protection of intellectual rights (86%), protection of personal data (86%), workplace health and safety (86%), applicability to all (86%), penalties for violation (86%), and special accountability of leaders (86%). Also, frequent topics are bribery and corruption (76%), not supporting political parties (76%), environment protection (76%), free and fair competition (71%), and the must to report on others violating the code (76%). Two third of the codes include control of the employee's political activity (64%), public representation (64%), real data (64%), disclosure and transparency (64%), safe products and services (64%), anonymous reporting (64%) and whistle blower protection (64%). More than half of the examined codes mention insider trading (57%), basic human rights (57%), contact with state officials (50%). Also, 57 % of the codes have a top manager prologue.

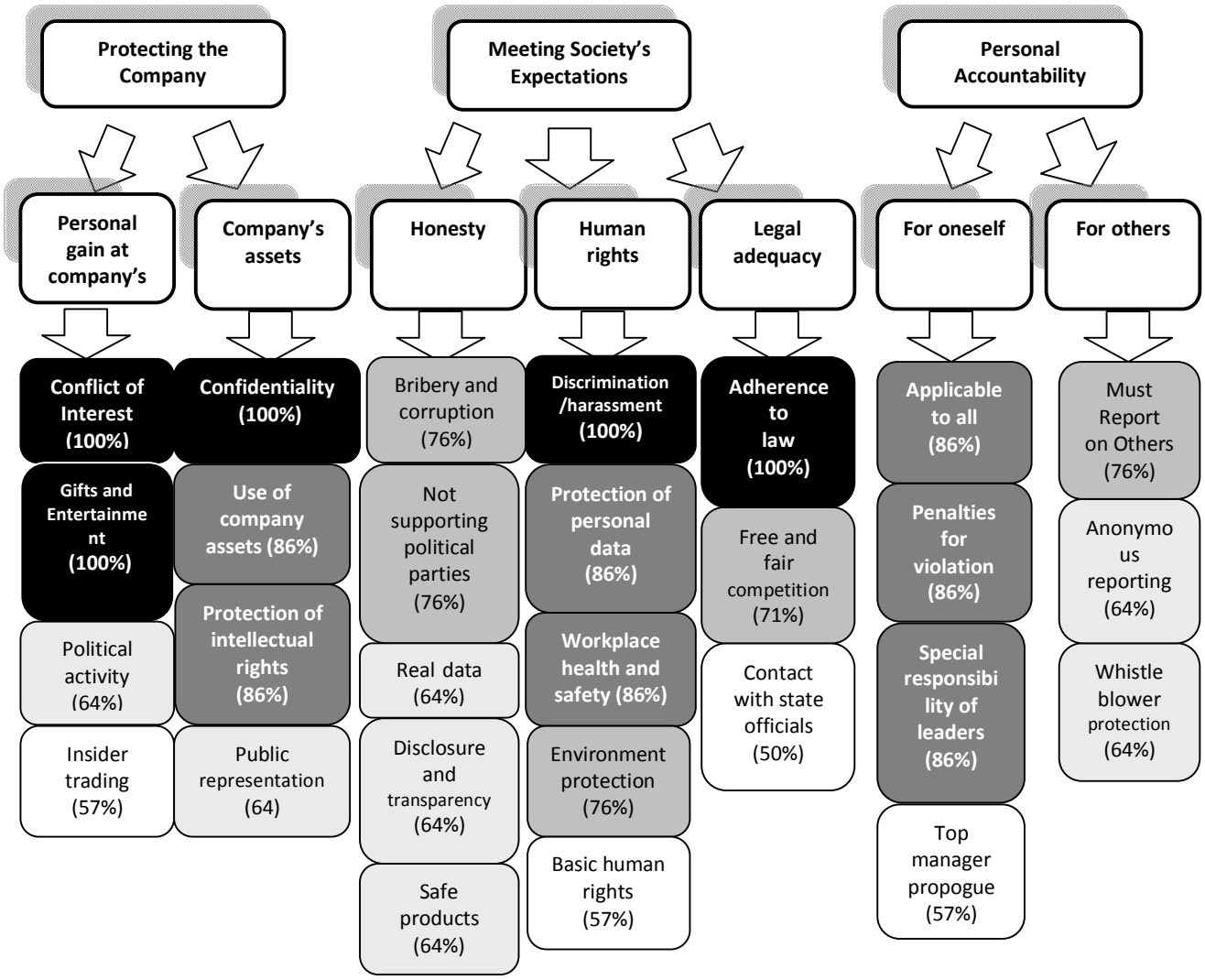
The empiric part of the above mentioned *LeFebvre* (2011) study compared the codes of ethics of the first 50 companies according to revenue in the USA and India. Each of these was available on the internet. **Comparing the Hungarian, American and Indian results** it can be stated that there are two areas that occurred at each company in all the three countries. These are: conflict of interests and confidentiality (Table 2.). We have overtaken the American companies regarding six areas: gifts and entertainment (difference: +4%), public representation (+6%), discrimination/harassment (+12%), workplace health and safety (+12%), environmental protection (+6%), adherence to law (+2%). We

have been overtaken by the Indian companies in two areas: insider trading (-19%) and use of company assets (-8%). However, 15 topics occurred more frequently in the Hungarian codes than in the Indian ones. We have a 54% advantage regarding applicability to all and 58% regarding the obligation to report on others violating the code and anonymous reporting.

Table 1: Main characteristic features of the examined companies and codes of ethics

Company	**MOL**	**Nokia**	**EON Földgáz Trade**	**Magyar Telekom**	**TVK**	**TIGÁZ**	**Richter**
Place according to revenue (2010)	1.	3.	7.	10.	17.	22.	24.
Branch of industry	energy industry	electronics industry	energy trade	telecommunication	chemical industry	energy service	pharmaceutical industry
Title of ethical document	Code of ethics	Code of behaviour	Code of ethics	Code of operation	Code of ethics	Code of ethics	Code of ethics
Extent	23 pages	8 pages	28 pages	19 pages	23 pages	24 pages	11 pages
Detailedness	Detailed	Less detailed	Detailed	Detailed	Detailed	Detailed	Less detailed
Principle- or rule oriented	Mixed but more rule-oriented	Principle-oriented	Mixed but more rule-oriented	Principle-oriented	Mixed but more rule-oriented	Mixed but more rule-oriented	Mixed but more rule-oriented
Typical terminology	'Expectations from employees of the group', 'Obligations of the group's employees'	'Employees of Nokia' 'Our employees' 'With this matter turn to the Ethical Office'	'All employees of E.ON Földgáz Trade Company Ltd.' 'our employees'	'We refrain from…' 'We do not take part in…' 'We confirm that…'	'Expectations from employees of the group' 'As an employee of the group it is their obligation to…'	'It is an expectation from all Eni employees', 'Eni has committed itself'	'The company expects all its employees to…'
Company	**Shell**	**OMV**	**MOL Energiakereskedő**	**Borsodchem**	**Metro**	**Szeren-csejáték**	**Telenor**
Place according to revenue (2010)	26.	29.	36.	39.	41.	45.	49.
Branch of industry	fuel trade	fuel trade	energy trade	chemical industry	wholesale (mixed)	entertainment industry	telecommunication
Title of ethical document	Code of ethics	Code of ethics	Code of ethics	Code of ethics	Business principles	Code of ethics	Code of ethics
Extent	80 pages	20 pages	2 pages	12 pages	13 pages	15 pages	7 pages
Detailedness	Detailed	Detailed	Not detailed	Detailed	Less detailed	Detailed	Less detailed
Principle- or rule oriented	Mixed but more principle-oriented	Principle-oriented	Principle-oriented	Mixed but more rule-oriented	Mixed	Mixed but more rule-oriented	Mixed but more rule-oriented
Typical terminology	'Be committed!', 'Act prudently!'	'We seek to…', 'We are obliged to…'	'We are committed', 'We do it responsibly'	'BorsodChem obliges itself to…' 'An employee of the Group'	'Employees of METRO Cash&Carry'	'All employees', 'The company expects'	'Telenor recognises' 'We have to inform'

Figure 1: Main topics of the examined codes of ethics



Source: Compiled on the basis of LeFebvre (2011, pp. 13)

Table 2: Comparison of the topics of codes of ethics

Topic	Frequency at **Hungarian** companies (%)	Frequency at **American** companies (%)	Difference between **Hungarian** and **American** data (%)	Frequency at **Indian** companies (%)	Difference between **Hungarian** and **Indian** data (%)
Protection of the company					
Personal gain at the company's expense					
Conflict of interests	100	100	0	100	0
Gifts, entertainment	100	96	4	92	8
Political activity	64	82	-28	26	28
Insider trading	57	98	-41	76	-19
Company assets					
Confidentiality	100	100	0	100	0
Use of company assets	86	96	-10	94	-8
Protection of intellectual rights	86	no data	no data	no data	no data
Public representation	64	58	6	56	8
Meeting social expectations					
Honesty					
Bribery and corruption	76	no data	no data	no data	no data
Not supporting political parties	76	no data	no data	no data	no data
Real data	64	94	-30	32	32
Disclosure and transparency	64	90	-26	62	2
Safe products	64	no data	no data	no data	no data
Human rights					
Discrimination/harassment	100	88	12	44	56
Protection of personal data	86	no data	no data	no data	no data
Workplace health and safety	86	74	12	66	20
Environment protection	76	70	6	46	30
Basic human rights	57	no data	no data	no data	no data
Legal adequacy					
Adherence to law	100	98	2	96	4
Free and fair competition	71	94	-23	32	39
Contact with state officials	50	no data	no data	no data	no data
Personal accountability					
For oneself					
Applicable to all	86	100	-14	32	54
Penalties for violation	86	90	-4	68	18
Special accountability of leaders	86	no data	no data	no data	no data
Top manager introductory	57	no data	no data	no data	no data
For others					
Must report on others	76	94	-18	22	54
Anonymous reporting	64	88	-24	6	58
Whistle blower protection	64	98	-34	34	30

Source: Hungarian data are taken from the present research; the source of American and Indian data is: *LeFebvre* (2011)

At American companies 11 topics occurred more frequently than in Hungarian codes, and with a significant difference. These topics include political activity (difference:-28%), insider trading (-41%), use of company assets (-10%), real data (-30%), disclosure and transparency (-26%), free and fair competition (-23%), applicability to all (-14%), penalties for violation (-4%), must report on others (-18%), anonymous reporting (-24%), and whistle blower protection (-34%).

Conclusion

The study has revealed that Hungarian codes of ethics are 74% similar to each other regarding their main topics. Gifts and entertainment, discrimination/harassment and adherence to law are given priority. The examined Hungarian and American codes show a 16% difference on average. Hungarian codes show a significant lag regarding insider trading, real data, disclosure and transparency, free and fair trade, anonymous reporting and whistle blower protection. Also, it is thought provoking that while 100% of the top 50 American and Indian companies put their codes of ethics on public display, among the top 50 Hungarian companies it is only 28%. Comparative data lead to the conclusion that Hungarian corporate codes are underdeveloped as compared to the American practice.

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Sailboat Rental: Determining the Price Based on its Attributes

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Abstract

This article examines the effect on price of different characteristics of sailing boats in the nautical segment of travel and tourism industry. The effect on price is estimated under the hedonic function by means of ordinary least squares model (OLS), as the data used in study are cross-sectional. Some 10,791 prices were gathered from approximately 400 sailboats from adriatica.net, a largest web based site for renting travel/tourism products in Croatia. The study reveals huge price differences between sail boats of different sizes, coupled with practically no difference between boats of same size but different brand. Other attributes with a significant effect on price are season, number of rental days, ship length, number of cabins, year of production, skipper, and number of persons. The resulting equation can assist charter companies in shaping inflation-proof pricing and investment strategies.

Keywords

Pricing, hedonic functions, sailboats, ordinary least squares model, Croatia

1. Introduction

Nautical tourism is the fastest growing sector of tourism in Croatia, and thus deserves thoughtful discussion. Qualitative and quantitative data will be presented through an in-depth analysis of both historical and current data regarding the nautical industry, as follows:

1.1. Nautical tourism

Croatia has a rugged coast with 718 larger islands, 389 islets and 78 reefs. These 1,185 islands are located along 1,777 kilometers of the Adriatic coast. Approximately 60 islands are inhabited year-round, which make up an area of 3300 km^2. The coastline has a Mediterranean climate, characterized by warm and dry summers, and moderate rainy winters.(22)

When analyzing types of tourism offered by the Republic of Croatia, nautical tourism stands out, as it represents one of the most popular forms. The Croatian Association of Nautical Tourism oversees the official segments of nautical tourism. The association was established under the Croatian Chamber of Commerce, and includes four groups: the Croatian Marinas Group, the Croatian Charter Vessels Group, the Croatian Diving Tourism Group, and the Cruising and Motor Sailboat Excursions Group.(22) It is the centre for obtaining information for yachtsmen, and aims to advance Croatia's nautical tourism. While there continues to be room for advancing the market, the last decade has shown intensive development of Croatia's nautical tourism. Despite this, Croatia is one of the few places where you can still avoid the crowds, more typical of southwest Europe's Mediterranean coast, while still increasing in popularity.(19)

1.2. Nautical tourism infrastructure

As for the current nautical tourism infrastructure, it is decent considering that it suffers from a lack of foresight; the marinas were built for yachts that were smaller than many currently used. Since there is a large demand for accommodation on bigger yachts, marinas will need to update their facilities and layouts. The coastline is spectacular and immensely varied and the Adriatic is well charted and buoyed".(15) "Natural indentedness of the archipelago coupled with a long tradition of seafaring has contributed to the creation of ideal conditions for the development of sailing."(18) In future plans it is important for Croatia to learn from the mistakes of other countries in order to preserve its unique natural beauty. (15) This rapid development of nautical tourism reminds one of the old saying *"Navigare necesse est. Vivere non est necesse."* (Sailing is a necessity, merely living is not)", perhaps a motto which is becoming more widely shared. "An interest in sailing reflects a longing of man for the original element of life, a longing for a primordial force that each experienced sailor is at the same time afraid of and inevitably attracted by."(16)

As mentioned, the popularity of nautical tourism has been increasing over the past few years, especially with wealthy customers that spend above average standard. Nautical tourism is a tourist product, because of its relation to entertainment, as well as water sports (recreational activities and regattas). The economic importance of nautical tourism should be apparent, for it increases service levels and "its development means revitalization of coastal resources as well."(23) This is key, since there has been a trend of vacating island towns and villages in search of jobs and opportunities in more urban, coastal region for many decades now. On that note, even undeveloped and less popular locations show potential.

1.3. Boat shows

The Zagreb Boat Show takes place in Croatia's capital every February and Split Boat Show, takes place in early April. The show has grown exponentially in a short period of time, particularly in its size and space. Another boat show that sprung up, is the Biograd na moru (Biograd on the sea); it takes place in early October, and is still a small show. (15)

1.4. Marinas in Croatia

There are 48 marinas along the Croatian coast, of which only 38 were officially registered as of March 31, 2004, and a mere four marinas were given category I status, meaning they provide the highest standards. Other services offered are associated with "swimming and excursions in nautical tourism, and organized nautical competitions (meetings at sea, nautical-tourism rallies, regattas, etc.) Croatian coast offers ideal conditions for all water sports (motor boating, water-skiing, speed boating, windsurfing, jet ski etc.)." (24)

ACI Club is a chain of 21 marinas, located from the southern coastal town of Dubrovnik to Umag in the northern part of the Croatian Adriatic. The company has been operational for 17 years and has helped in increasing interest in sailing. The ACI Club is known to professional navigators as a regatta organizer in dual sailing, and has hosted ACI cup and World Cup in dual sailing in Dubrovnik (1996) and in Split (2000). Its headquarters are located in Opatija. (24)

1.5. Adriatic sea

Adriatic Sea spans from the Balkan to the Apennine peninsula and was named after an ancient port. The Adriatic is an attractive resource for Croatian nautical tourism. East part of the coast belongs to the Republic of Croatia, and is "a unique area in Europe for cruising with motorboats, speedboats, or sailboats, but also for enjoying the underwater world. The French diving legend Jacques Cousteau once described Croatia's waters as the cleanest and clearest in the world." (27)

1.6. Sea temperature

The average sea temperature in the winter is 5°C, and summer temperatures range from 22 to 27°C. The average annual temperature of the Adriatic Sea is 17°C, with an annual average of 2,600 hours of sunshine, making the Adriatic and its many islands among the sunniest regions of Europe. The average annual temperature is 11°C. (27) Waves in the Adriatic rarely pose a problem for boaters, since big waves occur very rarely. Most often, waves in the Adriatic range in height between 0.5 and 1.5 meters, and very rarely exceed 5 meters. Typically these rare waves are caused by *Jugo,* a south-west wind that creates a more dynamic sea surface. (17)

1.7. Historical facts

Croatia's uniqueness can be attributed not only to its clear clean sea, but also for a thousand years of documented history and culture. The Adriatic Sea is the cradle of ancient civilizations in the region, and the most economical trade route between Europe and the East. The east coast of the Adriatic Sea and the accessible islands were inhabited in the beginning of the early Stone Age (archaeological findings in caves near the islands of Hvar and Palagruza, etc.). (20)

In the 6th century BC the ancient Greeks traded with the Illyrians by means of the Adriatic Sea, and founded their early colonies on many of the islands. Examples include *Pharos*, today's Starigrad, on the island of Hvar, as well as *Issa,* or Vis. Later establishments were developed on the coastline. When Romans arrived, they built palaces and summer residences, and spent much time at sea. Evidence of their seafaring activity can be found in many underwater archeological sights, which frequently uncover amphorae, in the northern region (*i.e.* Pula), as well as the southern region (*i.e.* Cavtat). Later on Slavs arrived, a group which the majority of Croatians recognize as their ancestors. The southern coastal city-state of Dubrovnik played a leading role in culture and trade at this point in history. (20)

In the 18th century, following Napoleon's short rule, the Austrian monarchy came to power. This monarchy fought with Italy for control of the Adriatic's eastern coast until the battle of Vis in 1866, at which time Austrians gained control over the region. Ancient artifacts can be found around the coast, and in the depths of the sea in the form of shipwrecks. Under Austro-Hungarian rule, trade and shipbuilding flourished. Even during the two World Wars, the Adriatic witnessed important naval battles. As a maritime route between East and West, the significance of the Adriatic Sea is great. (20)

1.8. Nautical tourism: the definition

Even though the concept of nautical tourism has been present in technical, scientific and everyday language, no formal definition has been accepted for nautical tourism. It may be thought of as a synonym for marine tourism, sailing tourism or yachting tourism, however, each of these terms can be thought of differently with varying emphasis. After extensive research, I have decided that the following definition is most appropriate: *Nautical tourism is navigating and residing of the yachtsmen on floating objects and/or in nautical tourism harbors for relaxation and recreation.*

1.9. Statistics

Considering global trends, Croatia is one of the rare countries in which there was no decline in tourists for the previous years. Pristine nature, cultural and historical tradition and legacy, mild Mediterranean climate, close proximity to European markets- all are positive attributes which make Croatia's tourism one of the most important sectors of the country's economy. (15) Tourism market is experiencing constant growth in the number of visitors, and the number of days tourists spend in the country. There has been a six percent increase in the number of tourist visitors and an eight percent increase in the number of days in which tourists stayed (in 2005). That is, there were almost ten million tourists who visited the country, resulting in a total of 51.4 million days, which tourists spent in Croatia. (31) According to the Croatian National Bank, the total proceeds from international tourism were 5.99 billion euros in 2005. In accordance with actual trends in foreign markets, Croatian tourist products are developing, respecting indigenous regional characteristics, through different forms of selective tourism, such as: nautical tourism; diving tourism; cruising on motor boats; sailing boat tourism; village tourism; horseback riding tourism; sport tourism; excursion tourism; medical tourism; adventure tourism; congress tourism; eco tourism; hunting tourism; fishing tourism; cultural and religious tourism.

"Of course there is more to the nautical tourism industry than marinas and berths – charter companies, boat building, boat repairs, boat equipment and services, marina equipment supplies and crew supply to name but a few. Hard data is not that easy to find and the ancillary services have yet to be classified into a directory that would make life a lot easier for visitors and probably generate some more cash for the industry." (15)

However, there has been some recorded and compiled data made available by the Ministry of Tourism. Specifically, 52,513 navigation licenses were issued to foreign vessels visiting Croatian waters in 2003. This increased by 1.8% in 2004. Statistics for the first nine months of 2004 showed a total of 1,925 vessels chartered, of which 629 (33%) flew a foreign flag. At this time there was 15,407 total moorings available, and "189,492 recorded moorings by vessels in transit, 76% of which were by vessels registered under a foreign flag. Profits from moorings by vessels in transit totaled 64,768,000 kunas (about £6 million) for the period, a 28 % increase for the same period of the previous year." (15)

Current research is insufficient in directly serving as a framework for creating long-term development plans for nautical tourism within Croatia. There has been partial research in marketing (the attitudes of yachtsmen), planning, and environment research (Tomas Nautika study). The largest source of information on nautical tourism can be found in governmental publications.

The following statistics are intended to show the current state of nautical tourism in Croatia, and are based on the national statistics publications issued by the Ministry of Tourism: In 2004, according to the type of the vessel, the published licenses which were issued to motor yachts (21.2%), sailing boats (18.9%), and other vessels (59.9%). The majority of these licenses were issued for boats 6 meters and under (49.5%), and the rest for boats exceeding 6 meters to 8 meters (17.5%), for boats exceeding 8 meters to 10 meters (10.9%), for boats exceeding 10 meters to 12 meters (11.2%), and for boats exceeding 12 meters to 15 meters in length (7.8%). (31)

The analysis of issued licenses for foreign vessels in the time period from 1996 to 2004 shows a continual trend of rising number of licenses issued, with the exception of 1999, an exception that reflected a regional glitch in the trend, with neighboring countries also recording a decline in license issuance, mainly attributed to NATO activity in the region. The year 2004 recorded a 56% increase in issuing licenses from 1996. While the past few years have seen increases, one must consider that they are still less than prewar levels. For example, in 1987, 66,451 licenses were issued, whereas 52,513 navigation licenses were issued in 2003 to foreign vessels visiting Croatian waters. This increased by 1.8% in 2004.

The majority of yachtsmen come from Western European countries. In permanent docking, the majority of vessels were under the Croatian flag (26%), closely followed by Austrian (24%) and German flags (21%). From the transit vessels, the majority again was under the Croatian flag (25%), closely followed by Italian (22%), German (17%) and Austrian flags (14%). The most common type of vessel is the sailing boat, which accounts for 62% of all vessels in transit, and 57% of all vessels that were on permanent stay in a harbor. (31)

Another upward trend is in the increasing number of yachtsmen coming to the country, whose number tripled from 1996 to 2004. Even though there are smaller proportions of tourist arrivals (8.3%) and stay-overs (2.4%) in nautical tourism, it has more dynamic rates of growth than stationary tourism. Stationary tourism is a form of tourism when tourists reside in immobile construction, for example hotels and motels, while being on a vacation. Nautical tourism is also less seasonal than stationary tourism. The average annual rate of increase for nautical tourism is 15.8%, which is 4.1% more than stationary tourism. These statistics are somewhat incomplete, since the data are only gathered in nautical tourism harbors, so yachtsmen can be recorded several times in their voyage to different harbors. Also, stay-overs are under-recorded since many yachtsmen anchor at places other than harbors, so no accurate data can be collected by current means. (31)
There have been two studies done on the characteristics of demand in nautical tourism of Croatia to date, both by TOMAS-Nautika (2001 and 2004). (31) The most important results of the study are as follows:

1. More than half of total boaters surveyed are the owners of the vessels (52%); 32% were in the possession of a charter company, and the rest were using vessels under someone else's name (16%). (31)
2. Every fifth yachtsman said that he/she found a skipper and/or crew very helpful. The average number of people on a boat was four, including the skipper. Most people sailed with their family members (39%), or friends (33%). (31)
3. 74% of foreign boaters had sailed in Croatia three times or more, and 42% visited the country six or more times, which shows loyalty to the nautical tourism product of Croatia. Only 11% of the yachtsmen recorded in the summer 2004 sailed in Croatia for the first time.(31)
4. Yachtsmen that chartered boats more often sailed between ports and harbors, rarely taking day trips from a single harbor. (31)
5. The voyage usually spanned 8 to 14 day stay-overs (38%), followed by 4 to 7 day stay-overs (26%), and 15 to 21 days stay-overs (21%). 14% of boaters stayed longer than 22 days. (31)

Charter companies operate from nearly every marina; approximately 50% of these are reportedly Croatian owned. The laws relevant to charter companies have recently changed, requiring any boat carrying passengers for money to be registered under the Croatian flag. "This has caused a bit of an upheaval within the industry but most of the foreign companies seem to be intent on staying. The rules are being reviewed and hopefully some sensible exceptions will be made without allowing the black charter industry, at whom the regulations were aimed, to flout them." (15)

2. Literature Review

2.1. Studies using hedonic model

One of the most extensively used models in real estate research has been the hedonic model. Despite significant simplifications in the assumptions the model has proven to be empirically viable, especially in examination of the relationship between property values and preferences for its different attributes. Specifically, the value or price of the property is defined as a function of the bundle of its attributes. The model's methods have long been used in research, before Court (1939) formally proposed the name hedonic in his seminal paper on price indexes in automobile studies. Stemming from the Greek word hedonikos, the name relates to the derivation of utility from consumption of goods and services.

The theoretical and statistical foundations of hedonic price theory are found in the works of Lancaster (1966), Rosen (1974), and Feenstra (1995). The early hedonic literature focuses on the explanations of the attribute or characteristic price. One understanding of it, proposed by Court (1939), views the attribute price as consumer's willingness to pay for the attribute. Lancaster (1966) expanded on this by "…breaking away from the traditional approach that goods are the direct objects of utility and, instead, supposing that it is the properties or characteristics of the goods from which the utility is derived" (Lancaster, 133). Furthermore, Lancaster's theory goes to say that goods are arranged in groups based on their attributes and that in the group they are consumed in various combinations. Rosen (1974) altered Lancaster's approach and assumed that goods within a group are consumed discretely. In other words, consumers do not maximize their utility by purchasing a bundle of goods with desired characteristics, but by consuming one that has the most desirable combination of them. Rosen assumed a non-linear relationship between price of a good and its attributes, while Lancaster saw this relationship as linear. The differences between Lancaster's and Rosen's approaches are not mutually exclusive as they seem to apply to different types of goods. Lancaster's theory best applies to non-durable goods, while Rosen's applies to durable goods.

2.2. Studies on price determinants in the tourism industry

Research on sailing boat rental price determinants has so far been non-existent. The most extensive research done on price determinants using hedonic model, as stated before, is in the real estate industry (especially research on price determinants in housing). However, there is a recent trend of using hedonic model in tourism research. The following is the body of knowledge in tourism research on hedonic price models: The influence of dependent variables on hotel room prices (Coenders, Espinet, and Saez 2003; Israeli 2002; Monty and Skidmore 2003; White and Mulligan 2002), inclusive tour or package tour prices (Aguilo, Alegre, and Riera 2001; Aguilo, Alegre, and Sard 2003; Clewer, Pack, and Sinclair 1992; Espinet et al. 2003; Papatheodorou 2002; Sinclair, Clewer, and Pack 1990; Taylor 1995), restaurant prices (Gunawardana and Havrila 1996), and airfare prices (Schwieterman 1995).

The biggest influence for this study was Coenders, Espinet, and Saez (2003) article "*Effect on prices of the attributes of holiday hotels: a hedonic prices approach*." Unlike the combination of time series and cross-sectional modeling (used in that study), which is random effects method (mixed modeling or panel modeling), this study introduces cross-sectional modeling by using ordinary least squares method (OLS), specifically log linear model. The real difference is that Coenders, Espinet, and Saez are using data based on information on the months from May to October for a time period from1991 to 1998. On the other hand, the data used in this study is for the month of July (two dimensions opposed to one). The results found by both of the studies are similar. One of the most relevant characteristics of a sailing boat in determining price is its length; likewise, Coenders, Espinet, and Saez found the most relevant characteristics of a hotel to price is star category. That article has identified some important variables that affect the price paid by tourists in the sun-and-beach segment, for which the major motivations of tourists are basically the same worldwide. Such results were found in this study where important variables affect the price paid by tourists in nautical tourism, specifically sailing boat rental.

The previously mentioned studies also found that many of the hotel room characteristics have no significance in explaining the price, and the difference between prices. I observed the same diagnosis, since the majority of my characteristics were irrelevant for price determination. However, a few significant ones provided a healthy model which explains a lot of functions, even correlation between the attributes.

Another informative article on the matter is a study done on Norwegian sun-and-beach package tours by Christer Thrane. Thrane followed the work of Espinet and provided a research similar to his. Researcher used two regression models to show the difference between a model without hotel star rating variable, and a model with hotel star rating variable.

3. Methodology

It is essential to produce a mathematical formula that will provide an easy way of determining sailboat rental prices. This will help charter companies determine practical and competitive prices. Building on the research of price determination in the real estate industry which used hedonic pricing model, the study involved the collection, compilation, and analysis of contemporary data on sailing boat attributes, characteristics, specifications, and prices in the scope of adriatica.net website database. The research includes the collection and analysis of quantitative data from the above-mentioned web site. The crux of this research lies in the extensive collection of raw data that will help to determine the variables, variations in pricing model, averages, and regressions using the hedonic pricing model. The results and findings will be discussed using descriptive and inferential statistics. This study focuses on the month of July, since it is representative of high summer season

characterized by moderate sailing conditions ("good winds"). Furthermore, this study examines data for renting a boat in one-week intervals (seven days). The price for the month of July is determined by finding the average price for the four weeks in July. Furthermore, the data for Bavaria sailing boats, the low-cost brand within the industry, are analyzed looking for possible correlations between engine type and other boat attributes.

The challenge of price determination concerns those in the academic, as well as the business sphere. Scholars propose how it should be determined, and offers solutions (i.e. means of doing it), businesses can use it and benefit from its application. Since there has been very little research with in this field, professionals in the industry are not accustomed to examine or implement research results. This and other quantitative research may help businesses develop future plans, through more accurate predictions, measurements and the simplification of otherwise complex material.

This study is significant for multiple reasons. Its initial practical use is in aiding charter companies in determining their sailing boat rental prices. Moreover, it offers a theoretical way for solving practical problems facing businesses, charter companies, tourist agencies, and the government. This could be a great tool for those companies wishing to better manage their prices, and to re-evaluate their current pricing systems and databases (or lack of). This research and the proposed results should provide a model for companies to determine if they are over pricing or under pricing. Such information can help companies to become a competitive player in this growing industry.

By having a mathematical formula that would easily show a price for renting a boat, charter companies could increase their efficiencies, and become a price leader by having comparative and competitive advantage over the industry. These are some of the ways Croatian charter companies can battle the increasing surge of foreign companies trying to capitalize on this fast growing market. Even banks have started giving away "easy-to-pay" loans to ones wanting to become ship owners realizing it is a win-win position for both parties (based on the previous data which show a huge growth in both the profits and number of yachtsmen entrepreneurs). (32)

3.1. Data

Studies on boat rental prices are still rare in Croatia. Charter boat rental prices are not even systematically collected by any official tourist or statistical office. An existing database of rental boat prices was used from adriatica.net for the purpose of this study. The database covers the whole coastal region of Croatia (Istria, Kvarner and Dalmatia). Hedonic functions are estimated by means of ordinary least squares model, specifically the log linear model. This study provides quantifiable results which should prove to be more easily applied to sailboat rental price determination than the qualitative data. The web site was chosen because of its simplicity, data availability and data extensiveness in sailing boat characteristics and because of the number of boats it contains in its register. All of the quantitative data collected originates from this web based site, a third-party operator that serves as a central point for sailboat rental in Croatia. Boat characteristics are divided into appliances, structural variables, and other. Aplliances are: Gas cooker with oven, electric refigerator, compass/echo sounder, nautical charts and nautical guide, GPS, VHF radio, pillows and blankets, radio-cassette players or cd, life jackets, distress flare kit, first aid kit, fire extinguisher, main anchor, dinghy inflatable, bimini top, navigation kit, cutlery, shower and/or toilet, auxiliary anchor, sun shade, deck shower, calibrated anchor chain, heating system, radar, port or starboard thruster, and electric winch for anchor. Structural variables are: The boat length, lenght at waterline, draft, maximum beam, number of cabins, number of beds, weight, balast, water tank capacity, and fuel capacity. Other variables not mentioned are put under the "other" category.

The following text briefly describes the process of data collection:

Data is accessed via the Adriatica.net website. First choose the option “Sailboats", which directs you to http://adriatica.net/charter/charter_en.htm where you choose the rental time period. Specified period for this study was from 1/6/2007 (Date of Departure) till 12/29/2007 (Date of Return), in order to get the listing of all the boats being available for rent in 2007. There are also several options one can choose to make the search more specific. However, to get all the data possible, the following options were selected before the search was conducted. “All sailboats” under boat type; number of persons is specified as “one," overall length as “not important," and “whole Adriatic” as region or port. When all those options were entered, the search was carried out. This listed 58 pages of sailboats each having 8 on average. The data range was approximately 464 sailboats. There were also a total of 56 boat characteristics.

4. Results

For this study, *Hedonic regression*, or more generally *hedonic theory*, is used. It is a method of estimating demand or prices in economics. It decomposes the item being researched into its constituent characteristics, and obtains estimates of the value of each characteristic. Essentially, it assumes a separate market for each attribute. One of the ways for estimating it is by using ordinary least squares (OLS) regression analysis. “Usually, a dummy variable (an attribute vector) is assigned to each attribute or group of attributes. Each characteristic within a vector is either included in the regression or not, by multiplying it by either 1 or 0.” (29)

In nautical tourism, it is used to adjust for the problems associated with studying a good that is as heterogeneous as a sailing boat. Because sailing boats are different, it is difficult to estimate the demand for them generically. Instead, it is assumed that a boat can be broken down into characteristics such as number of cabins, or number of beds. In this study, different characteristics specific to sailing boats were used. “A hedonic regression equation treats these attributes (or bundles of attributes) separately, and estimates prices (in the case of an additive model) or elasticity (in the case of a log model) for each of them. This information can be used to construct a price index that can be used to compare the rental price of sailboats in different cities, regions and countries, or to do time series analysis.” (29) As with Consumer Price Index (CPI) calculations, hedonic pricing can be used to correct for quality changes in constructing a sailing boat price index. It can also be used to analyze the demand for various sailboat characteristics, and sailboat demand in general.

Hedonic model may be estimated using ordinary least squares (OLS) regression analysis, which is used for the purpose of this study. “*Least squares* or ordinary least squares (OLS) regression analysis is a mathematical optimization technique which, when given a series of measured data, attempts to find a function which closely approximates the data (a "best fit"). It attempts to minimize the sum of the squares of the ordinate differences (called *residuals*) between points generated by the function and corresponding points in the data.” (29)

The formulas essential to this study are theoretical (a.), statistical (econometrical) (b.), and practical (c.).

a. Ln price = F (X)

Ln price = F (lnlength, age, gps, number of cabins, fuel capacity, engine power, gas cooker)

The equation shows the determinants of selling price on the right side of equation and rental price as a dependent variable on left side. The specification is log-linear as the dependant variable is in logarithmic form while independent variables are in either linear or logarithmic forms. In a case where the logarithm of a dependent variable is linearly related to some independent variable, we interpret it as a percentage (%) change in dependent variable caused by a change in the independent variable. In the case where we regress a logarithm of an independent variable on a logarithm of a

dependent variable, we interpret coefficients as constant elasticities. The use of logarithmic transformation goes beyond interpretational conveniences, as it is primarily used as a tool in prevention of heteroskedasticity, since the distribution of percentage changes tends to have more of a constant variance than distribution of changes.

b. Ln price= β0+ β1 x lnlength – β2 x Bavaria – β3 x age + β4 x gps + β5 x cabins + β6 x central Dalmatia+ β7 x fuel capacity + β8 x engine power + β9 x gas cooker

c. Ln price= 3.8575 + 1.4597 x ln 8 – 0.0775 x 0 – 0.0253 x 13 + 0.0674 x 1 + 0.0452 x 2 + 0.0220 x 0 + 0.0002 x 30 + 0.0034 x Volvo 19 + 0.0299 x 1

Table 1: Equation example on Benetau first 265 sailboat.

ship name	constant β0	Lnlength	Bavaria	age	gps	cabins	central Dalmatia	fuel capacity	engine power	gas cooker
Beneta u first 265	3.8575	1.4597	-0.0775	-0.0253	0.0674	0.0452	0.0220	0.0002	0.0034	0.0299
		8	0	1993	1	2	0	30	Volvo 19	1

5. Conclusion

The purpose of this unmatched study was to examine what are the determinants of sailboat rental prices. The practical significance of the research lies in its potential to aid in developing a model for determining rental prices for nautical tourism products in Croatia. This possible model would be useful to charter rental agencies, travel agencies, governmental and tourism institutions, as well as other interested investors. The resulting mathematical formula will provide an easy way of determining sailboat rental prices. This will help charter companies determine competitive prices and help their yield management practices.

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Appendix

Table 2:. Summary statistics

Variable Definitions	Variables	Observations	Mean	Std. Dev.	Min	Max
Natural log of Price	ln(Price)	409	7.801	0.365	6.908	8.795
Natural log of Boat Length	ln(Length)	409	2.510	0.158	2.032	2.818
Price in Euros	price	409	2612.306	989.997	1000	6600
Boat Length (in meters)	length	409	12.452	1.942	7.630	16.750
Bavaria, Yes=1, No=0	bavaria	409	0.396	0.490	0	1.000
Number of Cabins	cabin	409	3.403	0.978	0	6.000
Number of Beds	beds	409	7.078	1.889	4	12.000
Age in years	age	408	4.294	2.343	0	16.000
Engine Power	enginep	358	43.611	22.136	9	100.000
Volvo, Yes=1, No=0	volvo	358	0.517	0.500	0	1.000
Draft (in meters)	draft	409	1.787	0.419	0	2.550
Maximum Beam (in meters)	beam	409	3.848	0.779	0	6.050
Hull Length (in meters)	hull	409	5.498	6.121	0	19.490
Length at Waterline (in meters)	lengthw	409	4.837	5.412	0	15.250
Weight (in kilos)	weight	409	4439.225	4625.725	0	17000
Balast (in kilos)	balast	409	651.139	1154.045	0	5050
Water tank capacity (in liters)	waterc	409	383.435	218.344	0	1055
Fuel Capacity (in liters)	fuelc	409	172.819	93.139	0	500
Compass / Echo sounder, Yes=1, No=0	compass	409	1.000	0.000	1	1
Nautical charts and nautical guide, Yes=1, No=0	charts	409	0.941	0.235	0	1
GPS, Yes=1, No=0	gps	409	0.941	0.235	0	1
VHF radio, Yes=1, No=0	vhf	409	0.978	0.147	0	1
Electric shore connection/water hose ,Yes=1, No=0	conn	409	0.614	0.487	0	1
Number of Electric refrigerators	fridge	409	0.570	0.501	0	2
Gas cooker with oven, Yes=1, No=0	gasc	409	0.377	0.485	0	1
Pillows and blankets, Yes=1, No=0	pillow	409	0.834	0.373	0	1
Number of Radio-cassette players or cd,	radio	409	0.858	0.934	0	18
Life jacket	jacket	409	8.098	2.000	0	12
Distress flare kit, Yes=1, No=0	flare	409	1.000	0.000	1	1
First aid kit Yes=1, No=0	aid	409	1.000	0.000	1	1
Fire extinguisher Yes=1, No=0	fire	409	0.988	0.110	0	1
Main anchor Yes=1, No=0	manchor	409	0.462	0.499	0	1
Dinghy inflatable Yes=1, No=0	dinghy	409	0.550	0.498	0	1
Bimini top Yes=1, No=0	vim	409	0.677	0.468	0	1
Dubrovnik Yes=1, No=0	dubrovnik	409	0.042	0.200	0	1
Central Dalmatia Yes=1, No=0	cendal	409	0.330	0.471	0	1
Number of Persons	pers	409	8.333	1.761	4	12
Navigation kit Yes=1, No=0	nav	409	0.831	0.375	0	1
Cutlery	cutl	409	7.932	2.465	0	12
Number of Showers and/or toilet	show	409	1.259	1.067	0	5
Auxiliary anchor Yes=1, No=0	aanch	409	0.222	0.416	0	1
Sun shade Yes=1, No=0	sun	409	0.240	0.427	0	1
Deck shower Yes=1, No=0	dshower	409	0.457	0.499	0	1
Calibrated anchor chain Yes=1, No=0	cachain	409	0.262	0.440	0	1
Number of extra beds	xbeds	409	1.213	0.823	0	3
Heating	heat	409	0.117	0.455	0	7
Radar Yes=1, No=0	radar	409	0.007	0.085	0	1
Port or starboard thruster Yes=1, No=0	port	409	0.007	0.085	0	1
Electric winch for anchor Yes=1, No=0	winch	409	0.007	0.085	0	1

Table 3: Hedonic regression results for boat rental price equation

Dependent Variable ***ln(Price)***	*Coefficient*	*Std. Err.*	*t-statistic*	
ln(Length)	1.4597	0.0883	16.53	***
Bavaria	-0.0775	0.0113	-6.88	***
Age	-0.0253	0.0022	-11.76	***
GPS	0.0674	0.0188	3.58	***
Cabin	0.0452	0.0102	4.43	***
Central Dalmatia	0.0220	0.0093	2.36	**
Fuel Capacity	0.0002	0.0001	1.95	*
Engine Power	0.0034	0.0005	6.60	***
Gas Cooker	0.0299	0.0091	3.29	***
Constant	3.8575	0.1888	20.4300	***

*** - Significant at **the** 1% level; ** - Significant at **the** 5% level; * - Significant at **the** 10% level

Key Decision-Making Factors in Bank Mergers[1]

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Abstract

The paper presents some important determinants of mergers and acquisitions in the Croatian banking system. The aim of the research was to define the role of financial as well as strategic indicators as key factors in decision-making process within bank integrations. In fact, the most important period of merger wave in the bank industry occurred at the beginning of the century when several state-owned banks, after the rehabilitation program performed by the state, were privatized and consequently became majority foreign-owned. Apart from that process, development of the Croatian banking system was driven by other M&A decisions which influenced the macro indicators of concentration and the performance indicators of the banking system as a whole. It is questionable to what extent the decisions were made as a part of strategic plan to enter the banking system or the investors were mostly motivated by the performance of financial indicators of the observed banks. The research emphasizes the role of financial indicators and is based on the assumption that integration decisions rely firstly on comprehensive analyses of financial indicators. Consequently, using historical data on bank mergers and acquisitions in the Croatian banking system, different types of financial indicators, which probably affected the final investor decisions, were observed. With the assumption of only financial indicators as relevant in decision making and assuming the subjectivity of investors and strategic decisions as external factors, the level of significance for each financial indicator was calculated. Finally, according to the significance of some indicators, it was shown that some of the performance indicators played more important role in the M&A process. These results, based on the historical data of financial indicators, could be a relevant starting point for observation of future M&A processes which will probably occur in a future consolidation of the banking system.

Keywords

Financial indicators, bank integration, mergers and acquisitions (M&A)

[1] The views expressed in this article are those of the author and do not necessarily represent the views of his employer.

1. Overview of the Development of Banking Market in Croatia

Considering the changes that occurred in some last ten years it is visible that Croatian banking system was under the significant influence of merger and acquisition processes. Since the constitution of the Republic of Croatia, 20 years ago, the peak in the number of banks was reached at the end of year 1997 and year 1998, when 60 banks were licensed to provide banking services in Croatia. Meanwhile, many of these banks are not active any more due to several reasons among which one of the most important is the effect of M&A, which resulted in decrease in the number of banks. At the end of the first half of 2012 there were 32 banks in banking system (more precisely 31 banks and 1 savings bank), which at first glance seems to be almost only one half of the number of banks that were operating 15 years before. More precisely, during the observed period 10 new banks entered the banking system, but at the same time 38 banks retreated from the market. These numbers demonstrate serious changes in Croatian banking system which resulted from M&A process. The majority of decline in the number of banks happened in the first half of the last decade, which was also the period of major bank mergers and acquisitions, while in recent years only moderate changes in the number of banks were noticed and consequently rare examples of M&A. It was found by academic surveys that merger waves are differently stimulated by the private firm mergers and by the public companies. While private firm mergers are fundamentally driven by the existence of synergistic gains, public firm mergers are influenced by the overvaluation in the stock market (Blunc and Bartholdy, 2009). However, merger wave in Croatian banking system was driven by the strategic incentives in general, which implied effects of synergy as well.

Besides observing the number of banks, development of the banking system could be monitored through the sharp assets growth, mainly owing to the growth in assets of largest banks. Considering 94.2 billion HRK of total assets of 54 banks in the first half of 1999, and comparing it to the 403.0 billion HRK of total assets of 32 banks in the first half of 2012, it is obvious that total assets have risen more than four times. Although average annual increase in this period amounted to 23.8 billion HRK, considerable decrease in assets growth in last three years was noted, when average annual growth fell to the level of 11.2 billion HRK.

At the same time changes in concentration indicators were evident. Firstly, considering the concentration ratios[2] of several biggest banks in the industry, structural changes which resulted from previous merger processes could be noticed. While concentration ratio of two biggest banks fell slightly during the observed period, the same indicators for six and ten most important banks reported small growth. This indicates that historically banking system was mostly dominated by two most important banks while structural changes, that occurred with the M&A processes, led to a dispersion of market shares. Another concentration indicator is Herfindahl-Hirschman Index[3] (hereinafter: HHI) which provides even more complex picture of concentration in a particular industry. As there was significant change in bank number in previous years, shift of HHI was to be expected as well. During the observed period of ten years, value of HHI ranged between 1.169 and 1.417 units reaching its maximum value at the end of the first half of 2012. This level of concentration is considered as moderate and consequently should not generate any concerns on the domestic banking market.

Above mentioned changes in concentration indicators could be also explained by the process of privatization of domestic banks which played crucial role in the structuring of the nowadays banking system. Starting from year 1998 when only 6.7% of bank assets were in majority foreign ownership, there was a sharp changeover in ownership structure concerning the fact that at the end of the first half of 2012 even 90.6% of total bank assets referred to the banks with foreign ownership. After the

[2] a ratio that indicates the relative size of firms in relation to their industry as a whole
[3] HHI is calculated as the sum of the squares of the market shares of all companies competing in the market

rehabilitation program conducted by the government, several state-owned banks were privatized and became majority foreign-owned. It could be discussed if the incentive for the privatization is derived from the previous 1998-99 banking crises in Croatian banking system. One of the researches has shown that one of the outcomes of the crisis was the decision to sell the rehabilitated banks to foreign strategic investors and reasons which pushed government in such sales were country's growing foreign debt and deteriorating fiscal position (Kraft, Hofler and Payne, 2002). Other research concluded that banking crises play an indirect role in restructurings of the banking system, but the consolidation usually follows with the short time leg after the crisis (Cassis, 2011). In case of Croatia, merger wave was really remarkable few years after the period of banking crisis what actually confirms that the previously mentioned theory was correct. Among 17 banks that are currently owned by the foreign investors, the most important influence comes from Austria and Italy whose investors hold majority shareholding in 11 institutions. It is actually expected that the countries which are already good trade partners will try to improve their relations in financial sector as well. Thus, considering the short distance between the countries and relatively common cultural background (Erel, Liao and Weisbach, 2011), it was expected that Austrian and Italian capital influenced the Croatian financial sector.

Considering the evident influence of foreign investors it is interesting to observe whether the investment decisions were made mostly as a part of strategic plan to enter the banking system or the investors were though motivated by the performance of financial indicators of the observed banks. In case of four biggest banks, a process of banks' privatization was in most cases preceded by the process of rehabilitation program. According to the size of their assets, at the end of year 1999, the biggest four banks were following: Zagrebačka banka (26.66% of market share), Privredna banka Zagreb (16.59% of market share), Splitska banka (7.88% of market share) and Riječka banka (6.50% of market share).

Different from other three institutions, Zagrebačka banka didn't take part in rehabilitation program and its privatization was started with the process of international stock exchange listing which led to the changeover in the ownership structure. After several extraterritorial merger decisions, above mentioned bank is currently under control of Austrian Bank Austria Creditanstalt as a part of UniCredit Group.

Other three most important banks in Croatian banking system participated in the rehabilitation program which was operationally conducted by the State agency for deposit insurance and bank rehabilitation and which finally resulted in generating income from privatization, but at the same time in selling equity capital to the foreign investors from other European countries. Today, those three banks, after several merger transactions, are under control of Italian, Austrian and French majority owners.

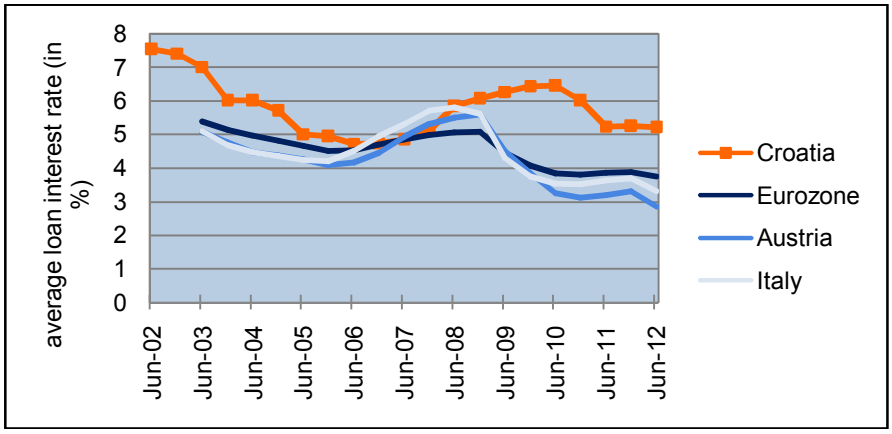
There is always a substantial debate about the model of privatization of previously mentioned banks, and not only these but smaller banks as well, which were under Croatian ownership before. Several theories which approve existence of state-owned banks could be mentioned, as they are created to address market failures or they should contribute to economic development and improve general welfare, but with the influence of fulfilling goals of politicians, it may also lead to corruption and misallocation (Sapienza, 2004). Anyway, many aspects of retention banks in state ownership or in their privatization could be observed, but it is not the exact target of this paper. It would be rather more interesting to examine what were the reasons which led foreign investors to enter the Croatian market and what kind of indicators could have been a trigger which pushed them to start buying shares.

From one point of view it could be assumed that investors were comparing rate of return in their domestic markets and in potential new market that they were penetrating. Such approach is

sustainable if investors found lucrative participating in Croatian market rather than in their systems because of the opportunity to achieve better results. In that sense, difference in interest rates shifts in Euro zone could be compared to the situation in Croatian banking system. Interest rate is defined as a charge to the borrower for the use of lender's assets which certainly contains some level of risk. In case of higher risk, debtor will be charged higher interest rate and in the case of lower risk, the level of interest rate will decrease proportionally. Considering these different level of risks, it is very common to include country risk as a collection of several risks which are associated with investing in a country and which will consequently influence on the level of bank interest rate.

The level of interest rate within ten year period in several different markets was analyzed and, considering strong economic relations with Austrian and Italian markets, averaged interest rates for house purchases in four different markets (Croatia, Euro zone, Austria and Italy) were compared. It is shown that there were deviation in interest rates, but even so, averaged interest rate on bank placements stayed somehow above European benchmarks which might be explained by higher degree of country risk specific for Croatian market, but equally as the intention of foreign investors to earn extra premium on Croatian market. Hopefully, this discrepancy will probably slightly decrease as the Croatian economy increasingly converges to European market. Some surveys found out that the effects of M&As are primarily expressed in three different ways: cost efficiencies, profit efficiencies and market power. An increase in market concentration allows the consolidated bank to exercise the additional market power through charging higher rates for services (Akhavein, Berger and Humphrey, 1997). Fortunately, it could be noticed that merger wave in Croatia has not directly influenced on prices of banking services.

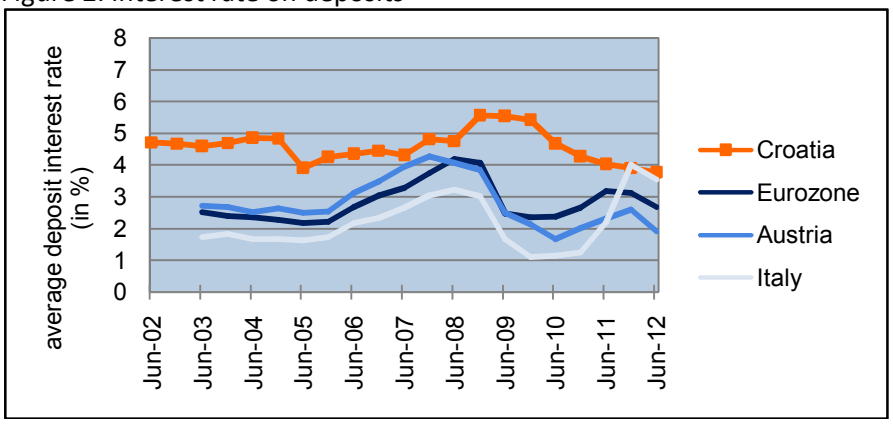
Figure 1: Interest rate on loans



Source: Croatian National Bank Bulletin, Statistical Data Warehouse of ECB

Similar trends were noticed in analyzing interest rate on long-term deposits of households. Though the shift of this interest rate in ten years period was not so obvious, clear difference between the deposits gains earned in Croatia compared to the average interest rate in Euro zone countries still exists. Although the differences between interest rates in Croatia and Euro zone are more evident at the loan transactions today, historical data shows that much significant differences between observed markets are seen in terms of interest rates on deposits.

Figure 2: Interest rate on deposits

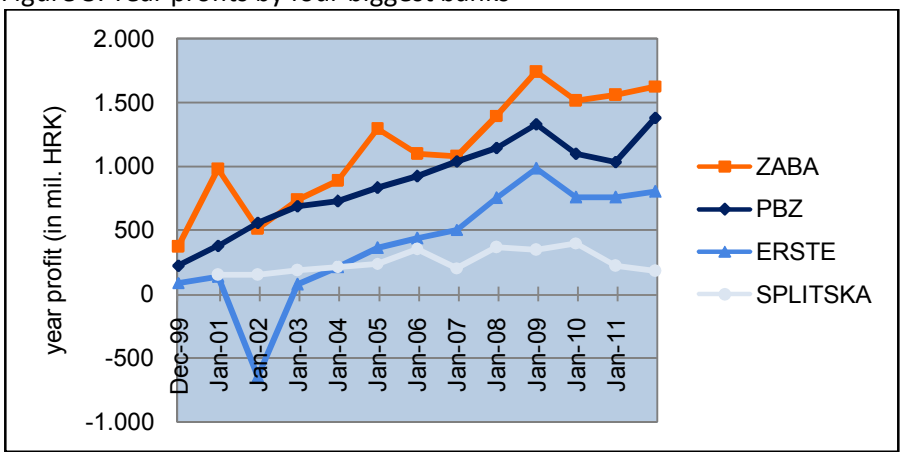


Source: Croatian National Bank Bulletin, Statistical Data Warehouse of ECB

Besides comparison of interest rates between different markets which could probably influence investor's decisions on bank integration, an interesting analysis of the effects of mergers on consumer loan interest rates was done. Based on the data of US banks, analysis shows that market concentration had different impacts on the level of interest rates considering the type of loans. While interest rates on unsecured personal loans have risen owing to bank mergers, at the same time interest rates on car loans have fallen. Further on the analysis explains that the first mentioned interest rate was affected by the market power of banks while in second case banks were using efficiency gains and passed it on to consumers (Kahn, Pennacchi and Sopranzetti, 2000). Therefore, besides observing the market the type of banking products and services should be considered as well.

Using the opportunity to acquire much cheaper sources of finance from abroad, with the aim of their placement in loans with higher interest rates, foreign investors considered entrance to the Croatian market as very lucrative. Efficient performance of the biggest banks can be monitored through year to year results, especially through the level of profits. Starting from the periods when they were acquired, banks generated high amounts of profits which even grew during the observed period of time. There is no doubt that profits earned by foreign investors exceeded direct costs of acquisitions and that investing decisions were fully reasonable. In order to emphasize the role of profits in decision making, the figure shows an overview of year profits of four biggest banks in the initial phase of M&A process.

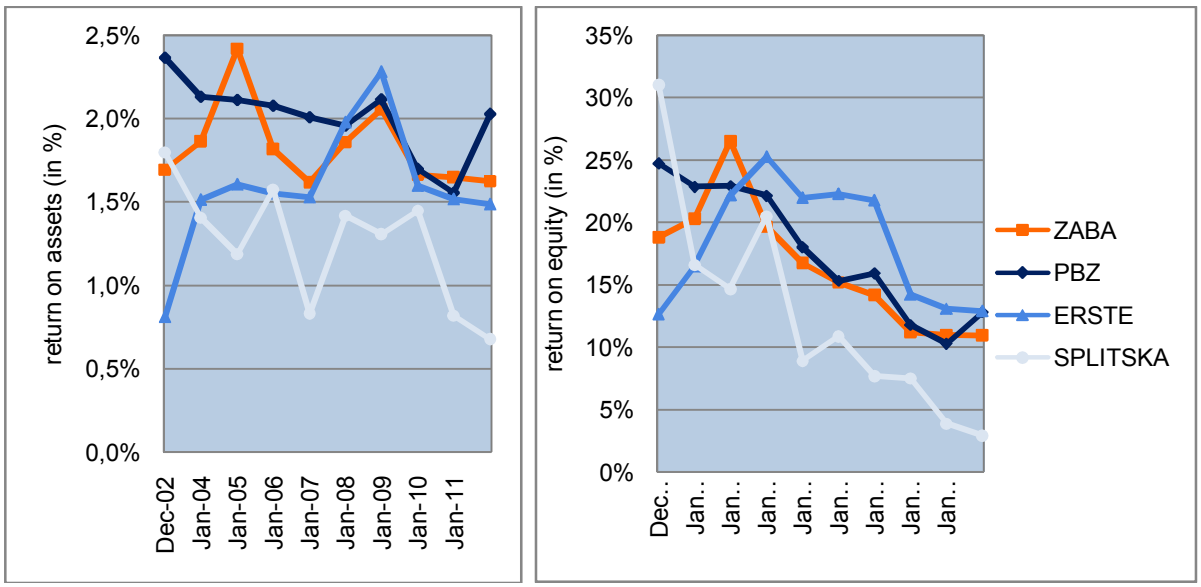
Figure 3: Year profits by four biggest banks



Source: Croatian National Bank Bulletin, Statistical Data Warehouse of ECB

Besides comparison of year profits, it is very common to compare some frequently used indicators of profitability which measure efficiency of bank management in terms of generating earnings. Indicator ROA (Return On Assets) shows how profitable are different kinds of company's assets in generating revenues. The second indicator usually measured is ROE (Return On Equity) which shows how much profit is generated from the shareholder's investments. Comparing the results of big four banks in almost last ten years, it is visible that the value of ROA fluctuated in interval of 0.50% to 2.50% with an obvious deterioration of results during the observed period. Only one of four banks improved its results, but mainly because of the realized loss in previous year and consequently lower starting point at the beginning of the observed period. Due to numerous recapitalizations, indicator ROE has recorded much stronger changes during the observed period. Concerning the level of capital and realized profits, indicator ROE fluctuated between 3% and 31% with an obvious slow down in last few years.

Figure 4: ROA and ROE indicators of selected biggest banks



Source: Croatian National Bank Bulletin, Statistical Data Warehouse of ECB

Previously mentioned results of the performance of banks indicate that banking business was and still is one of the most profitable and propulsive industries which subsequently make clear that investor's decisions about entering the market were reasonable. Especially, when the costs that investors paid to buy out shares of banks in rehabilitation program are compared to the gains or profits that they have earned during all these years, and putting it into relation with possible earnings that they could have earned in their domestic markets, it is easy to conclude that such a development of banking market favored investors of privatized banks. On the other hand, foreign investments had positive impacts on Croatian banking market as well, because foreign capital assured sufficient capitalization of banks and consequently adequate liquidity and solvency of banks which was very important in the process of structuring of financial system. It should also be mentioned that one of the effects of foreign investments is qualitative development of market participants which caused wider range of products and services available on the market.

2. Data and Method

After the short overview of the transformation of Croatian banking system stimulated by the implementation of the rehabilitation program and afterwards by the privatization of most important

banks, the incentive of investors to put their assets in some new potentially risky investments was questioned. In the literature about industrial organization two basic motives stand out: an efficiency motive and a strategic motive. Efficiency gains arise because takeovers increase economies of scale or scope. Strategic gains arise if M&As change the market structure and thus a company's competitive position and profit level (Coeurdacier, De Santis and Aviat, 2009). From the aspect of profitability, key financial indicators which analyze earnings showed that banks which were involved in M&A processes achieved very good business results. Possible explanations for defining the reasons for M&A processes in Croatia are probably these efficiency gains as the investors were motivated by the performance of the targeted bank. However, questionable is if they were motivated only by the performance of banks in the segment of profitability or there were also some other financial indicators which could be observed as relevant in the context of merger decisions. Besides that, it should not be excluded that some of the investors were not only motivated by financial reasons, but their decisions were part of strategic plan to enter the banking system and develop their business on some new emerging market.

Formulation of hypothesis was done on the assumption that integration decisions rely firstly on comprehensive analyses of financial indicators and consequently that financial indicators were key factors that impacted decision-makers when making integration decisions. With this assumption, the aim of the research was to compare the values of financial indicators of banks that were involved in M&A process and on the other hand financial indicators of banks which were not participants of M&A. Comparing the values of financial indicators of banks within and out of M&A process, it was assumed that between the banks which were selected as a target for M&A process exist some joint characteristics which made them different from those banks that were not part of concentration process. In fact, the aim of the research was to emphasize the role of comprehensive analysis of financial indicators in decision-making process by examining if the investors were really motivated by the performance of financial indicators.

Therefore, historical data on bank mergers and acquisitions in the Croatian banking system were used as well as different types of financial indicators. In fact, financial indicators are divided into six components and each of these components is subject of assessment to determine a bank's overall business condition. This model of uniform financial institutions rating system was firstly adopted in USA by the Federal Financial Institutions Examination Council in year 1979 and was used as a tool for evaluating the soundness of financial institutions.[4] The model is based on six essential components: the adequacy of capital, the quality of assets, the capability of management, the quality and level of earnings, the adequacy of liquidity and the sensitivity to market risk. After calculating the financial indicators for each of these components, rating system impose component rating and finally composite rating with the purpose of assessing aggregate strength and soundness of credit institution.

Previously mentioned tool for evaluating the financial institution was primarily used with the aim of grouping financial indicators according to their belonging components, while the role of this tool for rating each of these components will be omitted in this paper. Strictly regulated tool for supervising the operations of financial institutions requires collecting a wide range of information on bank's business activities which can effectively be used as a starting point for further research.

While the most important period of merger activities in Croatian banking system was the first half of last decade, the intention was to collect financial indicators data for the bank's activities in that exact period of time, but also in years with no real merger activities. Since this is a relatively long observation period, some of the financial indicators were not constantly used or were replaced with

[4] Federal Financial Institutions Examination Council: The Uniform Financial Institutions Rating System, 13 Nov 1979 and 19 Dec 1996, *Federal Register Vol. 61/245*

some upgraded financial ratios. Therefore, as some of the indicators have significant number of missing values which could indicate incorrect conclusions, these financial indicators were ejected from further analysis. Taking into account sufficient number of observations, quantitative analysis was based on 45 different financial indicators which were assigned to one of the above mentioned components according to their affiliation.

In the period from end of year 2000 to the end of 2009, 21 M&A processes were noted which actually changed the level of concentration on the banking market. In this context term "concentration" refers whether to acquisition of a majority holding in the bank capital or to acquisition of complete ownership rights in some credit institution. Most of these concentrations occurred in the first half of the last decade while in the latest period merger processes obviously slowed down.

For the purpose of selecting financial indicators which encouraged investors to select exactly one of the interesting banks, it was assumed that potentially interesting period for investors was the interval that preceded the point of time when the acquisition was performed. For example, if the acquisition of bank X was realized in April 2008, it is expected that interest in that bank was enhanced already in two previous time periods at least. Thereby, indicative periods for acquiring ownership were considered as June 2007 and December 2007.

Furthermore, the banks were distinguished according to their assets because it was assumed that in the process of acquiring new banks, investors were not interested in all market participants, but only in several banks with some similar features and of similar capacity. In other words, it was assumed that investors, who had capacity to buy shares of small-sized bank, were not at the same time capable to become a shareholder of biggest credit institutions and vice versa, investors in large banks were not interested to put their money into smaller banks. Considering that fact, several banks according to the asset size were selected as a potential target of purchasing. The selection of potentially interesting banks could never represent exact intention of investors, but limiting the number of potentially interesting banks could probably influence on better accuracy of the results. For example, after sorting banks by the criteria of asset size and calculating a percentile value for each bank in that order, banks which were 10 percentile above and banks which were 10 percentile below the position of the bank which was a real target for M&A process were chosen. Thus, 3 or 4 banks with the asset size above and 3 or 4 banks with the asset size below the targeted bank were selected and financial indicators of these banks were considered as significant in the process of investor decisions.

A method of classification or grouping of individual financial indicators, which had more or less impact on integration decisions and which consequently were used in building the decision tree, was used as a support in the statistical analysis and data modeling. This method was applied with the aim to define the relation of integration decisions and values of financial indicators, through assigning the intervals of financial indicators of banks which participated in bank integrations. As the values of financial indicators can be qualified by only two different attributes which represent participation in integration or on the other hand decision about avoiding integration, these binary values led to select the method of classification which is used as a fundamental support in building the decision tree. By iterative partitioning of values of individual financial indicators, attributes were split up into smaller intervals according to the criteria of indication of integration. As discrete, mutually exclusive values were taken in the research, building of a decision tree was developed on the basis of iterative dichotomiser 3 (ID3) whose concept was introduced by John Ross Quinlan (Quinlan, 1986). Actually, his research was later developed in introducing algorithm C4.5 which used information from iterative questioning for developing the decision tree. The concept of C4.5 was based on the set of data with their attributes which were further divided into more homogenous groups until the data became so similar that further partition was not feasible. It was important to select those attributes which

performed as optimal criterion to be placed as the root of the tree. Using the information theory based on the fundamentals of entropy or else calculating the information gain, the data with the optimal attribute to become the root were selected and the method was further recursively applied to the next level for the data in the leafs. The fact that attributes were expressed as a discrete variable with binary values and the condition that some of the variables were incomplete, it represents the reasons why there was chosen C4.5 classification method to develop a decision tree as a statistical tool in analyzing data. Furthermore, recursive partitioning of data has several benefits which are reflected as: making predictions is uncomplicated and easy understandable, it is resistant on data missing, the result of the model does not give a smooth response and finally, algorithms are easy to learn (Berk, 2008).

For the purpose of this research financial analysis was additionally supported by software Rapid Miner and application R commander (Rcmdr) (Venables, Smith and the R Core Team, 2012) which is based on the use of algorithm C4.5 that was already explained in the previous section. Using the entropy method from the set of data, a decision tree was constructed and limits of individual sets of data were defined which split the data regarding their various homogeneity. The final aim of the calculation was to estimate the weight of evidence as a measure of indication for bank integration and moreover to quantify a level of information value which indicates the significance of individual financial indicator in integration decisions. In fact, with the access to the results of calculated information value of each financial indicator, their predictability could be estimated and consequently financial indicators can be classified as more or less important in the process of decision making on possible mergers and acquisitions between banks.

3. Results of Statistical Analysis

Actually, calculating the information value of each financial indicator was done with the aim of defining predictability of individual financial indicator or estimating indication of financial indicators in the process of integration decisions (Howard, 1966). Therefore, the predictability is expressed through the statistical strength of financial indicators which define extreme high predictable financial indicators as those with values above 0.5, while the indicators with values between 0.3 and 0.5 are defined as high predictable etc.

After the statistical analysis of the given data, results show existence of three financial indicators with the extreme high predictability while the others have high predictability or less. Those financial indicators and their statistical strength are presented on the following table.

Table 1: Financial indicators with extreme high predictability

Financial indicator	Information value
six month growth of loans	0.71
ratio capital / assets	0.63
ratio received loans / assets	0.54
etc.	

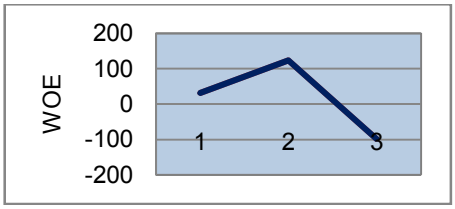
Source: Author's calculations

Highest predictable financial indicator with the value of 0.71 was six month growth of loans to the corporate clients and households. This indicator actually measures main activities of credit institution through giving loans to most important sectors excluding loans to financial institutions. Except emphasizing that this is the most predictive financial indicator, results of the analysis show that

according to the historical data, the highest indication for bank integration is calculated for the banks whose indicator of credit growth was located in the second group of split values. According to the defined limits for this indicator, it means that the most probable indication for bank integration can be expected by banks whose six month growth of loans is between 2.40% and 8.86%. Furthermore, the indication of integration for the values lower than 2.40% is still positive, but obviously not so powerful as in previous interval and financial indicators with values greater than 8.86% outcome the negative value of weight of evidence which actually means that there were scarce opportunities for bank integration from the aspect of this financial indicator. Indication for bank integration from the aspect of this financial indicator is illustrated on the following table and figure.

Table 2 and figure 5: Predictive values for credit growth indicator

No.	class limits	WOE	information value
1	-100% - 2.40%	32	0.04
2	2.40% - 8.86%	125	0.31
3	8.86% - 100%	-99	0.37
	total		**0.71**



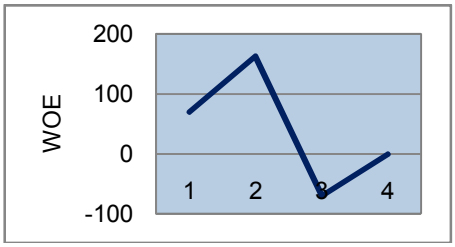
Source: Author's calculations

Reasonable explanation for selecting the second group of values as most predictable would be the fact that investors were interested in banks with stable credit growth or in banks whose activities were not characterized by extreme volatility. It means that banks whose credit growth was under 2% or even had negative values represented a warning signal to investors that core banking business was in some way unusual, while on the other hand banks with the credit growth above 9% represented institutions with excessive credit business which could be related to the higher rate of risk as well. In other words, progressive credit activities which are not supported with adequate capital background and other sufficient infrastructure could turn into the hazard business. Considering the comparison of average credit growth in years when mergers occurred, data shows that the banks which participated in bank integration had this financial indicator a little bit lower than the average value of banking sector.

Next financial indicator with extremely high value of predictability is ratio of capital and total amount of bank assets which actually demonstrate the sources of financing bank's activities. It could also be explained as a level of using the financial leverage because the more external financial sources are used the utilization of financial leverage is more obvious. By using the same method to create a decision tree, data set was split to four classes indicating the optimal homogeneity between different groups of data. By calculating further information value, this financial indicator is predictive as second best with value of 0.63. The highest indication for bank integration was shown by the banks whose ratio of capital and assets is located in the second group of split values and consequently this interval was the most indicative for further integration. Converting those results in numbers, it means that banks with values of observed ratio between 10.11% and 11.84% have the highest value of weight of evidence and therefore are the most indicative. Furthermore, the banks with lower degree of that ratio still have positive indication, while for banks whose ratio is above 12%, according to the historical data had very low indication to be the part of future integration. As before, illustration of results is presented on the following table and figure.

Table 3 and figure 6: Predictive values for indicator of ratio capital / assets

No.	class limits	WOE	information value
1	0% - 10.11%	70	0.09
2	10.11% - 11.84%	163	0.31
3	11.84% - 32.99%	-70	0.23
4	32.99% - 64.53%	-1	0
	total		**0.63**



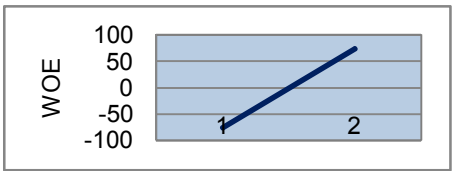
Source: Author's calculations

Before giving an explanation about the results of prediction for this financial indicator, it would be useful to present circumstances and adjustments of value for the mentioned indicator. In the first few years of this century the value of this indicator was at about 9% while from the year 2006 it started to grow sharply reaching the point of 14% at the end of year 2009. This fact is important for explaining the results of this analysis. Considering the fact that most of the integrations occurred in first half of the decade when the average value for this indicator was at 9%, it seems that indicative value for banks which participated in bank integrations was slightly higher than the average value. The explanation for this could be that investors, in the period of integrations, had more interest in banks with higher share of own capital because such decisions were more convincing and reduced the level of risks which usually appear when financing is not based on own sources. It should also be mentioned that in the observed period banking system was still under the influence of past rehabilitation program and privatization of banks and therefore investors were rather interested to invest in banks whose sources of finance were dependent on their own capital.

Finally, the third financial indicator with extreme high value of predictability is indicator from the segment of liquidity indicators and represents the ratio of received loans, as a source of finance, and total assets. It should be clear that besides the capital from the shareholders, the sources of finance are mainly based on liabilities which consist of deposits and received loans. In that way, sources can be further divided on domestic and foreign sources of finance. It is important to emphasize the foreign sources of finance because received loans were mostly foreign-owned, particularly from foreign investors who were interested in business activities on Croatian market. Information value calculated for this financial indicator was at 0.54 and data set was divided in two groups while the second group was estimated to be more indicative. It means that banks with ratio of received loans and total assets of 7.63% and higher had more probability to be the part of future bank integration. Apparently, there were also the banks, which integrated with some other banks, and had lower ratio of above mentioned, but this calculation was done to separate the groups of data concerning their predictive values. Results of the calculation are presented on the following table and figure.

Table 4 and figure 7: Predictive values for indicator of ratio received loans / assets

No.	class limits	WOE	information value
1	0 - 7.63%	-76	0.27
2	7.63% - 100%	74	0.27
	total		**0.54**



Source: Author's calculations

According to their business strategies, banks will choose the sources of finance which will support activities of granting loans. Generally, banks will try to maximize their profits by using the approach

of minimizing the expenses on received sources of funds and increase the interest income from granted loans. Therefore, it is very important to select funds which are appropriate in terms of costs. It could be supposed that banks, whose business activities are stable, get higher confidence and are better ranked in the market. With possession of better rating, the business with such banks would be more secure and the price for borrowing the money will be lower. Consequently, the banks with higher abilities to repay their debts will be less charged for the borrowed funds and they will probably more often take advantage of receiving loans from other entities on the market. Regarding that fact, it is expected from the investors to select the banks whose business is more confident and which will be more reliable in servicing their liabilities.

4. Conclusions

Regarding the obvious changes in Croatian banking system which was marked with numerous mergers and acquisitions of banks, the determinants which influenced the investors in their integration decisions were examined in the research. It should be mentioned that apart from the inevitable merger process, banking system was transformed by the specific rehabilitation program provided for the banks in difficulties and afterwards by the privatization of several banks. Even though, the research tries to define the reasons which motivated foreign investors to enter the Croatian market and what kind of indicators could had been a trigger which pushed them to bank integrations. Logically, investors were motivated by the performance of the targeted bank in terms of profitability, but certainly after the financial analysis, there could be found some other financial indicators which were observed as valuable in the context of merger decisions. It was assumed that if the investors were motivated by the performance of financial indicators, there could be found some joint characteristics of banks which had a potential to be the part of M&A process. Consequently, using historical data on bank mergers and acquisitions quantitative analysis of bank's financial indicators was done. As a support, a method of classification of individual financial indicators was used with the purpose to be a fundamental support in creating the decision tree. Final aim of calculation was to estimate the significance of individual financial indicator in integration decisions according to the historical data. The results of the analysis are probably surprising and were not possible to be forecasted in advance, but for each of them a logical explanation still can be found and what is more it could be a relevant starting point and helpful tool for observing future integration processes.

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Linking Resource Value to Sustainable Competitive Advantage: Investigation of Medium and Large Croatian Companies

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Abstract

In this study impact of resource and capability characteristics on sustainable competitive advantage is discussed. More specifically, the value of resources and its connection to competitive advantage and sustainable competitive advantage is examined, since according to Barney, value of resources is the only condition necessary for achieving sustainable competitive advantage. Although the above mentioned statement is widely accepted in strategy literature there is a lack of research on characteristics of resources, particularly value and rareness.

Empirical analysis was conducted on 265 large and medium-sized Croatian companies from all industries. Findings suggest that the companies with more valuable resources show higher levels of achieved competitive advantage. More specifically, resource value is positively related to all six examined elements of company's competitive advantage, but not all types of resources are equally relevant for its achievement. Among four groups of company's resources: physical, human, organizational and financial; physical resources proved to be the least relevant.

Keywords

Resource value, VRIN framework, resource-based view, competitive advantage

1. Introduction

Resource based view (RBV), rooted in evolutionary economics and the work of Edith Penrose (1959), focuses on relationships between company's internal characteristics and competitive advantage (Spanos and Lioukas, 2001). According to the VRIN framework, which is one of the basic concepts of RBV, if company possesses and exploits valuable, rare inimitable and non-substitutable resources and capabilities, it will achieve sustainable competitive advantage (Barney, 1991). But, only few empirical studies test the impact of resource characteristics on sustainable competitive advantage (Spanos and Lioukas, 2001; Newbert, 2007). As emphasized by Priem and Butler (2001), to infer that resources and capabilities are valuable and rare simply because they are related to competitive advantage is to assume that VRIN hypotheses that link resource characteristics to competitive advantage are factual and don't require any empirical confirmation. These hypotheses are in fact purely theoretical and for them to be supported empirical investigation is necessary (Priem and Butler, 2001; Newbert, 2008). Newbert (2007, 2008) also points that there is a lack of research on characteristics of resources, particularly value and rareness. Moreover, he analyses RBV-grounded empirical articles and concludes that, although the RBV is one of the most influential theories of strategic management, it has received only modest support that varies considerably with the independent variable and theoretical approach employed.

Furthermore, the dependent variable that resource based view tries to explain, i.e. the competitive advantage, although widely mentioned in strategic management, is not precisely defined. In other words, there is no consensus about the definition of competitive advantage, or the way it can be operationalized. Moreover, the terms performance and competitive advantage are often used as synonyms. The following section presents the theoretical background of two concepts analyzed: competitive advantage and VRIN framework, as well as theoretical propositions and hypothesis. Subsequent sections present empirical analysis and results.

2. Literature Review

The concept of sustainable competitive advantage was first introduced by Michael Porter (1985) in the analysis of competitive strategies, i.e. strategies that enable companies to achieve sustainable competitive advantage. According to Porter (1985), competitive advantage stems from the ability of company to create value for its buyers that will exceed the cost of its creation. Value is what buyers are willing to pay, and superior value stems from offering lower prices than competitors for similar benefits or unique benefits at a higher price.

According to Barney (1991), company has a competitive advantage when it is implementing a value creating strategy different from the strategies of its competitors. If competitors can't duplicate the positive effects of these strategies, competitive advantage is sustainable.

Peteraf (1993) defines competitive advantage as a sustainable above-normal returns which can be achieved only if four prerequisites are met. These prerequisites are resource heterogeneity, ex post limits to competition, imperfect mobility and ex ante limits to competition. Grant (2002) believes that the company has a competitive advantage when it earns a higher level of profits than its competitors. Foss and Knudsen (2003) criticize Barney's definition of competitive advantage, arguing that it is not clear what is meant by ''a unique value creating strategy that is not implemented by competitors''. They stress that the two main definitions of competitive advantage (Barney, 1991; Peteraf, 1993), are not related. In other words, company can continuously implement a unique strategy based on the resource acquired in a competitive market and thus, according to Barney, possess a sustainable competitive advantage. However, at the same time, it can generate only an

average, normal profit, which means that, according to Peteraf, there is no sustainable competitive advantage. Peteraf and Barney (2003) provide definition of competitive advantage that links this term to value creation and to demand side concerns. According to them, company has competitive advantage when it is able to create greater economic value. Economic value is defined as difference between the perceived benefits gained by the buyers and the economic cost to the company. This definition is consistent with the definitions given by Porter (1985), Barney (1991) and Peteraf (1993). Peteraf and Barney (2003) pointed out that there are multiple ways of achieving competitive advantage. Therefore, to achieve a competitive advantage, company doesn't have to be the best in all dimensions, but it must be superior in value creation.

Barney (1991) develops so-called VRIN framework, which states that valuable, rare, imperfectly imitable and not substitutable resources have the potential for creating sustainable competitive advantage. The value of resources lies in its ability to neutralize threats and enable company to exploit opportunities that arise in a business environment. Resource rareness implies that competitors don't have access to the particular resource, or that have limited access. Resources are imperfectly imitable if competitors can't obtain them on a particular market. If there is no other resource that could be used as an adequate and worthy replacement for the existing resource, existing resources are not substitutable. It is stressed that the value and rarity of resources are necessary conditions for achieving competitive advantage. But, for achieving sustainable competitive advantage, resources also have to be imperfectly imitable and not substitutable. Foss and Knudsen (2003) reflect on Barney's classification of VRIN conditions, and state that there are the only two necessary conditions for achieving sustainable competitive advantage: uncertainty and immobility. Barney, in his correspondence with authors concludes that the value of resources is the only necessary condition (Foss and Knudsen, 2003). Resources are valuable if they enable the company to design and implement strategies that improve its efficiency and effectiveness. It is important to emphasize that value of resources has to be estimated in the context of corporate strategy and the specific environment in which the company operates. Valuable resources that are not rare cannot be the sources of a competitive advantage. To achieve the competitive advantage, resource must be valuable and rare. However, this does not mean that valuable resources that are not rare are irrelevant for a company. These resources ensure the survival of the company and enable it to achieve competitive parity in the industry in which it operates. If company fails to exploit valuable resources, it will have the competitive disadvantage. If the resource that company possesses is not valuable, then it will not allow the company to choose and implement strategies that exploit opportunities and neutralize threats from the environment. Such resources are considered as weaknesses. Valuable resources that are not rare are considered strengths (Barney and Clark, 2007).
According to Barney (1992, 1995) resources and capabilities include financial, physical, human and organizational assets that the company uses to develop, manufacture and deliver products and services to customers. Financial resources include debt, equity, retained earnings, etc. The physical resources include machines, manufacturing plants and buildings. Human resources relate to the skills, knowledge, ability to make judgments, risk taking propensity and wisdom of individuals associated with the company. Organizational resources are history, connections, confidence, organizational structure, formal reporting structure, management control systems and compensation policies (Barney, 1995).

Although RBV is considered one of the most influential theories of strategic management (Powell, 2001; Priem and Butler, 2001, Newbert, 2008), its acceptance seems to be based more on the basis of logic and intuition than on the empirical evidence (Newbert, 2008). There are several studies that examine the connection between company's resources and performance. In most studies ''resource heterogeneity approach'' is employed, by which specific resource or capability is claimed to be valuable, rare, imperfectly imitable or non-substitutable, and then the amount of that resource or capability that firm owns is correlated with competitive advantage or performance (Newbert, 2007,

2008). This type of research provides evidence that a specific resource can help company to achieve competitive advantage, but does not verify the influence of resource characteristics (value, rareness, inimitability and non-substitutability on competitive advantage. Thus, according to the results of Spanos and Lioukas (2001), company's asset influences market performance, but not profitability. On the other hand, Accquah and Chi (2007) examine the relationship between firm-specific resources and firm-specific profitability, and conclude that firm-specific resources (corporate management capabilities, employee value-added and technological competence) enhance accounting-based and market-based measures of performance. Chimilievski and Paladino (2007) linked resource sustainability and capability dynamism to resource orientation (RO) and found that relationships between resource and capability characteristics and RO are significant. Wu (2010) divided resources in two groups, VRIN and non-VRIN, and concluded that both, VRIN and non-VRIN resources, are positively correlated to competitive advantages in low and medium volatility environments. In high volatility environments, only VRIN resources have influence on competitive advantage. But, analysis of the impact of individual characteristics of the resources on competitive advantage was not conducted in this study.

There are only few conceptual-level studies, i.e. studies examining underlying characteristics of resources and capabilities. According to study conducted by Markman, Espina and Phan (2004), competitive advantage is related to inimitability, but not substitutability of patents. Newbert (2008) found that value and rareness are related to competitive advantage. He points that there is a paucity of conceptual-level studies, particularly with respect to characteristics of value and rareness. So, in this article the value of company's resources and capabilities and its connection to competitive advantage will be investigated at the conceptual level.

Following the previous discussion, two hypotheses can be presented:

Hypothesis 1: The value of resources and capabilities that company owns and exploits is positively related to its competitive advantage.

Hypothesis 2: The value of resources and capabilities that company owns and exploits is positively related to sustainability of competitive advantage achieved.

3. Methodology

3.1. Data collection

The population is made of 1017 large and medium-sized Croatian companies with more than 100 employees. Such companies were identified based on the data from the Croatian Chamber of Economy. The study simultaneously employed online and mail survey. E-mail invitations containing a hyperlink to a web site with the online survey were sent to top managers in sample companies. A mail survey was sent at the same time, so respondents were able to choose the way they want to participate. A total of 271 completed surveys were collected, of which 265 surveys were usable. That resulted with the response rate of 26, 06% which is more than acceptable for this type of research (Drnevich and Kriauciunas, 2011; Protogerou, Caloghirou and Lioukas, 2008).

3.2. The measures

In operationalization of valuable resources and capabilities recommendations from Makadok (2001) and Newbert (2008) are adopted, as well as previously mentioned Barney's (1992, 1995) definition and classification of resources and capabilities. According to Newbert (2008), even if company

possesses the resources that have potential to create competitive advantage, that potential will not be realized if the company does not possess capabilities for resource exploitation. Furthermore, Makadok (2001) argues that no matter how outstanding company's capabilities are, they do not generate economic profits if the company fails to acquire the resources which will enhance the productivity of these capabilities. Therefore Newbert (2008) doesn't examine the characteristics of individual resources and capabilities, but the characteristics of relevant groups of resources and capabilities of enterprises. This means that value, or contribution in neutralizing threats and exploiting opportunities that arise in a business environment of physical (VA_PHY), human (VA_HUM), organizational (VA_ORG) and financial (VA_FIN) resources and capabilities is examined. The previous scale was assessed on a five-point scale ranging from 1 = not at all to 5 = entirely.

Competitive advantage is operationalized using earlier mentioned definition given by Peteraf and Barney (2003) through manager's perceptions of the company's success in comparison to major competitors, according to the following elements: a general advantage (or disadvantage) over competitors (CA1); sustainability of acquired advantage (CA2); the product/service quality and image (CA3); price of products/services (CA4); the production cost of product or cost of service delivery (CA5) and customer satisfaction with product/service (CA6). The scale was assessed on a five-point Likert-type scale ranging from 1 = much worse than competitors to 5 = much better than competitors.

4. Analysis and Results

Prior to hypothesis testing, descriptive statistics, and characteristics of the sample are shown. Table 1 shows the structure of the companies in the sample according to some main characteristics.

Table 1: Structure of companies in the sample according to the method of response, size and ownership

	online	mail	large	middle	domestic ownership	foreign ownership
Frequency	144	121	108	157	219	46
Percent	54,3	45,7	40,8	59,2	82,6	17,4

From the Table 1 shown above, it can be seen that 144 (54.3%) questionnaires were collected through mail survey, while 121 (45,7%) questionnaire was collected via online survey. Also, there are 108 (40,8%) large, and 157 (59,2%) middle-sized companies in the sample. It is revealed that 219 (82,6%) companies are in the foreign ownership. In Table 2 managers' perception of company's resource value is presented.

Table 2: Structure of managers' perceptions of resource value

	VA_PHY		VA_HUM		VA_ORG		VA_FIN	
	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent
1	3	1,1	1	,4	10	3,8	7	2,6
2	22	8,3	3	1,1	45	17,0	25	9,4
3	75	28,3	25	9,4	158	59,6	54	20,4
4	125	47,2	154	58,1	52	19,6	135	50,9
5	40	15,1	82	30,9	10	3,8	44	16,6

From the table it can be seen that the largest proportion of the respondents perceive that the company's physical, human and financial resources substantially contribute in neutralizing threats

and seizing opportunities that arise from the business environment. On the other hand, organizational resources contribute in neutralizing threats and seizing opportunities that arise from the business environment only to some extent. The smallest proportion of respondents thinks that the resources of their company are not valuable; i.e. perceives that the resources do not help company to neutralize threats and seize opportunities that arise from the business environment. Table 3 shows the structure of managers' perceptions of achieved competitive advantage, i.e. respondents' assessments of individual elements of achieved competitive advantage.

Table 3: Structure of managers' perceptions of achieved competitive advantage

	CA1		CA2		CA3		CA4		CA5		CA6	
	Freq.	Perc.	Freq.	Perc.	Freq.	Perc.	Freq.	Perc.	Freq.	Perc.	Freq.	Perc.
1	1	,4	1	,4	1	,4	2	,8	2	,8	3	1,1
2	15	5,7	20	7,5	6	2,3	18	6,8	46	17,4	67	25,3
3	94	35,5	87	32,8	67	25,3	111	41,9	116	43,8	1	,4
4	127	47,9	133	50,2	151	57,0	103	38,9	82	30,9	149	56,2
5	28	10,6	24	9,1	40	15,1	31	11,7	19	7,2	45	17,0

From the results shown in Table 3, it can be concluded that the largest part of the respondents perceive their company to be better than competitors by all six evaluated elements of competitive advantage. Slightly fewer respondents perceive that there is competitive parity between their company and competitors. Extremely few respondents answered that they perceive their company to be much worse than the main competitors. These results are not surprising, considering that the measure of competitive advantage is perceptive and subjective. In different words, it is possible that managers are biased in assessing competitive advantage of their company which leads to a better perception of the company in comparison to competitors.

Cluster analysis is performed to classify companies considering the value of its resources and capabilities. Number of categories is not given in advance, but analysis of the dendogram has shown that, with regard to the value of its resources and capabilities, the responding companies can be classified into two categories. Cluster analysis is than repeated, but this time with a fixed number of clusters. The aim of repeated cluster analysis is classifying companies into two clusters; one that contains companies with more valuable resources and capabilities, and one with less valuable resources and capabilities. From the table shown below it can be seen that first group contains 212, and second 53 companies.

Table 4: Grouping companies by resource value

Ward Method

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1	212	80,0	80,0	80,0
	2	53	20,0	20,0	100,0
	Total	265	100,0	100,0	

Mann-Whitney U-test was used to examine whether there is a difference in each of the four groups of resources and capabilities (financial, physical, human and organizational) among companies in first and second group. Given that the empirical significance of less than 5% for all four elements, one can conclude that companies differ in the value of financial, physical, human and organizational resources and capabilities (Table 5).

Table 5: Mann-Whithey U test of differences in physical, human, organizational and financial resources between companies with more, and those with less valuable resources and capabilities

Test Statistics[a]

	VA_PHY	VA_HUM	VA_ORG	VA_FIN
Mann-Whitney U	2424,000	768,500	2913,500	3456,000
Wilcoxon W	25002,000	23346,500	25491,500	26034,000
Z	-6,858	-11,050	-6,154	-4,688
Asymp. Sig. (2-tailed)	,000	,000	,000	,000

a. Grouping Variable: Ward Method

In the same way, using Mann-Whitney U-test, the difference in achieved competitive advantage between companies that have more valuable resources and capabilities and companies with less valuable resources and capabilities is examined. The results from Table 6 show that there is a significant difference in all six elements of achieved competitive advantage between companies with more, and companies with less valuable resources and capabilities, at the significance level of less than 5%. That leads to conclusion that both, hypothesis H1 and hypothesis H2, are supported.

Table 6: Mann-Whithey U test of differences in competitive advantage between companies with more, and those with less valuable resources and capabilities

Test Statistics[a]

	CA1	CA2	CA3	CA4	CA5	CA6
Mann-Whitney U	4149,500	4012,000	4101,500	4042,500	3950,500	4176,000
Wilcoxon W	26727,500	26590,000	26679,500	26620,500	26528,500	26754,000
Z	-3,203	-3,517	-3,407	-3,393	-3,560	-3,228
Asymp. Sig. (2-tailed)	,001	,000	,001	,001	,000	,001

a. Grouping Variable: Ward Method

Spearman's rho correlation was conducted on all variables. The results presented in Table 7 show that from 20 examined correlations, only five are not statistically significant.

Table 7: Spearman's Rho Correlation Matrix: competitive advantage and resource value

		VA_PHY	VA_HUM	VA_ORG	VA_FIN
CA1	Correlation Coefficient	,120	,187**	,240**	,156*
	Sig. (2-tailed)	,050	,002	,000	,011
CA2	Correlation Coefficient	,237**	,151*	,225**	,185**
	Sig. (2-tailed)	,000	,014	,000	,003
CA3	Correlation Coefficient	,134*	,165**	,195**	,091
	Sig. (2-tailed)	,029	,007	,001	,138
CA4	Correlation Coefficient	,105	,157*	,176**	,171**
	Sig. (2-tailed)	,087	,010	,004	,005
CA5	Correlation Coefficient	,033	,184**	,160**	,287**
	Sig. (2-tailed)	,590	,003	,009	,000
CA6	Correlation Coefficient	,110	,136*	,284**	,154*
	Sig. (2-tailed)	,074	,027	,000	,012

*p< 0.05; **p<0,01

All estimated correlations are positive, as predicted. It has been shown that connection between the value of physical resources and general advantage (or disadvantage) over competitors (CA1), price of products/services (CA4), production cost of product or cost of service delivery (CA5) and customer satisfaction with product/service (CA6) is not statistically significant. It can be concluded that the value of physical resources is the least connected to company's competitive advantage. Correlation between the value of financial resources and the product/service quality and image is not statistically significant. Correlation between all other elements is statistically significant, which means that human and organizational resources are significantly correlated to all six elements of competitive advantage (general advantage (or disadvantage) over competitors, sustainability of acquired advantage, the product/service quality and image, price of products/services, the production cost of product or cost of service delivery and customer satisfaction with product/service). So, based on the results presented above, the hypothesis H1 is supported. Also, it can be noted that all resource and capabilities groups (physical, human, organizational and financial) are significantly connected to sustainability of achieved competitive advantage, which leads to conclusion that hypothesis H2 is supported.

5. Conclusion

The findings of this study suggest that possessing and exploiting valuable resources and capabilities is connected to company's sustainable competitive advantage, which is in accordance with Barney's notion that value of resources is necessary condition for achieving sustainable competitive advantage. However, not all resources and capabilities are equally important for company. Results show that, while human and organizational resources prove to be significantly correlated to all six element of competitive advantage, physical resources are correlated with only two elements of competitive advantage: sustainability of competitive advantage and quality and image of products and services. Future researches should involve analysis of other resource characteristics and their relationship to sustainable competitive advantage and performance. In that way the VRIN framework as a whole could be verified.

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Evaluation of Lithuanian Tax System by V. Tanzi Qualification Diagnostic Indicators

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Abstract

The aim of the article – to evaluate Lithuanian tax system referring to V. Tanzi qualification diagnostic indicators verifying suitability of the method for tax system's evaluation. Research results revealed that Lithuanian tax system cannot be unambiguously evaluated according to all eight indicators. Lithuanian tax concentration largely complies with the recommendations of international tax specialists and four main tax types definitely dominate in Lithuania: VAT, personal income tax, profit tax, excise tax. In country's tax system there are low income taxes and it is not possible to evaluate if their administration is more expensive than the received incomes. Actual tax base is close to the potential one, and is increasingly approaching towards the potential base. Referring to the indicator of obligation, Lithuanian tax system may be evaluated as an effectively acting system.

Keywords

Lithuania, tax system evaluation, V. Tanzi indicators

1. Introduction

Neither tax system reform oriented to a higher collection of tax revenues will be effective if the reduction of tax number and administration costs of collection of tax revenues are ignored. It is important to evaluate country's tax system because when applying various evaluation indicators it is possible to distinguish problem aspects of Lithuanian tax system and to formulate argumentative preconditions in order to correct unfavorable situation regarding collectable tax revenues. There are many various solutions to evaluate and improve tax system, however, majority of them analyze separate elements of tax system but the tax system is a complex derivative that requires systemic attitude and complex evaluation. Tax system has been analyzed in complex only in several works so far, the author of one of them – V. Tanzi.

The aim of the article – to evaluate Lithuanian tax system referring to V. Tanzi qualification diagnostic indicators verifying suitability of the method for tax system's evaluation.

Tasks:

1. to review possible methods of evaluation of tax system and to distinguish theoretical aspects of application of V. Tanzi qualification, diagnostic indicators.
2. to analyze Lithuanian tax system during 2004-2011 applying V. Tanzi qualification diagnostic indicators, distinguishing the main problems of method application.

Methods of the research – evaluating country's tax system, literary analysis as well as data analysis and synthesis of State Tax Inspectorate under the Ministry of Finance of the Republic of Lithuania and Statistics Department have been carried out. V. Tanzi qualification diagnostic indicators were used to evaluate Lithuanian tax system. To process and systematize data, methods of grouping, comparison and graphic representation were used, systematic attitude and method of logical analysis were applied.

Research results revealed that systematically tax system may be evaluated by three methods. For the research of evaluation of Lithuanian tax system we have chosen V. Tanzi qualification diagnostic indicators. It has been determined that Lithuanian tax system cannot be unambiguously evaluated according to all eight indicators. Lithuanian tax concentration largely complies with the recommendations of international tax specialists and four main tax types definitely dominate in Lithuania: VAT, personal income tax, profit tax, excise tax. In country's tax system there are low income taxes and it is not possible to evaluate if their administration is more expensive than the received incomes. Actual tax base is close to the potential one, and is increasingly approaching towards the potential base. Referring to the indicator of obligation, Lithuanian tax system may be evaluated as an effectively acting system since during all the analyzed period more than 95% of potential tax system is collected though the costs of tax administration services functioning makes 1,27% from the collected tax amount what should be evaluated negatively and it is necessary to search for opportunities to reduce tax administration costs. The main drawback of V. Tanzi method – undefined principles of indicators' calculation and evaluation criteria. It is unclear how to evaluate some indicator's results and this indetermination creates preconditions for various interpretations that stimulate unambiguous perception and evaluation of situation, therefore, when applying this method, many conclusions depend upon an individual researcher.

Tax system, its effectiveness and ways how to evaluate country's tax system were analysed by Gill J. B. S. (2000); Norvaišienė A., Slavickienė A. (2005,2007); Skačkauskienė, I. (2007); Bivainis J., Skačkauskienė I. (2007,2009); E. Toder (2007). The work about optimum taxation was presented by Mankiw, et al., (2009). The work about the method of tax system evaluation referring to V. Tanzi qualification diagnostic methods was analyzed by Tanzi V. (2004, 2005, 2007); Rudytė D.,

Šalkauskienė L., Lukšienė L. (2009); Juozaitienė, L. (2009); Skačkauskienė, I. (2009); Jakštonytė G., Giriūnas L. (2010), et al.

2. Methods of Evaluation of Tax System

At present there is no one unanimous method of evaluation of state tax system. Systematically, tax system is evaluated by three methods according to (Bivainis, Skačkauskienė, 2009):

1. Classical taxation principles and indicators that express them;
2. V. Tanzi qualification diagnostic indicators;
3. J. Gill diagnostic indicators.

Each taxation principle is evaluated by indicators that express classical taxation principles: fairness, effectiveness, elasticity and simplicity of tax administration. Evaluating tax system by the first method, each taxation principle might be evaluated by quantitative methods and comparative analysis afterwards. The second method is used to evaluate how the tax system is functioning according to the answers suggested by the qualification diagnostic indicators.

J. Gill (2000) suggests to carry out such analysis explicitly analyzing revenue collection according to his set of indicators. The main idea of the method – when applying the model of compatibility (the highest efficiency is reached when separate parts of the system are consistent with each other) to analyse tax system systematically through the prism of tax revenue collection (Skačkauskienė, 2009). Analyzing tax system components from this aspect, their influence to the system is revealed which efficiency depends upon the harmony between the components. J. Gill distinguishes three groups of indicators that describe collection of tax revenues – inherent qualities of tax system, efficiency and productivity. Analysis of such diagnostic indicators reveals the gaps and positions of the process of revenue administration where the increvenueme administration does not correspond the expectations of the state and taxpayers.

Many scientists (Gill, 2000; Norvaišienė, Slavickienė, 2005; Buškevičiūtė, 2005; Rudytė, Šalkauskienė, Lukšienė, 2009; Jonikienė, 2010) agree that there is no unanimous attitude how to properly evaluate the efficiency of country's tax system, but they agree that efficiency of tax system may be evaluated not only by quantitative but also qualitative methods referring to their practical application, effective dialog between tax collectors and tax payers as well as other elements of taxation and tax collection.
Having analysed scientific sources about evaluation of tax system efficiency we may state that there are no methods of evaluation of country's tax system that would be unanimous and acceptable to majority of world theorists and practitioners. Tax systems are being formed during a long period of time, improved many times and corrected if needed. So, the evaluation of tax system efficiency preserves the attitude of an individual researcher towards the formulated conception of the problem and the selected method of research (Pajuodienė, 1993). In this article in order to evaluate Lithuanian tax system we have chosen V. Tanzi qualification diagnostic indicators out of three possible methods of tax system evaluation.

3. Questionnaire of V. Tanzi Qualification Diagnostic Indicators

V. Tanzi presents a diagnostic test of revenue productivity – a set of certain indicators where a question is presented for each indicator and using the obtained answers, it is possible to evaluate country's tax system positively, negatively or satisfactorily (referring to the whole of the answers) (Jakštonytė, Giriūnas, 2010). The indicators of tax system evaluation and questions defining them according to V. Tanzi qualification diagnostic indicators are presented in Table 1.

Table 1: **Indicators of tax system evaluation and questions defining them**

Name of the index	Question
Concentration index	Is a great part of tax revenues collected applying a relatively low number of taxes and tax tariff values?
Dispersion index	Are there not many taxes that provide low tax revenues but cause many problems while being administrated?
Erosion index	How actual tax base is close to the potential one?
Collection lag index	Are the taxes paid in due time, i.e. at the moment determined by the laws on taxes?
Specificity index	Does the tax system depend upon taxes that tariffs are specific (determined referring to products physical qualities – quantity, weight) but not upon the value?
Objectivity index	Is a great part of taxes determined according to objective criteria?
Obligation index	Does the tax system function properly and quite effectively?
Tax collection costs' index	Are the costs of tax collection minimal?

Source: Skačkauskienė, I. (2009) referring to V. Tanzi qualification diagnostic indicators application in Lithuanian example. Business, management and studies

Positive and negative but well-grounded answers to the author's questions allow evaluating efficiency of tax system of a particular country. From the presented diagnostic indicators the most meaningful are obligation index and tax collection costs' index, since they show the efficiency of tax system (Tanzi, 2007). The size of the gap between tax amount possible to collect according to the law and actual tax revenues as well as costs of tax administration also determine the efficiency of tax system activities of a particular country. Tax system is evaluated positively when 85-90% of all potential tax revenues are collected and expenses of tax administration compose 0,5% of all collected tax revenues (Jakštonytė, Giriūnas, 2010). However, not many countries at the same time reach the level of both indicators because the lag from the potential collection is much bigger, and better collection is possible only having greatly increased administration costs (Skačkauskienė, 2009). For instance, in Italy the mentioned expenses compose 0,5%, but it is considered that 35% of potential tax amount is not colleted. In Portugal it is considered that 10% is not collected, however, the tax collection expenses compose even 5% (Tanzi, 2004).

According to the experience of developed countries, successful functioning of tax system depends upon four complexes of factors: tax legal base, organization of tax services, training of their employees, system of qualification development, information of society about their rights, duties while paying taxes (Skačkauskienė, Bivainis, 2007). When applying these qualification diagnostic indicators, more attention is paid to the aspects of tax system productivity and administration simplicity (Rudytė, Šalkauskienė, Lukšienė, 2009). Besides, evaluation of tax system according to V. Tanzi qualification diagnostic methods is not exact due to indetermination of indicators' questions in both content and measurement senses.

4. Research Methods

Empirical quantitative research was carried out analyzing the data of Lithuanian tax system during the period 2004-2011. Statistical data was taken from the sets of annual reports of Statistics Department, Ministry of Finance and State Tax Inspectorate. Quantitative research performed applying V. Tanzi qualification diagnostic indicators involved indexes of concentration, dispersion, erosion, lag, obligation and tax collection costs. Indexes of specificity and objectivity have been analysed applying qualitative research. For the analysis of concentration index data about incomes from particular taxes of Ministry of Finance was used, the number of tax tariffs and tendencies of

their change were determined when analyzing particular law provisions regulating taxes. In order to determine from which taxes the most revenues were collected, the analysis of tax revenues structure was carried out.

Dispersion index was calculated referring to the data of national budget about the collected tax revenues, but due to the shortage of data the presumption was made that administration expenses of all the taxes are relatively equal therefore, Lithuanian tax system has not been evaluated according to this indicator.

To calculate erosion index statistical data of execution of tax revenues of National budget was used. The determined plan of tax revenues was equated to potential revenues from a certain tax, and the fact – actual collected revenues. To evaluate lag index the data of State Tax Inspectorate (STI) about the delays of tax liabilities of taxpayers and their amounts was used, the reasons of tax liabilities default were emphasized.

Specificity and objectivity indexes were evaluated by qualitative method. In the first case the collected revenues from these taxes were analyzed, for this purpose the analysis of tax revenues' structure and dynamics of the National budget was carried out. However, specificity index was not evaluated precisely because methodically it has not been determined how many of such taxes are to be and how to distinguish ineffective ones. To analyze objectivity index the tax revenues indicated in the tax collection report of the national budget were chosen, however, it is complicated to determine if all the taxes are objective and fair.

Obligation index shows the effectiveness of functioning of tax system, it is a gap between the amount possible to collect following the laws and actually collected tax amount. To evaluate this coefficient, the data about planned tax revenues by the State Tax Inspectorate and actually collected tax revenues was used. Tax collection costs' index was calculated referring to STI presented data about collected revenues and experienced expenses of tax administration. According to V. Tanzi (2007) this indicator should fluctuate in the range of [0;1].

5. Evaluation of Lithuanian Tax System Referring to V. Tanzi Qualification Diagnostic Indicators

During the period 2004-2011 the greatest part of revenues were collected to the national budget from tax revenues, every year averagely collected part of taxes in state's budget composed around 76,59% of all national budget's incomes. During all investigated period 2004-2011 country's tax revenues increased 56,91% from 11086,34 million LTL to 17395,72 million LTL. Having disclosed dynamic and structural image of tax revenues of Lithuanian national budget we may carry out a more detailed analysis referring to V. Tanzi (2005, 2007) qualification diagnostic indicators.

Concentration index helps to answer a problem question about tax tariffs' sizes and collected revenues. Having analysed a part of country's main taxes in tax revenues of national budget and changes of standard tariffs it is obvious that Lithuanian tax concentration (see table 2) largely meets recommendations of international tax specialists. Despite of fluctuations of standard tariffs in Lithuania the domination of four main taxes becomes obvious according to comparative weight: value added, personal income, profit and excises taxes. Other country's taxes involve only a small part of tax revenues of national budget (less than 10%) although during all analyzed period their comparative weight in all country's tax revenues was fluctuating but it might be possible to notice the decline tendency of incomes collected from other taxes.

The indicator of *dispersion index* shows if in the functioning tax system there are taxes that condition little tax revenues but their administration is as difficult as administration of other taxes that bring

higher country's tax revenues. Since State Tax Inspectorate does not provide administration expenses of each tax, while analyzing this indicator we make a presumption that administration of all taxes is equally complicated and requires expenses but quantitatively these administration expenses are not expressed. Therefore, this indicator is evaluated referring to particular revenues collected by taxes to the national budget.

As it is obvious from the below presented table 2, in the country certain taxes that bring variable and very small tax revenues exist and some taxes are changed or eliminated. To the state's treasury the lowest tax revenues were collected from lotteries and gambling games, sugar, means of transport, inherited property and other taxes that are presented in 2 below the bald line.

Table 2: Part of all Lithuanian taxes in the tax revenues (%) of national budget in 2004-2011

Tax	**Part of the tax in country's tax revenues**							
	2004	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**
VAT (%)	35,45	37,53	39,42	42,00	42,42	41,30	46,39	48,88
Personal income tax (%)	27,55	27,65	26,01	24,45	23,44	23,02	22,08	21,69
Excises (%)	16,76	15,82	15,22	15,05	15,39	19,79	19,31	18,27
Profit tax (%)	10,54	11,69	12,33	11,02	13,36	10,37	6,07	5,02
Tax on land (%)	0,28	0,28	0,26	0,25	0,22	0,3	0,33	0,32
Real estate tax (%)	1,94	1,65	1,5	1,3	1,16	1,64	1,9	1,58
Income deductions according to the Forestry Law of the Republic of Lithuania (%)	0,12	0,13	0,11	0,12	0,1	0,16	0,22	0,42
Sugar Taxes (%)	0,3	0,04	0,01	0,24	0,11	0,02	0,03	0,05
Lottery and gambling game tax (%)	0,12	0,19	0,14	0,16	0,15	0,19	0,16	0,16
Transport means taxes (%)	0,49	0,38	0,5	0,75	0,66	0,61	0,73	0,77
Taxes for environment pollution (%)	0,5	0,46	0,38	0,34	0,33	0,38	0,15	0,32
Charges (%)	0,63	0,64	0,58	0,57	0,77	1,21	1,38	1,34
Taxes of international trade and transactions (%)	1,34	1,22	1,17	1,12	1,15	1,09	1,14	1,18
Tax of inherited property (%)	0,02	0,02	0,03	0,04	0,03	0,03	0,02	-
Social tax (%)	-	-	2,34	2,59	0,71	-0,11	-	-
Income deductions according to the law on financing of road maintenance and development programme of the Republic of Lithuania (%)	3,94	2,3	-	-	-	-	-	-
Tax of commodity circulation (%)	0,01	0,00	-	-	-	-	-	-
Market taxes (%)	0,01	0,00	-	-	-	-	-	-

Source: composed by the authors referring to the data of the Ministry of Finance

Referring to the presented table we cannot evaluate country's tax system unambiguously by V. Tanzi dispersion index. Having performed data analysis it has been determined that in Lithuanian tax system there are quite a lot of taxes giving small incomes however, there is no data about particular expenses of their administration so it is not possible to state that some taxes are useless or should be changed.

Erosion index which shows relationship's cohesion between actually existing and potential tax base was determined referring to the data announced by the Ministry of Finance that are generalized in table 3.

Table 3: Implementation of the plan of main tax revenues of Lithuanian national budget (%) in 2004-2011

Taxes	2004	2005	2006	2007	2008	2009	2010	2011
VAT (%)	84,9	108	103,6	109,9	90,9	108,8	120	102,9
Personal income tax (%)	120,6	111,6	108	96,9	94	87,1	104,9	102,9
Excises (%)	100,2	103,4	106,4	106,8	95,3	99,7	93,2	91,4
Profit tax (%)	139,6	113,8	113,5	87,8	107,3	98	105,1	74,1

Source: composed by the authors of the work referring to the data of the Ministry of Finance

As the table 3 shows, during all analyzed period except 2004 the fact of collected incomes from value added tax exceeded the plan, till 2008 this may be explained by increasing consumption and from 2009 by a properly determined new standard tariff rate. Actual incomes of profit tax only in 2007 and 2009 lagged behind the potential incomes (plan), in 2009 this was influenced by a 20% increase in the standard profits tax rate, when the tariff was reduced again in 2010, the collected actual incomes exceeded the plan. Collection of personal income tax clearly shows country's economic decline since actual collected incomes did not implemented the plan during this period and this was influenced not only by changes of tariffs but also growing emigration extents, decreasing population number, increasing unemployment.

Till 2007 excises' incomes were higher than estimated and from 2008 collection of incomes did not implemented the plan, this might be influenced by changes of excises while implementing EU commitments. Generalizing we may state that actual tax base is close to the potential one. However, an open question still remains – how objectively and reasonably the state estimates potential tax base (plan).

Lag index is analyzed in order to evaluate if the taxes in the country are paid on time, i.e. following the determined terms. Recovery of tax arrears is implemented by regions' State Tax Inspectorates. Table 4 is presented for the evaluation.

Table 4: Lithuanian state budget revenue from fines and forfeiture in 2004-2011

Year	2004	2005	2006	2007	2008	2009	2010	2011
Plan, mln. LTL	35,84	36,34	40,40	46,57	76,57	76,57	76,57	46,05
Fact, mln. LTL	36,67	46,57	61,39	73,35	72,94	50,06	47,36	33,36
Fact's difference form the plan (+/-)	0,83	10,23	20,99	26,78	-3,62	-26,51	-29,21	-12,69
Plan implementation, %	102,3	128,15	151,96	157,50	95,26	65,38	61,85	72,44

Source: composed by the authors of the work referring to the data of State Tax Inspectorate

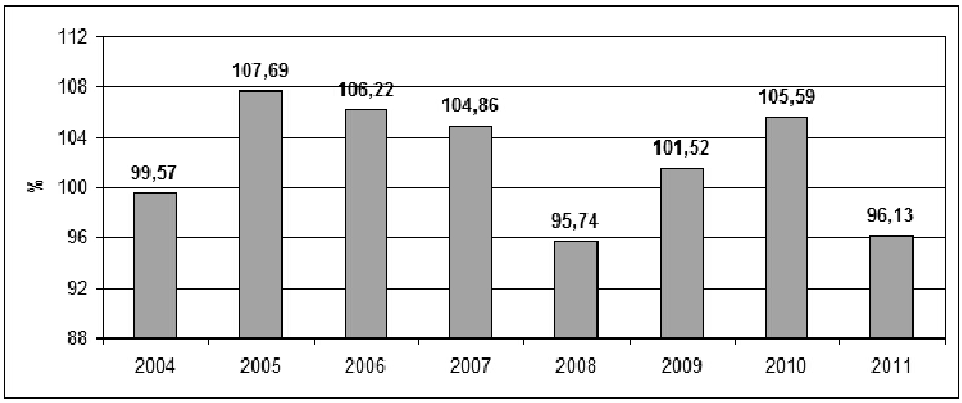
Referring to the data presented in table 4, we may state that when evaluating Lithuanian tax system the meaning of this indicator is evaluated negatively since quite a big part of revenue to the state budget is collected from fines and forfeiture for not paying taxes. This shows that not all taxpayers pay taxes on time or even try to hide them increasing the capacity of shadow economics. The positive aspect is that from 2008 till 2011 a tendency of decreasing revenue from fines and forfeiture is noticeable and it does not reach the expected plan. Consequently, state's budget revenues received less from fines and forfeiture from 2008 than it was foreseen, this shows that existing fine system for violations (delays in tax payment) became more effective since taxpayers pay tax duties on time. This can be influenced by fines for tax payment delays or their hiding, better financial condition of taxpayers or stronger consciousness of taxpayers.

Specificity index shows dependence of tax system upon taxes which tariffs are specific, i.e. they are determined referring to product's physical characteristics. In Lithuanian tax system there are taxes which tariffs do not depend upon the value of a product or service. These are excises, customs duty,

market tax, tax for state natural resources, oil and gas tax, pollutions taxes. However, it is impossible to evaluate Lithuanian tax system unambiguously by specificity index because V. Tanzi does not specify how many such taxes should be in a good tax system and how to evaluate which of the existing taxes is not suitable for country's tax system. While evaluating the collected tax revenues, it has been determined that excises are very important and necessary taxes for Lithuanian tax system, because they are one of four taxes that bring the highest tax revenues, whereas revenues provided by other taxes are significantly lower (see Table 2).

Obligation (constraint) index helps to evaluate the efficiency of functioning of tax system. The efficiency of functioning of tax system is shown by the gap between the amount of taxes possible to collect following the laws and the actual amount of collected taxes. The implementation of plan of tax collection is presented in figure 1.

Figure 1: Implementation of the plan of tax revenue collected administrated by the STI



Source: composed by the authors of the work referring to the data of the Ministry of Finance

In accordance of tax revenues with the plan, Lithuanian tax system may be evaluated as an effectively functioning system since during all analyzed period more 95% of potential tax amount is collected and the expenses of tax administration services compose around 1,27% from the collected tax amount (see table 6). During all analyzed period, planned tax collection differed from the actual tax collection around 7% when deviation of 10-15% is possible (Tanzi, 2007).

Objectivity index helps to evaluate the situation of tax system considering if the determined taxes are objective. In Lithuania all taxes at least with regard to taxation base are determined following objective principles (Rudytė et al, 2009). Table 5 presents tax revenues and estimated tax burden. In order to analyze objectivity principle we have chosen tax revenues indicated in the report of revenue collection of national budget.

Table 5: Change of Lithuania tax revenues, gross domestic product (GDP) and tax burden in 2004-2011

Year	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**
Tax revenues (mln. LTL)	11086	12899	15605	18631	21787	16463	15722	17396
GDP prices of that time (mln. LTL)	62997	72402	83227	99229	112084	91914	95074	78301
Tax burden (%)	17,60	17,82	18,75	18,78	19,44	17,91	16,54	22,22

Source: composed by the author of the work referring to the data of the Ministry of Finance

As we may see in the table 5, tax burden during analyzed period varied unevenly, until 2008 it increased from 17,6% to 19,44% and this was conditioned more by even growth of GDP rather than by tax revenues. The greatest leap is obvious when comparing 2005 with 2006 when tax burden

increased by 0,93%. In 2009 there were many changes in national tax system and the national economy started to decline, consequently, GDP decreased as well as colleted tax revenues, this conditioned the decrease of tax burden to 17,9%. Only in 2011 when national economy started to stabilize, GDP and tax revenues began to grow the tax burden composed 22,22% and was the highest during all analyzed period. During all the period of 2004-2011 the tax burden increased by 4,62%. If in this calculation base involving not only tax revenues to state budget but also to municipalities, State Social Insurance Fund budget, the tax burden would be higher. This indicator is not exact because shadow economy is not evaluated which, according to the experts, in Lithuania reaches 27%, although the department of statistics presents quite a softened indicator of shadow economy – 19% (Rudytė et al, 2009). Like every state, Lithuania while forming tax system is pursuing horizontal justice, that all who have equal opportunities would be taxed equally and vertical justice that those who have different opportunities would be taxed differently. With the growing taxpayer's incomes increasingly bigger part should be allocated for the taxes. During the analyzed period when all the indicators reflecting economy's scopes were growing, the scope of taxes paid to the national budget was growing as well but when these indicators were decreasing, the collected tax revenues were also decreasing (2009, 2010), this conditioned the changes of tax burden in Lithuania. Lithuanian tax system might be evaluated positively according to the objectivity principle.

The last indicator recommended by V. Tanzi – *tax collection costs' index*. The smaller the part of STI maintenance expenses compose in the total amount of collected taxes the higher efficiency of STI is. While calculating this indicator, all taxes, payments, fines collected by the institution that are transferred to the national budget also to Health insurance and Guarantee fund are involved in the taxes, payments collected by STI. STI expenses involve actual subsidies of tax administration programme including subsidies for investment projects (table 6).

Table 6: Collected revenues and expenses of Lithuanian STI in 2004-2010

Year	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
STI collected revenues, mln. LTL	10636,4	13722,3	16491,9	19620,8	23042,17	16412,2	15353,7
STI activities' expenses, mln., LTL	191,6	194,4	204,7	225,5	244,731	193,4	164,03
Tax collection costs, %	***1,80***	***1,42***	***1,24***	***1,15***	***1,06***	***1,18***	***1,07***

Source: composed by the author referring to the data of the Ministry of Finance

During the analyzed period till 2008 tax collection costs were decreasing, this showed that efficiency of tax administrator's activities was growing. The analysis let us state that in Lithuania the proportion of tax administration expenses and tax revenues varied from 1,8% to 1,06%. Lithuanian tax administration expenses do not exceed 2% limit, however do not fit in the limits of the interval [0;1], therefore, the conclusion might be that in Lithuania tax administration expenses are not minimum. Referring to this criterion Lithuanian tax system is ineffective it is necessary to search opportunities to reduce tax administration costs. This would positively affect not only the state but each economy subject that pays taxes.

6. Conclusions

There are various methods of evaluation of tax system but majority of them analyses only separate elements of tax system and do not analyze the tax system as a whole. Usually evaluation of tax system preserves the attitude of an individual researcher towards the formulated conception of the problem and selected research methods. Systematically the tax system may be evaluated according to three methods. V. Tanzi qualification diagnostic indicators are one of the methods that investigate tax system in complex. Eight indicators suggested by the author are analyzed that involve qualitative

and quantitative evaluation criteria. Each criterion has a question and referring to the obtained answers it is possible to evaluate country's tax system positively, negatively or satisfactorily (depending upon the whole of the answers).

During all analyzed period 2004-2011 Lithuanian tax revenues increased by 56,91%. Lithuanian tax system cannot be evaluated unambiguously according to all eight indicators. Evaluating concentration indicator we may state that Lithuanian tax concentration greatly correspond to recommendations of international tax specialists and in Lithuania four main taxes dominate: value added tax, personal income tax, profit tax and excises duties. Due to the shortage of data, dispersion indicator cannot be evaluated objectively, possible only to say that there are low income bringing taxes and it is impossible to evaluate if their administration is more expensive than received incomes. According to erosion indicator it is possible to state that actual tax base is close to the potential one and is getting closer to it. Evaluating lag index we may highlight that quite a number of revenues is collected from fines and forfeiture due to not paying taxes, therefore it is evaluated negatively. Evaluating specificity index it has been determined that in Lithuanian tax system there are taxes which tariffs do not depend upon the price of a product or service, but some of them for instance, excises bring high revenues to the national budget, so the evaluation of the index is not clear. According to obligation indicator Lithuanian tax system may be evaluated as an effectively functioning system because during all analyzed period more than 95% of potential tax amount is collected, although the expenses of functioning of tax administration services make around 1,27% from the collected tax amount and do not fit in the interval [0;1], what should be evaluated negatively and it is necessary to search for opportunities to reduce tax administration costs. The essential drawback of V. Tanzi method – undefined principles of indicators calculation and evaluation criteria. It is not clear how to evaluate certain obtained indicator's results positively or negatively. This indetermination forms preconditions various interpretations that conditions unambiguous perception of situation and evaluation therefore when applying this method many conclusions depend upon an individual researcher.

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Incorporating Anglo-American Reorganization Provisions in Bankruptcy Law: A 10-year Lesson from Thailand*

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Abstract

This paper argues the adoption of Anglo-American type of reorganization provisions into national bankruptcy law shall be cautious. Since Thailand started to accommodate such provisions, reorganization, apparently, has limited usefulness – benefitting only large-scale debtors because it does not fit with the nature of Thai business culture, i.e. the borrowing-lending relationship and less-than-arm's length business connections. Debt restructuring led by the central bank in cooperation with commercial banks, instead, is overwhelmingly more successful, efficient, and effective because any ailing firm can renegotiate its borrowing contract rather easily in the low transaction cost environment. The adoption of non-indigenous provisions shall be made prudently.

The argument applies towards the standardization of insolvency legislation. Standardizing bankruptcy procedures shall be made carefully and national economic conditions including local business nature and uniqueness are worth examined before any enactment or amendment. Otherwise, benefits of international trade and investment would be achieved at the expense of economic efficiency.

Keywords

Reorganization, bankruptcy, Thailand, standardization of law, debt restructuring

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1. Introduction

The Asian Financial Crisis in 1997, and its later contagious effect on the global economy, prompted Thailand to amend many business-related laws in order to cope with economic adversaries. One of them was bankruptcy legislation which has been amended in 1999 to incorporate reorganization provisions allowing a corporate debtor to remain in business given creditors' consent as an option to liquidation.

Reorganization provisions are featured in Anglo-American legal practices such as the famous US Chapter 11 in US Bankruptcy Code and the Administration in UK Insolvency Act of 1986. Many countries adopt this type of provisions while others remain to their liquidation-based bankruptcy. Reorganization is available only for corporate debtors, not for personal debtors. The debtor in this paper refers to the corporate debtor.

This paper wants to review, in the context of Thailand, whether the adoption of reorganization is appropriate. In other words, is it economically efficient for Thailand to use this proceeding? If not, reorganization is not the answer to bankruptcy universally and the attempt of UNCITRAL to encourage the harmonization of insolvency laws and the facilitation of cross-border insolvency are plausibly disagreeable. Therefore, variation of several bankruptcy proceedings must exist across countries depending on their economic fundamentals.

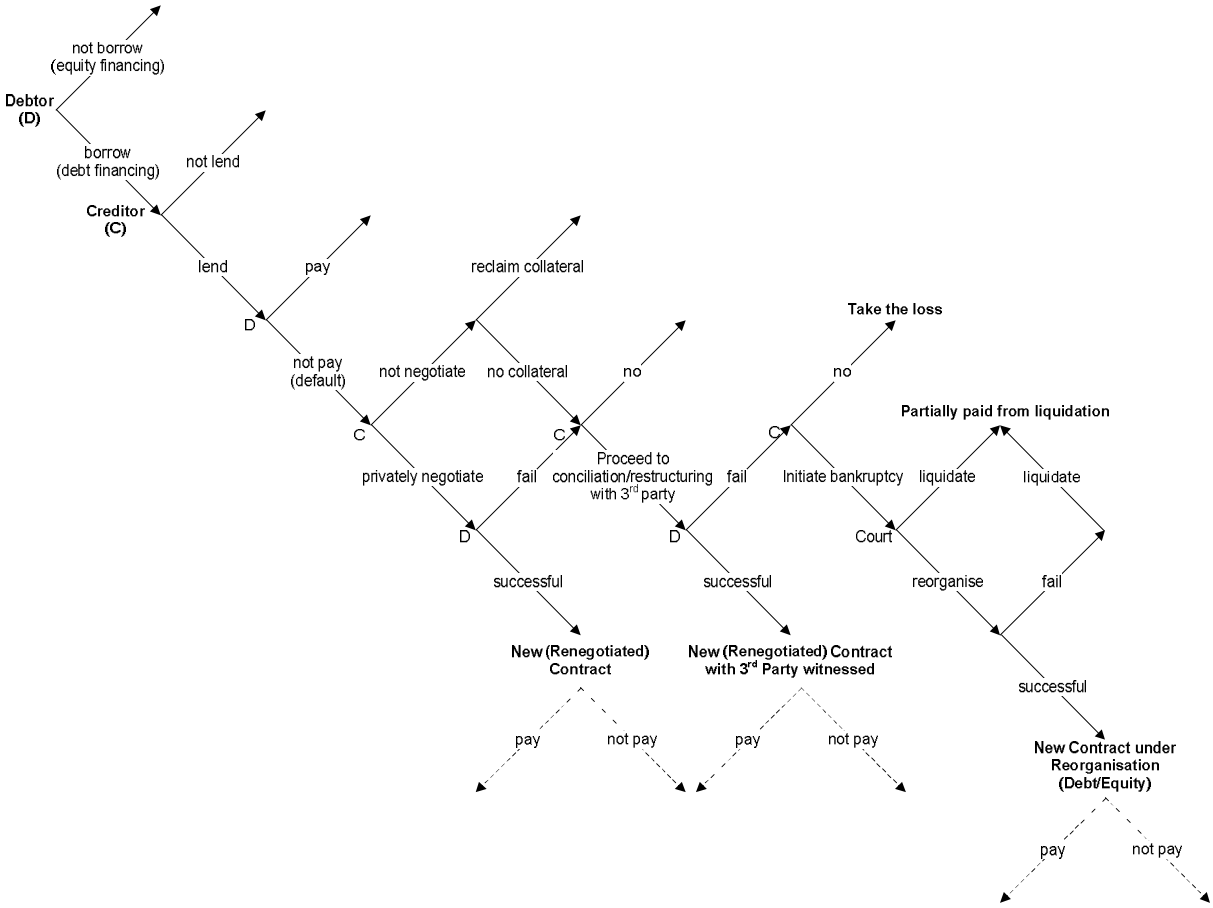
The paper is organized in 5 sections. After the introduction, Section 2 provides some essential basics on bankruptcy from economic perspective. Section 3 focuses on evidences of Thailand's insolvency legislation and private workouts. UNCITRAL's initiatives are briefly examined and followed by implications from Thailand's perspective in Section 4. Section 5 concludes this paper with recommendations.

2. Basics on Bankruptcy

Essentially, bankruptcy is one of many important components in a borrowing-lending relationship. It is a legal procedure which is usually implemented when all other options have depleted after the debtor's asset is insufficient to service the creditors' claims. Bankruptcy is not a stand-alone process but a sequel to many other attempts after the event of debtor's insolvency. To analyze bankruptcy legislation, it is vital to consider it in the context of the borrowing-lending relationship in general. Considering only the law itself would lead to the misperception and may induce many undesirable and unintentional behaviors of creditors and debtor.

The nature of borrowing-lending relationship is sequential and, many times, recursive. Figure 1 illustrates this in the form of decision tree. We can see that bankruptcy is just one branch of possible alternatives that creditors and/or debtor choose. Bankruptcy is optional, not mandatory. Before reaching the bankruptcy procedure, many other procedures have been tried.

Figure 1: A Simplified Decision Tree of Borrowing-Lending Relationship including Bankruptcy with Reorganization



2.1. Insolvency and bankruptcy in economics perspectives

Insolvency is a circumstance whereby the amount of debt owed to creditors exceed the assets owned by the debtor. Subsequently, full repayment of all debts is impossible. Since all debts are not due at the same time, some creditors are in the advantageous position to have their debts fully repaid at the expense of other creditors (which have to bear the loss transferred from the debtor). The debtor's default is a tell-tale of insolvency; however, it may be used strategically to induce renegotiation with creditors.

Without the original borrowing contract, there would be no insolvency. In other words, the borrowing-lending relationship or contract is a prerequisite of insolvency. More importantly, more than one of such relationship is a necessary condition for insolvency.

Since the debt contract involves many periods, uncertainty, thus, plays a significant role. Creditors bear the risk of debtor's moral hazard. The debtor, in the mean time, bears the business risk. When the situation changed and the debtor is insolvent, there is an opportunity for the debtor to renegotiate with creditors for plausible solution. For a single creditor, it is straightforward: if the creditor is not satisfied, she would take over the debtor's asset; otherwise, the original contract would be replaced by the renegotiated new contract.

However, some factors that may prevent such renegotiation: number of creditors, amount of loan taken from each creditor, debtor's business outlook and the possibility of further default. These

factors influence transaction cost of renegotiation. When the transaction cost is sufficiently low, renegotiation would eventually give the economically most efficient outcome (Coase, 1960). Unfortunately, the level of transaction costs within each relationship cannot be ascertained. A debtor, for instance, with more creditors, *ceteris paribus*, would face more difficulties trying to convince diverse creditors than another debtor with fewer creditors. Even they had agreed on renegotiated terms, there is no guarantee against future debtor's default. This heightens transaction costs further. By backward induction, creditors may not be willing to renegotiate from the outset.

Therefore, bankruptcy is created to overcome these problems. It accelerates all debts with different maturities to the present and provides the protection for debtor's assets against any claim using usual legal means (the 'stay'). The faith of the debtor is being decided by creditors' voices which are determined by the proportional claims over the debtor's assets (or *pro rata* or *pari passu* basis). The debtor could be liquidated or reorganized depending on its economic valuation. Under *liquidation* or *piece-meal liquidation*, debtor's assets are sold on a piece-meal fashion, usually through highest-bidder auction; cash earnings (or *realization*) from the sale will be distributed to all creditors according to the predetermined classification. The debtor firm could be sold as a whole which is called *going-concern*. Meanwhile, *reorganization* provides the possibility for the debtor to continue through organizational and/or managerial restructuring to improve its efficiency.

It is vital for bankruptcy legislation to direct the debtor's assets to the highest valuation. Such valuation is based on the creditors' perspective towards the debtor. With low transaction cost, creditors' valuation of the debtor's assets would be close to the real economic value. But when the transaction costs are high – particularly, when there are many creditors, creditors' valuation is diverse. Each creditor does not care what the real value of the firm as a whole is as long as they are paid. The mechanism design of bankruptcy legislation shall concern about this discrepancy.

It is worth noting that bankruptcy is one of all available alternatives to solve insolvency (see Figure 1). Principally, bankruptcy is a mechanism for debt renegotiation with the court acting as an umpire. Debt renegotiation could be done through various other mechanisms.

2.2. Alternatives for debt renegotiation

There are many venues for debt renegotiation. Certainly, the original borrowing-lending relationship determines what alternative is preferred. Economically speaking, they would select the one with the lowest expected cost. However, the cost and the outcome of each option cannot be ascertained from the outset. They normally proceed gradually from the least cost one to the costlier. Meanwhile, their net benefits from early settlement decline over time and more complex proceedings. Generally, we can categorize these alternatives into two according to their legal binding force.

2.2.1. Non-binding alternatives

For non-binding alternatives, the debtor settles with creditors privately for whatever solution they had reached – known as private workout. The debtor firm may cease to exist or may continue depending on the agreement. Conditions for such solution are information symmetry, especially the value of the debtor firm is aligned and mutually perceived by all parties; the transaction cost for negotiation is sufficiently low; creditors are certain with their entitlements and the debtor will be abided by the agreement even without any legal enforcement (including no debtor's shirking in the future). If either party does not follow this agreement, there is no specific legal consequence except their *a priori* rights from the initial contract.

2.2.2 Legal-bounded alternatives

When non-binding attempts are unsuccessful, legally-binding alternatives are still available. They may decide to draft the new contract to amend the original debt contract (usually known as compromise contract/agreement or contract of composition) which effectively replaces the rights, duties and entitlements of the original one with the newly negotiated one. Bankruptcy legislation in many countries legally recognizes and endorses this kind of private agreement (such as UK Administrative Receivership led by the bank (Armour and Frisby, 2001)). However, the debtor may strategically negotiate with some creditors and leaving other creditors vulnerable to this new agreement. In this case, the formal bankruptcy is required to prevent such debtor's strategic and opportunistic behavior.

Noting that at this stage the transaction cost is presumably high and the debtor's and creditors' valuation of the firm are misaligned. Normally, these approaches introduce the third party to be a mediator or conciliator. This third party shall have some information of the debtor to facilitate the solution to insolvency. It could be financial institutions who know financial conditions of debtor and creditors or, in the most extreme case, the court using the formal bankruptcy procedure.

Non-bankruptcy procedures may fail to recognize all creditors' entitlement. Bankruptcy is publicly known and all creditors shall be called in to claim their rights. This prevents creditors being taken advantage of either by the debtor or other creditors. Under bankruptcy, there are two orientations: liquidation- and reorganization-orientations as discussed earlier. In some countries, bankruptcy is solely liquidation whilst in some others incorporate the possibility of reorganization into the law. No country has only reorganization.

2.3. Efficiency of insolvency alternatives

Choosing among many approaches for insolvency is difficult for both parties. For bankruptcy, the court also has difficulties choosing between liquidation and reorganization (if available). It is always arguable that what is relatively more efficient. But it is impossible to pinpoint which procedure economically superior than another (White, 1998).

All choices are conditional on how the debtor relates with his creditors originally based on their original borrowing-lending contract (Thavornyutikarn, 2006). Additionally, Stiglitz (2001) asserts the importance of economic fundamentals of each particular country on the optimal balance of different procedures. Economically speaking, all procedures, legally binding and non-binding, shall be available to channel the troubled company to its highest valuation; hence, the economic efficiency is achieved. The mechanism design of bankruptcy law shall reflect this concept and utilize the nature of the initial debt contract without focusing solely on legal substances and proceedings. Table 1 summarizes appropriate procedures for insolvency under different conditions between debtor and creditors.

Table 1: Appropriate Procedures for Insolvency under Different Conditions

Conditions	*Appropriate Procedures*			
	Legally non-binding	**Legally binding**		
		Private Agreement w/ Third Party	Formal Bankruptcy	
Original Debt Contract (before insolvency)				
Debtor's asset specificity/non-verifiable variables/non-market assets (human capital)	Low	Low-Medium	High	
Separation between ownership and control	No – Low	Low – Medium	High	
Number of creditors	Few	Not many	Many	
Amount of debt	Not large	Relatively not large	Large	
Length of contract	Short	Relatively short	Long	
Diversity of debt proportional to each creditor	Very similar	Similar – Diversified	Highly Diversified	
Repeated relationship between debtor and creditor	Regularly repeated	Repeated	One-off – irregularly repeated	
Likelihood of moral hazard	Low	Medium	High	
Ease of monitoring by creditors	Easy	Easy - Medium	Difficult	
Legal enforcement of original contract	Yes	No	No	
Renegotiated Contract (after insolvency)				
Ease of renegotiation	Easy	Medium	Difficult	
Difference between the company's value perceived by the debtor and creditors	Low	Low-Medium	High	
Differences of company's value perceived by different creditors	Low	Low-Medium	High	
Likelihood of debtor's shirking (moral hazard after renegotiation)	Low	Low-Medium	High	
Accuracy of market valuation of the company's value	High	Medium-High	Low	
Value of the company as a whole	Depending on negotiation	Depending on negotiation	*Liquidation*	*Reorganization*
			Low	High
Possibility of future recursive debt contract	Depending on negotiation	Depending on negotiation	Low	High
Legal enforcement of renegotiated contract	No	Yes	Yes	

3. Thailand's Amendment of Bankruptcy Legislation and Lessons Learned

This section explains how Thailand amended its bankruptcy legislation to incorporate the reorganization-based procedure and what the empirical results are. There was a private alternative attempt to bankruptcy during the same period which worth considering and comparing.

A 1997 Asian Financial Crisis exerted tremendous pressure on Thailand's economy. Many companies went out of business including 56 financial institutions (IMF, 2000). Thailand was believed to be the origin of this contagion (Kaufman, Kruger, and Hunter, 1999). Thailand, later, took IMF Programme

and the reform of bankruptcy act was one of many institutional repercussions and legal reforms (IMF, 2000).

An inclusion of reorganization clauses was the highlight of Thailand's bankruptcy reform. Previously, corporate debtor under bankruptcy must be liquidated by court-appointed receiver (absolute receivership).

3.1. Evidence of reorganization in Thailand

After the amendment of Bankruptcy Act in 1998, many distressed corporate debtors have been through the process of reorganization. Thavornyutikarn (2006) analyzed the empirical evidence on this using a firm-level panel data of 166 companies in various stages of reorganization between 1998 and 2000 and limited dependent variable econometric analyses. The results were the characterization of corporate debtor at each step in reorganization. Table 2 summarizes the characteristics of those firms explained in term of its effects on probabilities being admitted into reorganization and being successfully reorganized respectively.

Table 2: Characteristics of Corporate Debtor Entering to and Exiting from Reorganization in Thailand

Characteristics	Probability of Entry to Reorganization	Probability of Exit from Reorganization*
Asset Specificity (total asset/number of employees)	n/a	–
Amount of debt	+	n/a
Number of creditors	+	–
Proportion of debt owed to financial institution creditors	+	+
Proportion of debt owed to trade creditors	+	–
Difference between interest expenses and earnings	–	–
Proportion of unburdened assets (working capital/total assets)	–	+
Operating revenue per employee	n/a	+
Proportion of operating expenses to total assets	n/a	–

Source: simplified from Thavornyutikarn (2006)
Notes: A shaded box indicates the contradiction with what it should be (compare with Table 1);
* refers only to successfully reorganized firms

Thavornyutikarn (2006) discovered some discrepancies in the Thai reorganization as follow. The procedures was inclined towards the debtor with many financial institution creditors which shall not using reorganization but the private workout led by those financial institutions (Eisenberg and Tagashira, 1996; Hoshi, Kashyap and Scharfstein, 1996) or something similar to a privately-appointed (bank-appointed) administrative receivership of the UK (Armour and Frisby, 2001). This is further discussed below in 3.2.

Moreover, Thailand's reorganization was against trade creditors which are more affected by debtor's insolvency than financial institution creditors since they have no ability to diversify their risks.[1] And because they are vital to the continuity of the distressed debtor (Biais and Gollier, 1997), reorganization would be less likely to be successful if they are less protected (Sautner and Vladimirov, 2012). Biais and Gollier (1997) also asserted that trade creditors can reduce information asymmetry between the debtor and other creditors. Trade creditors relate with the debtor in a more repeated fashion and sometimes have lower costs of monitoring the debtor (see Table 1). Thus, they are presumably good informants which shall be included in reorganization in helping all creditors to realize the real value of the firm. This is another shortfall of the Thai reorganization provisions.

Asset specificity is another dimension which was not concerned by reorganization provisions. A corporate debtor with higher asset specificity tends to have lower market value for such specific assets and reorganization shall preserve those values. Empirically, the mechanism did the opposite.

A number of creditors worked oppositely at the entry and the exit. It did increase the probability of being accepted into reorganization since the transaction costs could be prohibitively high for any private workout. But it shall not be significant in determining the chance of being successfully reorganized because the procedure must be able to extract some information from the debtor about its real value. This implies information asymmetries had not been alleviated in the process.

After the recent recollection of data, we discover interesting sets of statistics. Table 3 shows the petition for reorganization according to the database of the Central Bankruptcy Court.[2] Table 4 indicates statistics of bankruptcy cases from the Central Bankruptcy Court.

Table 3: Petition for Reorganization, 1999 – 2012

Year	Reorganization Petition filed by		Total Reorganization Petition	Ratio of Debtor/Creditor
	Creditor	*Debtor*		
1999	3	2	5	0.67
2000	9	20	29	2.22
2001	2	0	2	n/a (creditor)
2002	0	1	1	n/a (debtor)
2003	0	2	2	n/a (debtor)
2004	0	8	8	n/a (debtor)
2005	1	5	6	5.00
2006	3	15	18	5.00
2007	3	26	29	8.67
2008	4	1	5	0.25
2009	n/a	n/a	n/a	n/a
2010	3	28	31	9.33
2011	14	17	31	1.21
2012*	3	24	27	8

Source: Online Database, Central Bankruptcy Court
Note: * as of July 2012

[1] Even in the US, where its Chapter 11 is famous for having inclination towards the debtor. The Bankruptcy Code was revised to provide better protection for trade creditors under Section 546(c) and 503(b)(9) of Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) in 2005.

[2] Accuracy of this data cannot be verified because it is the online, unpublished, database retrieved at the terminal computer of the Central Bankruptcy Court.

Table 4: Bankruptcy Cases between 1999 and 2012

Year	Number of Cases in						Ratio of Liquidation to Reorganization
	Liquidation			Reorganization			
	Outstanding	*Adjudicated*	*%*	*Outstanding*	*Adjudicated*	*%*	
1999	416	210	50.48	25	21	84.00	16.01
2000	1,200	928	77.33	139	119	85.61	8.63
2001	1,845	1,159	62.82	104	96	92.31	17.74
2002	2,592	2,026	78.16	68	61	89.71	38.12
2003	3,944	2,321	58.85	58	53	91.39	68.99
2004	7,306	5,061	69.27	57	49	85.96	128.18
2005	10,266	5,524	53.81	46	36	78.26	223.17
2006	17,986	8,789	48.87	62	40	64.51	290.09
2007	24,577	16,046	65.29	79	55	69.62	311.10
2008	25,301	9,978	39.44	78	60	76.92	324.37
2009	33,848	23,975	70.83	60	40	66.67	564.13
2010	24,129	17,586	72.88	73	59	80.82	330.53
2011*	15,161	10,317	68.05	48	37	77.08	315.85
		Average	62.77			79.90	

Source: Central Bankruptcy Court (2012)
Note: * as of November 2011

Table 5: Amount of Debt in Bankruptcy Cases between 1999 and 2012

Year	Cases in						Ratio of Average Debt Amount in Reorganization to Liquidation
	Liquidation			Reorganization			
	New Cases	*Amount of Debt* (mil. Baht)	*Average Debt Amount* (mil. Baht)	*New Cases*	*Amount of Debt* (mil. Baht)	*Average Debt Amount* (mil. Baht)	
1999	416	10,148.74	24.39	25	153,796.90	6,151.88	252.17
2000	994	129,104.16	129.88	135	672,012.29	4,977.87	38.33
2001	1,573	628,270.47	399.41	84	367,349.91	4,373.21	10.95
2002	1,906	688,251.05	361.10	60	144,095.24	2,401.59	6.65
2003	3,378	94,197.72	27.89	51	163,557.62	3,207.01	115.01
2004	5,683	77,440.99	13.63	52	167,422.46	3,219.66	236.27
2005	8,021	408,754.28	50.96	38	30,736.38	808.85	15.87
2006	13,244	174,121.58	13.15	52	94,974.52	1,826.43	138.92
2007	15,380	187,249.21	12.17	57	178,678.63	3,143.71	257.47
2008	16,770	257,650.02	15.36	54	125,729.90	2,328.31	151.55
2009	18,525	388,620.03	20.98	42	61,913.31	1,474.13	70.27
2010	14,256	387,754.23	27.20	53	38,312.14	722.87	26.58
2011*	8,618	339,634.78	39.41	34	67,160.41	1,975.31	50.12
		Average	87.35			2,815.53	

Source: Central Bankruptcy Court (2012)
Note: * as of November 2011

It is apparent that reorganization (see Table 3) were likely to be used by the debtor rather creditors. Within the past decade, debtors filing for reorganization are, on average, 4.48 times higher than creditors. This indicates that the mechanism of reorganization provisions has an inclination towards debtor.

Statistics from Table 4 seems to confirm this. Liquidation cases outnumbered reorganization cases by staggering 200 times on average. This denotes the increasingly insignificance of reorganization in term of cases. Noting that, the rate of adjudication in reorganization is higher than in liquidation. It

seems to contradict with the general intuition that reorganization is much more difficult to achieve than liquidation. This possibly hints the procedural bias.

Table 5 reveals the amount of debt owed to creditors in liquidation and reorganization. On average, the value of debt in reorganization is 32.23 times higher than in liquidation. This could explain why Thailand was in need of bankruptcy reform during the crisis. Owning to the fact that not many debtors seeking reorganization, all of them were high-profile cases (extremely high debt) and their failure may inflict substantial damage to the Thai economy. Also, it could explain the bias for debtors (against creditors) inherited in the Thai bankruptcy legislation, especially reorganization.

3.2. Private workout in Thailand

As mentioned earlier in 2, the insolvency problem is not completed without the consideration of informal approaches and the initial borrowing-lending relationship. This section covers the evidence of private workouts in Thailand to compare the performance of reorganization procedure from 3.1.

Since real private workouts are not recorded, there is no information about it. However, studies in Japan by Eisenberg and Tagashira (1996); Hoshi, Kashyap and Scharfstein (1996) and in the UK by Armour and Frisby (2001) indicated the pivotal role of financial institutions in leading the private workouts for distressed debtors. Thailand shares a very similar financial landscape with these two countries particularly in debt financing. There is limited number of commercial banks and most business debtors are linked with these banks (Akira, 1996; Pongpaichit and Baker, 1995; Thavornyutikarn, 2006).

Indeed, the Bank of Thailand (BoT), set up the facility called Corporate Debt Restructuring Advisory Committee (CDRAC) in 1998. CDRAC is effectively a parallel mechanism for debt restructuring assisting distressed debtors to be solvent[3]. Its purpose is to persuade financial institutions who are creditors to continue providing loans to debtor businesses and assisting the debt restructuring process in order to reduce the non-performing loans (NPLs) (Dasri, 2000; Thavornyutikarn, 2006). Agreements under CDRAC are privately negotiated between the troubled firm and its financial institutions in a single, unified, group. Successful renegotiation resulted in a new multilateral, legally-bound, contract outlining the debt restructuring process. However, under the Thai bankruptcy legislation, this scheme is not recognized as a bankruptcy proceeding but as contractual obligations under the law of contract which would be overruled if the bankruptcy proceeding of the debtor commences.

Empirically, CDRAC was highly successful. Table 6 illustrates the progress of debt restructuring through CDRAC facilities.

[3] It is called Bangkok Approach, after London Approach where CDRAC mechanism modeled on (Dasri, 2000)

Table 6: Debt Restructuring under BoT's CDRAC Scheme

Year	CDRAC Debt Restructuring						Average Debt Amount per Case (million Baht)
	Cases			Amount of Debt (million Baht)			
	Outstanding	*Restructured*	*%*	*Outstanding*	*Restructured*	*%*	
1999	199,909	173,709	86.89	2,192,608	1,072,095	48.89	10.97
2000	608,447	532,196	83.47	2,340,347	1,953,520	87.46	3.85
2001	523,430	476,137	90.96	2,570,940	2,429,093	94.48	4.91
2002	n/a						
2003							
2004	11,705	11,441	97.75	1,499,089	1,497,820	99.92	128.07

Source: CDRAC, Bank of Thailand (1999 – 2001; 2004)
Note: Data of 2002 and 2003 are not available.

Note that the amounts of debt undergone CDRAC scheme were always significantly larger than in liquidation and reorganization combined. Notwithstanding, success rates in debt restructuring outperformed adjudication rates of liquidation and reorganization in terms of number of cases and amount of debt. This affirms our conjecture about the nature of borrowing-lending relationships and solutions to insolvency in Thailand. Most cases can be settled outside formal procedures. If private workouts failed, debtors are more likely to be liquidated unless the value of debt is exceptionally high. The per-case average debt is the range of 10 – 130 million Baht for CDRAC, 15 – 400 million Baht for liquidation, and 700 – 6,000 million Baht for reorganization (compare Table 5 and 6). Liquidation and reorganization shall not be differentiated by the debt value. Both must be accessible for the debtor depending on whichever gives the highest valuation. Reorganization shall not be used to preserve high value debts but to preserve the debtor that worth more active than defunct. Analogously, liquidation shall not be used for the distribution of low value debts but to respect creditors' rights when the debtor is worth more defunct than active.

3.3. Comparing private workout and formal bankruptcy

Based on the cases and outstanding debt under CDRAC in Table 6, Table 7 compares private workout and formal procedures of bankruptcy in percentage terms.

Table 7: Comparison of private workout and formal bankruptcy procedures

Year	**Percentage of Base Cases** (Outstanding cases and debt amount in CDRAC as a base line)					
	Cases			Amount of Debt (million Baht)		
	Liquidation	*Reorganization*	*Combined*	*Liquidation*	*Reorganization*	*Combined*
1999	0.208	0.013	0.221	0.463	7.014	7.477
2000	0.163	0.022	0.186	5.516	28.714	34.231
2001	0.300	0.016	0.316	24.437	14.289	38.726
2002	n/a					
2003						
2004	48.552	0.444	48.996	5.165	11.168	16.344

Interestingly, more than 40 per cent of debtors in reorganization had successfully reached agreements under CDRAC (Thavornyutikarn, 2006). Thus, all figures on reorganization must be discounted by 40 per cent, rendering it even less important. Their entry into reorganization was questionable and suspiciously strategic. Also, it posed a threat of forum shopping and, subsequently, undermining borrowing-lending relationships.

In all cases, formal bankruptcy is accounted for less than half of private workout – both in terms of number and outstanding debt. Therefore, formal bankruptcy is, in general, less operative than private workout. Within bankruptcy, liquidation is relatively more active than reorganization in term of cases; while reorganization is relatively more active than liquidation in term of debt value. In the context of Thailand, reorganization is possibly redundant; thus, the adoption of such provisions is economically inefficient. It is too expensive to institutionalize reorganization where most cases could be solved in private workouts.

4. UNCITRAL on Bankruptcy: Legislative Guide and Model Law on Cross-Border Insolvency

United Nations Commission on International Trade Law (UNCITRAL) aims to modernize and harmonize rules on international business by providing legislative guides and model laws, information dissemination, and technical assistance. Insolvency is one of the covered areas.

4.1. On the legislative guide

The Legislative Guide (the Guide) offers guidelines and recommendations on how to draft efficient and effective insolvency legislation and system. Despite the fact that the Guide does not intend to "provide a single set of model solutions" (UNCITRAL, 2005), the UN General Assembly Resolution did believe that the harmonization of insolvency legal framework would be established, international standards of insolvency would be developed, and recommend the Model Law on Cross-Border Insolvency to be implemented.[4] We disagree with this belief.

Lessons learned from Thailand indicate the impossibility of an internationally harmonized insolvency legal framework since the legislation must be drafted and concern about the nature of borrowing-lending relationship (because it determines how insolvency evolves and be solved) and economic fundamentals which varies from country to country[5] to attend economic efficiency.

The Guide, however, provides many useful commentaries on key issues and respective recommendations for enactment and/or amendment.[6]

4.2. On the model law

Due to the expansion of international trade and investment, insolvency becomes international issues particularly for multinational investors. Incompatibility of bankruptcy procedures creates the barrier for international transactions. UNCITRAL proposed the Model Law on Cross-Border Insolvency for cooperation among legal authorities, improvement of business certainty, and protection of stakeholders' entitlement (UNCITRAL, 2005).

[4] UN General Assembly Resolution, A/RES/59/40, 16 December 2004

[5] This coincide with the Guide in Part I, I, A. Introduction, 3. stating "The *Legislative Guide* does not provide a single set of model solutions to address the issues central to an effective and efficient insolvency law, but assists the reader to evaluate different approaches available and to choose the one most suitable in the national or local context" (p.2).

[6] For example, the authors found that the topic of conversion of reorganization to liquidation (in Part 2, IV. Reorganization, 14. Conversion to Liquidation, pp. 232-233), especially, "If conversion to liquidation requires a new application for commencement to be made, rather than relying upon the original application as the basis for the converted proceedings, it may lead to further delay and diminution of value") is useful for revising the Thai bankruptcy law since the failure of reorganization does not trigger liquidation and the new application for liquidation is required (Thavornyutikarn, 2006).

Many works emphasized on how the enactment of the Model Law improves international trade and investment for their respective economies including Rotjanasiributr (2001) for Thailand and Locatelli (2008) for Brazil. The direct adoption, however, shall be warned and differences among national laws are respected.[7]

In the context of Thailand, the Model Law may not be relevant for a couple of reasons. First, as discussed earlier in 3, most debtors in financial distress are likely to use private workouts compare to formal bankruptcy by large margin. Secondly, foreign companies are strictly regulated and must be explicitly permitted[8]; subsequently, there are not many foreign firms *ex ante* to be possibly insolvent. Even though the adoption reduces uncertainty internationally, other legal barriers, which are more crucial than bankruptcy, still exist in preventing international trade and investment. Lastly, the Thailand's saving-investment gap is wide, even though narrowing[9], implying not many Thai investors abroad and their difficulty from insolvency of their debtors is contained.

The compatibility of insolvency legislation across nations is undeniably beneficial and encourages international transactions, but at the expense of less efficient bankruptcy procedures that are not fully tailored for national exclusivity. Moreover, there are many more laws in Thailand that shall be reformed to achieve the same objective.

5. Conclusion and Recommendations

Bankruptcy law is much dependent on how borrowing and lending are related. A close, repeated, and less-than-arm's length borrowing-lending relationship rarely needs a formal bankruptcy proceeding since private workouts are more effective and efficient due to the low transaction cost setting. Thailand's lessons reveal that incorporating reorganization provisions into the bankruptcy law of Thailand is unnecessary. It, also, benefits a limited number of large-scale debtors at the expense of creditors and existing relationships. Thus, adopting any international law to the national legislation must be thorough and must contemplate on the nature of the subject matter.

This caveat applies to the attempt of UNCITRAL for standardization of insolvency law and its cross-border provisions. The international unification must be traded off with economic efficiency in each country. UNCITRAL Legislative Guide and Model Law on Cross-Border Insolvency, nevertheless, are worth reviewing for appropriate and selective amendment of respective legislation that promotes economic efficiency, not the standardization of law.

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Implication of Macroeconomic Data and Real Estate Data for Investment Decisions in Central Eastern European Markets[1]

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Abstract

The paper at hand analyzes the correlation of macroeconomic data and selected real estate data in 8 major Central Eastern European countries (CEE countries) in order to cluster these countries and derive targeting capital investment-strategies in real estate for these countries.

Based on data sequences of Eurostat and the national statistical data as well as market reports, major correlations in selected countries were analyzed for macroeconomic data like unemployment, inflation or GDP and real estate data like housing costs, number of employees in the construction industry or development of building permits. The countries chosen for this analysis were Germany, Austria, Poland, Czech Republic, Slovenia, Slovakia, Hungary and Romaniain the years 2005 to 2011. The analysis could demonstrate different correlations within the countries and the variables implying different investment strategies for institutional investors. A correlation could be found at building permits and GDP, building permits and unemployment, building permits and inflation as well as employment in real estate industry and GDP, employment in real estate industry and unemployment rate as well as housing cost and GDP, housing cost and unemployment. A cluster analysis for the analyzed countries could not be successfully conducted; therefore, each country had to be analyzed in detail for possible investments. These detailed analyses were undertaken in cooperation with major leading institutional investors.

Keywords

CEE-countries, macroeconomic data, correlations, real estate, investment decisions, institutional investors

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1. Introduction

Based on the geographical, economical and historical relationships, Eastern European Countries have always been an attractive and interesting investment alternative for Austrian and German companies and investors. During the enlargement of the European Union in 2004, countries like Poland, Slovenia, Slovakia, Czech Republic or Hungary and in 2007 countries like Romania became increasingly important for investors – also for institutional investors – based on reliable legal and economic conditions.

Institutional investors rely on an equilibrated portfolio diversification with different asset classes in different countries (Markowitz, 1952). Within the portfolio diversification, the here analyzed investments in real estate are one part of the investment strategy, attributed with stability and reliability. To fulfill the requirements of an optimal portfolio diversification, different correlations within the real estate markets play an important role for real estate investments. The real estate market can be considered as a non-transparent, inefficient market (Truebestein, 2010). To avoid increasing costs for analyzing each market and to prevent cluster-risks, it might be of interest to see, if different Eastern European markets can be clustered in different groups, based on macroeconomic and real estate related criteria. In a further step, it might be important to see, if these different markets have become similar in their developments. The European Union, the Euro, the alignment of the interest rates as well as an increasing transparency of the real estate markets and the increasing globalization of the industry, especially the financial industry, have resulted in an alignment of different western European markets [cf. Figure 01], so portfolio diversification might become more difficult and timing has become more important.

In the following parts, selected macroeconomic and real estate criteria are chosen and analyzed for the selected countries in order to cluster different regions and countries.

Figure 01: Correlations of different European Cities

1991-2000

	London City	Paris CBD	Munich	Brussels	Madrid
Paris CBD	0,34				
Munich	-0,30	0,36			
Brussels	-0,28	0,53	0,91		
Madrid	-0,11	0,68	0,62	0,79	
Praha	0,32	-0,07	0,46	0,39	0,22

2001-2010

	London City	Paris CBD	Munich	Brussels	Madrid
Paris CBD	0,81				
Munich	0,75	0,85			
Brussels	0,49	0,70	0,41		
Madrid	0,87	0,94	0,85	0,61	
Praha	0,80	0,77	0,50	0,71	0,76

Source: Investments (2011)

2. Data and Analyzes

In order to guarantee a homogeneous and reliable data-set, the data of the *European Commission* and *Eurostat* were taken and analyzed (Eurostat). In addition, the general results were compared to the reports of international renowned real estate related companies like Jones Lang LaSalle, CBRE or BNP Paribas.

Macroeconomic criteria
Gross domestic product (GDP)
This ratio is a measure of the total economic production activity and encompasses the entire value of all goods and services for the use, that were produced in a given period and country. The GDP measures the sum of all income earned in a particular period of the economy (Blanchard and Illing, 2006, pp. 829).

Unemployment rate
The unemployment rate is calculated nationally and therefore varies based on the definitions. For the analysis, the employed rate of the registered unemployed to the labor force is used. Therefore the relative underutilization of the labor supply is measured.

Inflation
Inflation is the increase in the general price level (Blanchard and Illing, 2006, pp. 834). The data used indicate the inflation of the reporting period as a percentage.

Real Estate related criteria
Building permits
This ratio reflects the index of approved m² of usable space in each country. Therefore all kinds of buildings and their uses are integrated (Eurostat). However, the fact has to be considered that it is an index and not the absolute square m². For the calculation of the correlation, however, this is not a disadvantage, as the ratio of the changes is used.

Housing costs
Hereby the average exposure of the population of a country for the cost of living is shown. The value is given and specified as a percentage value. This is advantageous for the calculation of the correlations and facilitates the comparison of different countries.

Number of workers in the construction industry (employment)
This indicator in the form of an index shows the number of workers in the area of construction. The construction industry index has been adjusted by those industries that are not primarily associated with the building and development of real estate. Thus, the used Eurostat data can be used as a real estate index and evaluated accordingly.

3. Correlations

During the analysis, more than 20 correlations were calculated and interpreted in order to show possible indices. For the following analysis, 9 correlations were used and analyzed.

Building permits and GDP
For the calculation of the correlation of the approved m² of usable space and the Gross Domestic Product, several countries with a clear correlation can be identified. It can be shown, that Germany, Austria and Hungary have a positive correlation and the Czech Republic and Slovenia have a negative correlation. It can be marked, that a positive correlation is coming along with an increase in the GDP and an increase in the number of authorized m² floor space whereas a negative correlation can be seen for those countries with a decreasing GDP [cf. Figure 02].

One possibility, why the building permits diminish with an increasing GDP is based on phase-shifted data points. While GDP allows a relatively quick short term measurement, the ratio of building permits is rather a lagging indicator. In a longer view, the negative correlation could be adapted.

Figure 02: Correlations: Building permits and GDP

	Building permits - index m²				Correlations' Coefficient
Country	**2008**	**2009**	**2010**	**2011**	
Germany	69,27	71,11	75,54	91,94	0,7965639
Austria	111,6	113,3	126,53	139,72	0,9329722
Poland	192,34	158,46	151,53	153,71	-0,4217269
Romania	205,19	121	100,9	90,23	0,6633599
Slovakia	147,94	103,69	88,47	72,92	-0,9593627
Slowenia	115,03	85,41	78,47	56,55	0,1935022
Czech Republic	115,32	97,29	77,61	75,61	-0,8499416
Hungary	100,32	98,37	92,55	98,74	0,9999999

	GDP (Volume in € Mio.)			
Country	**2008**	**2009**	**2010**	**2011**
Germany	2.454.890	2.346.900	2.462.100	2.551.050
Austria	277.846	271.974	281.179	295.091
Poland	326.945	369.065	322.763	369.991
Romania	133.895	130.574	116.247	127.104
Slovakia	57.963	61.237	65.422	67.945
Slowenia	35.803	34.294	35.798	35.354
Czech Republic	135.996	147.026	145.324	151.784
Hungary	100.320	98.370	92.553	98.738

Building permits and unemployment rate

All the analyzed countries in this comparison obtain a negative correlation. This seems reasonable, as the construction industry represents a significant share of total employment market in each country. Consequently the determined correlation shows that an increasing number of building permits comes along a decreasing unemployment rate. This relationship is based directly on an increasing demand for labor due to the number of contracts awarded in the construction industry [cf. Figure 03].

Figure 03: Correlations: Building permits and unemployment rate

	Building permits - index m²				Correlations' Coefficient
Country	**2008**	**2009**	**2010**	**2011**	
Germany	69,27	71,11	75,54	91,94	-0,9732891
Austria	111,6	113,3	126,53	139,72	-0,0286347
Poland	192,34	158,46	151,53	153,71	-0,9018886
Romania	205,19	121	100,9	90,23	-0,9977333
Slovakia	147,94	103,69	88,47	72,92	-0,9273464
Slowenia	115,03	85,41	78,47	56,55	-0,9727358
Czech Republic	115,32	97,29	77,61	75,61	-0,8800664
Hungary	100,32	98,37	92,55	98,74	-0,7027436

	Unemloyment Rate			
Country	**2008**	**2009**	**2010**	**2011**
Germany	7,50	7,80	7,10	5,90
Austria	3,80	4,80	4,40	4,20
Poland	7,10	8,20	9,60	9,70
Romania	5,80	6,90	7,30	7,40
Slovakia	9,50	12,00	14,40	13,50
Slowenia	4,40	5,90	7,30	8,20
Czech Republic	4,40	6,70	7,30	6,70
Hungary	7,80	10,00	11,20	10,90

Building permits and inflation
As a result of this calculation, it can be stated that all the countries obtain a positive correlation. In all the countries – except for Romania – however, the correlation can be characterized as weak [cf. Figure 04].

This can be explained within the following three variants. One possibility might be, that there is no connection between the building permits and the inflation rate. A second possibility might be – due to the fact that the building permits are a lagging indicator and the inflation rate is a dynamically determined average –that the correlation is not particularly strong. In a long-term view, these values might be stronger. The third option is, that with an increasing inflation rate, also the need for home ownership increases. Home ownership is considered to security at impending inflation. Inflation targets also tenants who are exposed to higher rents especially with rent adaption options (indexations). At an increasing inflation this stimulates a kind of rethinking of homeownership that in turn will have a direct impact on the building permits.

Figure 04: Correlations: Building permits and inflation

	Building permits - index m²				Correlations' Coefficient
Country	**2008**	**2009**	**2010**	**2011**	
Germany	69,27	71,11	75,54	91,94	0,3489408
Austria	111,6	113,3	126,53	139,72	0,4807133
Poland	192,34	158,46	151,53	153,71	0,5895519
Romania	205,19	121	100,9	90,23	0,9247158
Slovakia	147,94	103,69	88,47	72,92	0,2224544
Slowenia	115,03	85,41	78,47	56,55	0,7250126
Czech Republic	115,32	97,29	77,61	75,61	0,7204696
Hungary	100,32	98,37	92,55	98,74	0,2088736

	Inflation			
Country	**2008**	**2009**	**2010**	**2011**
Germany	2,80	0,20	1,20	2,50
Austria	3,20	0,40	1,70	3,60
Poland	4,20	4,00	2,70	3,90
Romania	7,90	5,60	6,10	5,80
Slovakia	3,90	0,90	0,70	4,10
Slowenia	5,50	0,90	2,10	2,10
Czech Republic	6,30	0,60	1,20	2,10
Hungary	6,00	4,00	4,70	3,90

Employment and GDP
In Germany an increase in the number of employees as well as in the gross domestic product can be recorded. In recent years an economic stimuli like subsidies and measures in areas such as renovation, energy modernization and expansion of buildings have been undertaken. The idea was to reduce the negative impacts of the economic development in recent years. These measures were – to a major part – terminated in 2011, so in 2012 stagnation in the construction sector can be expected. It can also be noted that countries with the largest decline in GDP had the strongest decline in the employment rate. This particularly relates to the countries of Eastern Europe, especially Romania is affected, where a positive correlation of employees of the construction area and GDP is recorded. The impact of the financial crisis can be observed in countries like Slovakia, Czech Republic and Poland, where the employment rate in the building area has been decreasing since 2008. However, the GDP growth rates are above the European average and have risen sharply despite the crisis. This is generally due to the sustainable economic growth, which in part is also due

to the EU accession. This is shown in a negative correlation, that, however, in the opinion of the Eastern Institute in Regensburg (Knogler, 2010) may disappear. Based on current surveys no meaningful correlation between these pair ratios can be found [cf. Figure 05].

Figure 05: Correlations: Employment and GDP

	Employment - index				Correlations' Coefficient
Country	**2008**	**2009**	**2010**	**2011**	
Germany	102,45	103,66	105,92	109,93	0,7607091
Austria	101,75	104,15	103,48	105,51	0,5978323
Poland	117,93	122,47	124,1	133,46	0,5981031
Romania	122,46	103,75	88,15	87,51	0,7780796
Slovakia	126,25	128,84	125,45	120,91	-0,7394319
Slowenia	133,89	132,3	119,69	103,44	-0,217799
Czech Republic	104,23	101,98	99,62	97,83	-0,8862581
Hungary	93,97	86,34	86,47	85,01	0,4637795

	GDP (Volume in € Mio.)			
Country	**2008**	**2009**	**2010**	**2011**
Germany	2.454.890	2.346.900	2.462.100	2.551.050
Austria	277.846	271.974	281.179	295.091
Poland	326.945	369.065	322.763	369.991
Romania	133.895	130.574	116.247	127.104
Slovakia	57.963	61.237	65.422	67.945
Slowenia	35.803	34.294	35.798	35.354
Czech Republic	135.996	147.026	145.324	151.784
Hungary	100.320	98.370	92.553	98.738

Employment and general unemployment rate

By comparing the number of workers in the real estate construction area (employment) and the general unemployment rate, it can be observed that in most countries, the unemployment rate decreases when workforce in the construction industry increases. In countries like Germany, Romania, Slovenia, Czech Republic and Hungary, the building industry represents a key economic indicator with considerable influence. Only the country of Poland had a positive correlation between the two indicators identified as both the number of employees as well as the unemployment rate in the years 2008 to 2011 increased. Poland is a country with very continuous and dynamic economic growth and draws the primary share of GDP from the industrial sectors mining (coal), automotive and mechanical engineering, metal and steel industry as well as electrical, transport, food, textile and automotive industries. The construction industry is limited in terms of GDP to just 6.5 % in the prior of 2011 [9]. This arises in a positive correlation. In the building industry, a steady increase can be seen, whereas a negative correlation between the number of employees and the unemployment rate can be observed [cf. Figure 06].

Figure 06: Correlations: Employment and unemployment rate

	Employment - index				Correlations' Coefficient
Country	2008	2009	2010	2011	
Germany	102,45	103,66	105,92	109,93	-0,9501735
Austria	101,75	104,15	103,48	105,51	0,5107593
Poland	117,93	122,47	124,1	133,46	0,8293619
Romania	122,46	103,75	88,15	87,51	-0,9832811
Slovakia	126,25	128,84	125,45	120,91	-0,409324
Slowenia	133,89	132,3	119,69	103,44	-0,9167278
Czech Republic	104,23	101,98	99,62	97,83	-0,7837917
Hungary	93,97	86,34	86,47	85,01	-0,9415994

	Unemloyment Rate			
Country	2008	2009	2010	2011
Germany	7,50	7,80	7,10	5,90
Austria	3,80	4,80	4,40	4,20
Poland	7,10	8,20	9,60	9,70
Romania	5,80	6,90	7,30	7,40
Slovakia	9,50	12,00	14,40	13,50
Slowenia	4,40	5,90	7,30	8,20
Czech Republic	4,40	6,70	7,30	6,70
Hungary	7,80	10,00	11,20	10,90

Employment and inflation

Regarding the interaction between the employment in the construction area and the inflation rate of the surveyed countries only the correlations for Romania and Hungary are derived "hypothetically". In these countries, both, the number of employees as well as the inflation rate decreased. This is probably due to the fact, that Romania was severely affected by the economic crisis and thus the number of employees and the level of prices have decreased. In Hungary, this trend could also be recorded. All other countries studied show no correlation. The selected data collection and the derived correlations show no clear tendencies for the two numbers [cf. Figure 07].

Figure 07: Correlations: Employment and inflation rate

	Employment - index				Correlations' Coefficient
Country	2008	2009	2010	2011	
Germany	102,45	103,66	105,92	109,93	0,2303804
Austria	101,75	104,15	103,48	105,51	-0,017204
Poland	117,93	122,47	124,1	133,46	-0,1281972
Romania	122,46	103,75	88,15	87,51	0,8034574
Slovakia	126,25	128,84	125,45	120,91	-0,6327222
Slowenia	133,89	132,3	119,69	103,44	0,3259223
Czech Republic	104,23	101,98	99,62	97,83	0,6264464
Hungary	93,97	86,34	86,47	85,01	0,9568999

	Inflation			
Country	2008	2009	2010	2011
Germany	2,80	0,20	1,20	2,50
Austria	3,20	0,40	1,70	3,60
Poland	4,20	4,00	2,70	3,90
Romania	7,90	5,60	6,10	5,80
Slovakia	3,90	0,90	0,70	4,10
Slowenia	5,50	0,90	2,10	2,10
Czech Republic	6,30	0,60	1,20	2,10
Hungary	6,00	4,00	4,70	3,90

Housing costs and GDP

Comparing the figures of housing costs and GDP it can be observed that in several countries a relationship of two variables is given. While the correlation is strongly positive in Austria and Slovakia, a moderate correlation in Slovenia and a strong negative correlation in Poland can be seen. In these countries, the economic performance has consistently grown – apart from the 2008 crisis and their temporal delay in the following year. The negative correlation exists in countries that are marked by decreasing housing costs, in the two other countries the costs have increased over the period or have almost remained unchanged and are positively correlated. Accordingly, one might assume that in a good economic performance of a country and the level of rents increases, resulting in higher expenditures on housing. The costs increase accordingly [cf. Figure 08].

Figure 08: Correlations: Housing costs and GDP

	Housing costs - %						Correlations' Coefficient
Country	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	
Germany							
Austria	15,80	16,40	17,60	17,60	17,00	17,30	0,9103076
Poland	22,90	21,40	20,20	19,10	18,30	18,40	-0,9685632
Romania			21,20	22,70	20,10	20,20	0,2732189
Slovakia	10,00	10,30	11,70	11,30	11,90	12,80	0,9200147
Slowenia	19,30	20,00	22,60	13,40	16,20	14,90	-0,6517343
Czech Republic	20,40	21,70	21,20	21,00	19,90	20,70	-0,3396777
Hungary	22,10	19,00	18,70	20,70	20,10	21,40	-0,165623

	GDP (Volume in € Mio.)					
Country	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Germany	2.210.630	2.306.660	2.389.590	2.454.890	2.346.900	2.462.100
Austria	240.342	254.243	268.634	277.846	271.974	281.179
Poland	211.624	259.641	290.551	326.945	369.065	322.763
Romania			103.926	133.895	130.574	116.247
Slovakia	36.257	41.701	49.172	57.963	61.237	65.422
Slowenia	28.319	30.412	33.184	35.803	34.294	35.798
Czech Republic	98.052	111.974	125.075	135.996	147.026	145.324
Hungary	85.370	92.225	89.696	100.320	98.370	92.553

Housing costs and unemployment rate

The correlation of the two variables housing costs and unemployment rate is not conclusive. Romania and Austria have a negative, Poland a positive correlation. For all other countries no relation of the two variables can be determined. In countries with a low unemployment rate, a negative correlation of the variables can be seen. Poland has the highest unemployment rate in the three countries and a strong positive correlation. One might assume that the unemployed can catch their exposure to the housing costs by grants and subsidies. Interestingly, the in housing costs in Austria of approximately 17% are lower than in Eastern European member states at about 20% [cf. Figure 9].

Figure 09: Correlations: Housing costs and unemployment rate

	Housing costs - %						Correlations' Coefficient
Country	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	
Germany							
Austria	15,80	16,40	17,60	17,60	17,00	17,30	-0,8728324
Poland	22,90	21,40	20,20	19,10	18,30	18,40	0,922202
Romania			21,20	22,70	20,10	20,20	-0,9503397
Slovakia	10,00	10,30	11,70	11,30	11,90	12,80	-0,3075495
Slowenia	19,30	20,00	22,60	13,40	16,20	14,90	-0,0636842
Czech Republic	20,40	21,70	21,20	21,00	19,90	20,70	-0,2572615
Hungary	22,10	19,00	18,70	20,70	20,10	21,40	0,279134

	Unemloyment Rate					
Country	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Germany	11,30	10,30	8,70	7,50	7,80	7,10
Austria	5,20	4,80	4,40	3,80	4,80	4,40
Poland	17,80	13,90	9,60	7,10	8,20	9,60
Romania			6,40	5,80	6,90	7,30
Slovakia	16,30	13,40	11,10	9,50	12,00	14,40
Slowenia	6,50	6,00	4,90	4,40	5,90	7,30
Czech Republic	7,90	7,20	5,30	4,40	6,70	7,30
Hungary	7,20	7,50	7,40	7,80	10,00	11,20

Housing costs and inflation rate

The analysis of the variables housing costs and inflation rate show that in two countries, Poland and Slovakia, a negative correlation can be found. Only in Romania a positive correlation can be observed. Housing is one of the main components of the cost of living. The higher the cost of living – ownership or rent – are, the more it favors the inflation rate. Similarly, the inflation increases the rents – a negative cycle [cf.Figure 10].

Figure 10: Correlations: Housing costs and inflation rate

	Housing costs - %						Correlations' Coefficient
Country	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	
Germany							
Austria	15,80	16,40	17,60	17,60	17,00	17,30	0,2362089
Poland	22,90	21,40	20,20	19,10	18,30	18,40	-0,7001413
Romania			21,20	22,70	20,10	20,20	0,7036054
Slovakia	10,00	10,30	11,70	11,30	11,90	12,80	-0,7699898
Slowenia	19,30	20,00	22,60	13,40	16,20	14,90	-0,1121773
Czech Republic	20,40	21,70	21,20	21,00	19,90	20,70	0,4343138
Hungary	22,10	19,00	18,70	20,70	20,10	21,40	-0,5221188

	Unemloyment Rate					
Country	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Germany	1,90	1,80	2,30	2,80	0,20	1,20
Austria	2,10	1,70	2,20	3,20	0,40	1,70
Poland	2,20	1,30	2,60	4,20	4,00	2,70
Romania			4,90	7,90	5,60	6,10
Slovakia	2,80	4,30	1,90	3,90	0,90	0,70
Slowenia	2,50	2,50	3,80	5,50	0,90	2,10
Czech Republic	1,60	2,10	3,00	6,30	0,60	1,20
Hungary	3,50	4,00	7,90	6,00	4,00	4,70

4. Findings of the Correlations

The variable *approved area (m²)/ building permits* is correlated with all macroeconomic variables. Based on the GDP a positive correlation within Germany, Austria and Hungary could be calculated. Negative values could be explained with a time lag: whereas the GDP allows a relatively actual economic implication, the variable building permits could be seen as a time-lagged indicator.

In terms of *unemployment* a clear negative correlation for all analyzed countries could be shown. This seems plausible as the construction industry offers a significant proportion of the total labor market in each of the analyzed counties. Consequently, the unemployment rate decreases with an increasing number of building permits.

Comparing the *building permits* and the *inflation* a positive correlation can be observed in all the countries whereas in all the countries – except Romania – the correlations were very low. Here, the presumption could infer that with increasing inflation also the idea of home ownership becomes more attractive. This could be supported by the existing theory of "asset-security" when purchasing "real" objects.

In a further analysis the data of *workers/ employment in the real estate industry* were used and correlated to the macroeconomic data set. In Germany, an increase of the number of employees and the gross domestic product could be recorded. This is presumably due to the fact that in recent years, several governmental stimuli were passed like modernization of real estate, renovation of real estate or energy efficiency programs to prevent an economic downturn.

Comparing the number of workers in real estate and the general *unemployment rate* it could be observed, that in most countries the unemployment rate decreases when employment in the construction areas increase. In Germany, Romania, Slovenia, Czech Republic and Hungary, the construction industry is a major economic indicator with considerable influence on the total employment.

In the last part of the analysis the *housing costs index* was compared to the GDP. At first glance, it was obvious that in several countries a relationship of the two variables can be observed. The correlations were positive as well as negative. Thus, one could assume that in a good economic performance of a country also the level of rents increases and therefore higher costs have to be applied for housing and thus increase the cost-indices. The correlation with the unemployment rate does, however, not conclude uniquely. Romania and Austria show a negative correlation, Poland a positive correlation. It could be assumed that unemployed groups receive grants and subsidies to reduce their costs and consequently housing costs could be intercepted.

The other comparisons and correlations could not obtain targeting results. Basically it could be observed, that the variables *GDP* and *unemployment rate* offer several possibilities for correlations within the *real estate sector* and *real estate* specific *data-sets*.

Finally, the analysis of the correlations could show different correlations and no determining results of the countries so that a clustering of variables could not be undertaken in a first step, respectively undertaken with difficulties. Concluding the analysis, it can be seen, that there are many different developments within the selected markets that offer interesting (real estate) investment opportunities for institutional investors.

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The Efficiency Analysis of Non-Life Insurance Companies Active in Turkey

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Abstract

This paper evaluates the technical efficiencies of non-life insurance companies, which are active in Turkey in 2007, using Data Envelopment Analysis (DEA). DEA, which is a non-parametric method, facilitates to examine different input-output components. DEA is a management evaluation tool that assists in identifying the most efficient and inefficient decision making units (DMUs) in the best practice frontier. In this study, as inputs of 23 non-life insurance companies, the number of agents, the number of brokers, fixed assets, shareholders' equity and as outputs the investment incomes, premiums received are used. Empirical results of BCC and CCR models, which are DEA models, show that the most efficient insurance company is RAY.

Keywords

Banker-Charnes-Cooper (BCC), Charnes-Cooper-Rhodes (CCR), Data Envelopment Analysis (DEA), Efficiency, Insurance

1. Introduction

Insurance is fundamental for protecting individuals against the hazards of life. One of the important functions of insurance companies is to create funds for investments, which are crucial for economic growth, in an economy. Hence, the role of insurance industry is critical in developing economies. However, the number of studies analyzing the performance of the insurance companies in developing economies is very limited. Hao and Chou (2005) analyze the cost efficiency of life insurance companies in Taiwan. Tone and Sahoo (2005) analyze the cost efficiency in the Indian life insurance industry. Barros and Obijiaku (2007) evaluate the performance of Nigerian insurance companies, from 2001 to 2005, combining operational and financial variables by using Data Envelopment Analysis (DEA), also analyzing the situations of these companies in relation to the frontier of best practices. Yao et al. (2007) only estimate the efficiency of insurance industry in China without considering other aspects of insurance companies that may be just as important or even more so. Wei (2009) introduces a modified measure of risk-adjusted efficiency by using a multistage DEA to estimate the real efficiency level for the 284 insurance companies in China from 1999 to 2006. Dutta and Sengupta (2011) calculating the efficiency scores of the major life insurance companies in India over the period of five financial years from 2004 to 2008 (Barros and Obijiaku, 2007; Kasman and Turgutlu, 2009; Wei, 2009; Dutta and Sengupta, 2011).

The literature on the performance of the Turkish insurance companies has been also limited. Ciftci (2004) investigates the technical efficiency of life and non-life insurance companies in Turkey over the 1998 to 2002 period using DEA. Kilickaplan and Basturk (2004), address the technical efficiency issue in the non-life insurance companies in 2002 using DEA. Kilickaplan ve Karpat (2004) evaluate the total, technical and scale efficiencies of Turkish life insurance companies in the 1998 to 2002 period by using Tobit model. Sezen et al. (2005), also analyze the technical efficiency of the non-life insurance companies in the 1998–2003 period. Kasman and Turgutlu (2007) investigate the technical efficiency of a sample of Turkish life insurance companies, using the DEA, chance-constrained DEA (CCDEA) and stochastic frontier analysis (SFA) for the period 1999-2005. Kasman and Turgutlu (2009) examine the cost efficiency and scale economies of insurance companies in the Turkish insurance industry over a 15-year period, 1990–2004 (Kilickaplan and Karpat, 2004; Kasman and Turgutlu, 2007; 2009).

The primary aim of this study is to examine the technical efficiency performance of non-life insurance companies in Turkey in 2007 by using two base DEA models CCR and BCC and finding the most efficient ones. Additionally, finding how much the inputs of the inefficient insurance companies should be decreased and how much the outputs of them should be increased for making them efficient as the others.

2. The Concept of Efficiency and Data Envelopment Analysis

Efficiency is commonly defined as inputs/outputs and it is aimed to maximize the outputs from a given set of inputs. In the case of the insurance industry we would like to maximize our profit, or similarly we would like to minimize our costs (Harton, 2010). Modern efficiency measurement was started by Farrell (1957), who proposed that the efficiency of a firm consists of two components: technical efficiency (TE) and allocative efficiency. TE reflects the ability of a firm to obtain maximal output(s) from a given set of input(s) or to use minimal input(s) to obtain a fixed level of output(s). Allocative efficiency reflects the ability of a firm to use the input(s) in optimal proportions, given their respective prices. These two measures are then combining to provide economic efficiency. The objective of TE can be achieved by many combinations of inputs that are a feasible set of efficient input mixes (Dutta and Sengupta, 2011).

Farrell (1957) first advanced the concept of deterministic non-parametric frontier to measure the relative technical efficiency employing the envelope curve. Measured units lying on the production frontier are efficient for their combinations of inputs and outputs, whereas others that are not lying on the production frontier are inefficient. Farrell defined that TE multiplied by allocative efficiency is overall one. Afterwards Charnes, Cooper and Farrell (1978) developed DEA model which was extended from signal input and output to multiple inputs and outputs. DEA is a nonparametric linear programming technique, which constructs a linear frontier and measures the relative efficiency of a set of similar units, usually referred to as decision making units (DMUs). Its concept is that the best practice for firms lying on the production frontier, which results in having an efficiency value of one. In contrast, the firms being below the production frontier have a less value than one and they are said to be less efficient (Chen and Lin, 2007; Kumar and Gulati, 2008).

Since DEA is a mathematical programme for measuring performance efficiency of organizations popularly named as DMUs, the DMU can be of any kind such as manufacturing units, a number of schools, banks, hospitals, police stations, firms etc. DEA measures the performance efficiency of these kinds of DMUs, which share a common characteristic that they share non-profit organization where the measurement is difficult. Although DEA was initially used to assess the relative efficiency of not-for-profit organizations such as schools and hospitals, gradually its application has been extended to cover for-profit organizations such as banks as well. Over the years, DEA has emerged as a very significant technique to measure the relative efficiency of banks (Kumar and Gulati, 2008; Mantri, 2008). Evaluation of efficiency and productivity using DEA has become a popular method by many scholars around the world. However the banking industry has been the most frequently evaluated and measured sector compared to the insurance industry (Abidin and Cabanda, 2011). DEA assumes the performance of the DMU using the concepts of efficiency or productivity, which is measured as the ratio of total outputs to total inputs. The efficiencies estimated are relative to the best performing DMU is given a score of 100 % and the performance of the other DMUs vary between 0-100 % (Mantri, 2008). The number of DMUs to be compared depends on the objectives of the DEA study and the number of homogenous units required to be compared in the application. Nevertheless there are various opinions regarding the number of DMUs. Norman and Stoker (1991) argued that the number of DMUs should be at least 20. According to Boussofiane (1991), in terms of the reliability of the study there should be at least (m+n+1) number of DMUs, where m is the number of inputs and n is the number of outputs (Bakirtas et al., 2010).

A measure of technical efficiency under the assumption of constant returns-to-scale (CRS) is known as a measure overall technical efficiency (OTE). The OTE measure helps to determine inefficiency due to the input/output configuration as well as the size of operations. In DEA, OTE measure has been decomposed into two mutually exclusive and non-additive components: pure technical efficiency (PTE) and scale efficiency (SE). This decomposition allows an insight into the source of inefficiencies. The PTE measure is obtained by estimating the efficient frontier under the assumption of variable returns-to-scale. It is a measure of technical efficiency without scale efficiency and purely reflects the managerial performance to organize the inputs in the production process. Thus, PTE measure has been used as an index to capture managerial performance. The ratio of OTE to PTE provides SE measure. The measure of SE provides the ability of the management to choose the optimum size of resources (Kumar and Gulati, 2008).

3. Data Envelopment Analysis Models and Super Efficiency Approach

There are many different variations of DEA, but the two most basic approaches in DEA as constant returns to scale and variable returns to scale. The model built on constant return to scale assumption is called CCR (Charnes, Cooper, Rhodes), while the model based on variable return to scale assumption is called BCC (Banker, Charnes, Cooper). According to Charnes et al. (1978) there is an

important relation between the scales and the efficiencies of the enterprises studied under constant return to scale assumption. As per CCR approach, in situations in which all inputs can be controlled, the input-oriented models and output-oriented models give the same relative efficiency values. However, according to Banker et al. (1984) an increase in inputs leads to a disproportionate increase in outputs. Therefore, as per BCC approach, while input-oriented models enable determination of how much the inputs of the inefficient DMUs should be decreased in order to be able to obtain a certain output level; output-oriented models enable the determination of how much the outputs should be increased so that inefficient DMUs become efficient with a given input combination (Bakirtas et al., 2010; Harton, 2010). Allowing variable returns to scale effectively means when defining efficiency of a given insurance company it is only compared to other insurance company of a similar size. Assuming scale advantage exists, this is equivalent to compensating smaller organizations for their reduced efficiency. Assuming that economies of scale exist, within a BCC model a small organization will appear efficient, but within a CCR model the small organization will appear inefficient (Harton, 2010).

3.1. CCR model

The CCR model can be classified into input-oriented model, which minimizes the input levels given output levels and output-oriented model, which maximizes the output levels given input levels. Under the assumption of constant returns to scale which indicates input levels rise proportionally to output levels, the overall TE value will equal using input-oriented model or output-oriented model (Chen and Lin, 2007). CCR applies to the situation, in which all DMUs operate under the most suitable scale. However, DMUs may not operate under optimum scale due to full competition conditions not being present, finance problems and other reasons (Bakirtas et al., 2010)

3.1.1. Input-oriented CCR model

To evaluate the efficiency of the kth DMU, we have to minimize the input levels given output levels. In other words, we analyze the “maximization” of output levels given input levels for DMU_k using the following method. The original fractional programming is as in Eq. (1) (Ciftci, 2004; Chen and Lin, 2007; Abidin and Cabanda, 2011).

$$\begin{aligned}
&\max h_k = \sum_{r=1}^{s} u_r y_{rk} / \sum_{i=1}^{m} v_i x_{ik} \\
&\text{subject to } \sum_{r=1}^{s} u_r y_{rj} / \sum_{i=1}^{m} v_i x_{ij} \le 1 \quad j = 1, \cdots, n \\
&v_i \ge 0;\ i = 1, \cdots, m \\
&u_r \ge 0;\ r = 1, \cdots, s
\end{aligned} \tag{1}$$

In Eq. (1) h_k is the estimate of relative efficiency for the kth DMU_k, u_r is the rth weighted level of inputs for the kth DMU, v_i is the ith weighted level of inputs for the jth DMU, x_{ij} is the ith level of inputs for the jth DMU, y_{rj} is the rth level of outputs for the jth DMU (Chen and Lin, 2007). As it is difficult to find solutions using the fractional programming and is likely to calculate infinite solutions, the fractional programming is transformed into the linear programming and solutions are found using the duality which is in favor of reducing the number of constraints. The linear programming is as in Eq. (2) and the duality in linear programming is as in Eq. (3) (Ciftci, 2004; Chen and Lin, 2007; Abidin and Cabanda, 2011).

$$\max h_k = \sum_{r=1}^{s} u_r y_{rk}$$
$$\text{subject to} \sum_{i=1}^{m} v_i x_{ik} = 1,$$
$$\sum_{r=1}^{s} u_r y_{rj} - \sum_{i=1}^{m} v_i x_{ij} \le 0; \quad j = 1, \cdots, n$$
$$v_i \ge 0; i = 1, \cdots, m$$
$$u_r \ge 0; r = 1, \cdots, s \tag{2}$$

$$\min w_k = q_k$$
$$\text{subject to} \sum_{j=1}^{n} y_{rj} \lambda_j \ge y_{rk}; r = 1, \cdots, s$$
$$\sum_{j=1}^{n} x_{ij} \lambda_j \le q_k x_{ik}; \ i = 1, \cdots, m$$
$$\lambda_j \text{ is the weight } \lambda_j \ge 0; \quad j = 1, \cdots, n$$
$$-\infty \le q_k \le +\infty \tag{3}$$

The development of output-oriented model is the same as for input-oriented one. To evaluate the efficiency of the kth DMU, we have to maximize the output levels given input levels using the same method mentioned above in input-oriented model. In the case of evaluation of efficiency, no matter which model is chosen. The value of q_k which is equal to one indicates that DMU_k is relatively efficient, whereas the value of q_k which is less than one indicates that DMU_k is relatively inefficient (Chen and Lin, 2007).

3.2. BCC model

Banker, Charnes and Cooper (1984) presented the BCC model which applies to the cases of variable returns to scale. The efficiency values obtained from the solution of BCC model is named as TE. In this way determination of TE value also enables the measurement of SE value. By evaluating the current input combination optimally, the success rate for the generation of the biggest possible outcome is defined as TE, the success in producing on optimum scale is defined as SE. BCC model measures PTE and calculates SE using OTE in CCR model divided by PTE. Hence, we further know inefficiency mainly stems from pure technical inefficiency or scale inefficiency. As the CCR model, the BCC model also can be classified into input-oriented model and output-oriented model (Chen and Lin, 2007; Bakirtas et al., 2010).

3.2.1. Input-oriented BCC model

The original fractional programming is as in Eq. (4) and the linear programming is as in Eq. (5) (Ciftci, 2004; Chen and Lin, 2007).

$$\max z_k = \sum_{r=1}^{s} u_r y_{rk} - u_0 / \sum_{i=1}^{m} v_i x_{ik}$$
$$\text{subject to} \sum_{r=1}^{s} u_r y_{rj} - u_0 / \sum_{i=1}^{m} v_i x_{ij} \le 1,\ j = 1,\cdots,n$$
$$u_r \ge 0;\ r = 1,\cdots,s$$
$$v_i \ge 0;\ i = 1,\cdots,m$$
$$u_0 \in (-\infty,+\infty) \tag{4}$$

$$\text{Max}\, z_k = \sum_{r=1}^{s} u_r y_{rk} - u_0$$
$$\text{subject to} \sum_{i=1}^{m} v_i x_{ik} = 1,$$
$$\sum_{r=1}^{s} u_r y_{rj} - \sum_{i=1}^{m} v_i x_{ij} - u_0 \le 0,\ j = 1,\cdots,n$$
$$u_r \ge 0;\ r = 1,\cdots,s$$
$$v_i \ge 0;\ i = 1,\cdots,m \tag{5}$$

The duality in linear programming is as follows (Ciftci, 2004; Chen and Lin, 2007):

$$\min w_k = q_k$$
$$\text{subject to} \sum_{j=1}^{n} y_{rj}\lambda_j \ge y_{rk},\ r = 1,\cdots,s$$
$$\sum_{j=1}^{n} x_{ij}\lambda_j \le q_k x_{ik},\ i = 1,\cdots,m$$
$$\sum_{j=1}^{n} \lambda_j = 1$$
$$\lambda_j \text{ is the weight } \lambda_j \ge 0; \quad j = 1,\cdots,n$$
$$-\infty \le q_k \le +\infty \tag{6}$$

The concept of output-oriented model is the same as for input-oriented one. To evaluate efficiency of the kth DMU, we have to maximize the output levels given input levels using the same method mentioned above in input-oriented model (Chen and Lin, 2007).

3.3. Super efficiency approach

The super-efficiency model gives efficiency scores by eliminating the data on the DMU to be evaluated from the solution set. For the input model this can result in values which give the DMU the status of being “super efficient”. These values are then used to rank the DMUs and thereby eliminate some (but not all) of the ties that occur for efficient DMUs (Yen and Othman, 2011).

Assume there are m inputs, s outputs and n DMUs. Andersen and Petersen (1993) excluded DMU_j from the decision-making reference collection and the super-efficiency score of DMU_j is estimated as follows (Chen et al., 2010).

super-BCC Model:

$$\min_{E_j,\lambda_1,\lambda_2,\cdots,\lambda_n} \quad E_j$$

$$\text{subject to } E_j X_j - \sum_{\substack{k=1\\k\neq j}}^{n} z_k X_k \geq 0$$

$$-Y_j + \sum_{\substack{k=1\\k\neq j}}^{n} z_k Y_k \geq 0$$

$$\sum_{\substack{k=1\\k\neq j}}^{n} z_k = 1$$

$$z_k \geq 0, k = 1,\cdots,n$$

$$E_j \text{ is free} \tag{7}$$

In Eq.(7), E_j is the super-efficiency score of DMU_j estimated by the Andersen and Petersen (AP) model; X_j is the input vector of DMU_j; Y_j is the output vector of DMU_j; z_k is the intensity of DMU_k. This model's feature is to exclude the DMU out of the reference set. If the DMU is inefficient, then the reference set does not change in this model. On the other hand, the frontier will change if the DMU is efficient and the score of efficiency is larger than 1. This says that the AP model does not change an inefficient DMU's score, but an efficient DMU's score in this model is larger than 1. Therefore, this model seems to solve for the efficiency with a value of the rankings, but follow-up scholars find that this model can't be estimated (infeasible). In practice, they are still unable to model all efficient DMUs and do the right value rankings (Chen et al., 2010).

4. Application and Results of Analysis

In this study, the performances of non-life insurance companies operating in Turkey in 2007 are examined using DEA. The input-oriented CCR and BCC models are obtained for each insurance company. By using an input orientation, one can determine whether an insurance company can produce the same level of input with less ouput. In addition, super efficiency model is estimated to find the degree of efficiency of insurance companies.

The first step in DEA is determination of the DMUs. In this study, DMUs are non-life insurance companies. The data were collected from insurance and pension annual report 2007 of the Republic of Turkey Prime Ministry Undersecretariat of Treasury Insurance Supervisory Board. The second step of DEA is determination of inputs and outputs. In this study, the number of agents, the number of brokers, fixed assets, shareholders' equity are considered as input variables and investment incomes, premiums as output variables. Determination of inputs and outputs based on the conclusion of review previous studies on insurance companies. The data set used in this study is presented as in Table 1.

Table 1: Insurance Companies, Inputs and Outputs

	Input 1	Input 2	Input 3	Input 4	Output 1	Output 2
Insurance Company	**Number of Agents**	**Number of Brokers**	**Fixed Assets**	**Shareholders' Equity**	**Investment Incomes**	**Premiums**
AIG	309	28	1849842	23260911.01	3238697.48	154397637.2
AKSİGORTA	1401	33	49736439	2638533699	120606335.1	792710644.6
ANADOLU	1453	54	20423428	644088129.1	127879695.6	1192587098
ANKARA	487	33	2729739	52972876.69	9090090.03	192121733.8
AVIVA	622	44	1206411	69484574.81	22554504.58	223215268.3
AXA OYAK	1452	33	32600134	352910426.8	115685481.4	1129744758
BAŞAK GROUPAMA	1332	43	16419247	90060082.94	40860200.85	467986891.1
BİRLİK	357	11	167307	10387875	1742464	113616205
ERGOİSVİÇRE	1381	44	12688202	141682313.7	26252188.39	636646722
EUREKO	119	38	2306771	94995703.18	9692422.83	415466359.4
FİBA	603	36	4408759	9411580.41	3631319.61	289331062.3
GENERALİ	258	27	65797154	196984011	20575772.05	74543116.65
GÜNEŞ	1143	48	17090344	68644764.17	10668780.95	637523807.8
GÜVEN	2601	15	5328586	20245171.02	4118918.37	222893121.5
HDI	601	22	4085995	10188097.51	3903096.94	157754632.4
HÜR	542	6	1418499	51178905.09	9468866.61	42047858.31
IŞIK	362	9	31852007	255121836.8	59135211.02	105492692.5
KOC ALLIANZ	1224	48	11864804	45252527.61	8785354.05	860806488
LIBERTY	373	16	17326104	49079914.8	9014028.07	151718242.4
RAY	492	34	-1503922	25546917.71	3358135.69	270988567.3
TEB	142	34	1209190	19911303.5	2721301	154835614.2
T. GENEL	302	38	30715845	253598078.9	34433888.57	321761159.4
YAPI KREDİ	711	24	719326	25558045.86	5034278.84	628142638.6

Techinical efficiency scores related to insurance companies in Table 1 are obtained from input-oriented CCR and BCC models. The results of CCR and BCC models are illustrated in Table 2 and Table 3, respectively.

Table 2: The results of CCR

CCR Model		
DMUs	**Efficiency**	**Referans sets**
AIG	0.5578	6 (0.02) 1.0 (0.02) 2.3 (0.20)
AKSİGORTA	0.5251	3 (0.02) 6 (0.66) 1.7 (0.70)
ANADOLU	**1.0000**	**2**
ANKARA	0.5764	5 (0.17) 6 (0.04) 1.0 (0.01) 2.3 (0.17)
AVIVA	**1.0000**	**4**
AXA OYAK	**1.0000**	**8**
BAŞAK GROUPAMA	**1.0000**	**4**
BİRLİK	0.7065	5 (0.04) 2.0 (0.03) 2.3 (0.16)
ERGOİSVİÇRE	0.5796	5 (0.00) 6 (0.20) 2.3 (0.66)
EUREKO	**1.0000**	**6**
FİBA	**1.0000**	**2**
GENERALİ	0.4932	10 (0.10) 1.7 (0.33)
GÜNEŞ	0.6317	6 (0.05) 1.0 (0.02) 2.3 (0.91)
GÜVEN	0.6706	6 (0.00) 7 (0.06) 2.3 (0.31)
HDI	0.9075	7 (0.05) 1.1 (0.46)
HÜR	0.9753	3 (0.06) 5 (0.05)
IŞIK	**1.0000**	**3**

KOC ALLIANZ	0.8453	7 (0.05) 1.1 (0.08) 2.3 (1.30)
LIBERTY	0.5593	6 (0.06) 7 (0.03) 2.3 (0.11)
RAY	**1.0000**	**1**
TEB	0.9204	6 (0.01) 1.0 (0.13) 2.3 (0.15)
T. GENEL	0.7750	1.0 (0.65) 1.7 (0.48)
YAPI KREDİ	**1.0000**	**9**
Mean	**0.8141**	

Table 3: The results of BCC

BCC Model		
DMU	**Efficiency**	**Referans sets**
AIG	0.8340	6 (0.01) 8 (0.46) 1.0 (0.02) 2.1 (0.50) 2.3 (0.01)
AKSİGORTA	0.7175	3 (0.40) 6 (0.60)
ANADOLU	**1.0000**	**2**
ANKARA	0.7162	3 (0.00) 5 (0.10) 6 (0.04) 8 (0.50) 1.0 (0.04) 2.1 (0.31)
AVIVA	**1.0000**	**1**
AXA OYAK	**1.0000**	**8**
BAŞAK GROUPAMA	**1.0000**	**0**
BİRLİK	**1.0000**	**6**
ERGOİSVİÇRE	0.5920	6 (0.20) 8 (0.12) 2.1 (0.06) 2.3 (0.62)
EUREKO	**1.0000**	**5**
FİBA	**1.0000**	**0**
GENERALİ	0.6845	8 (0.09) 17 (0.32) 2.1 (0.60)
GÜNEŞ	0.6320	6 (0.05) 1.0 (0.02) 2.1 (0.02) 2.3 (0.90)
GÜVEN	0.9135	6 (0.02) 8 (0.80) 1.6 (0.00) 2.3 (0.18)
HDI	**1.0000**	**0**
HÜR	**1.0000**	**1**
IŞIK	**1.0000**	**3**
KOC ALLIANZ	**1.0000**	**0**
LIBERTY	0.9065	6 (0.01) 8 (0.76) 1.0 (0.09) 1.7 (0.09) 2.1 (0.05)
RAY	**1.0000**	**0**
TEB	**1.0000**	**6**
T. GENEL	0.7960	6 (0.04) 1.0 (0.55) 1.7 (0.40)
YAPI KREDİ	**1.0000**	**4**
Mean	**0.9040**	

As seen from Table 2 and 3, as the results of input-oriented CCR and BCC models, the insurance companies of which efficiency score is 1 are considered as efficient. The efficiency score less than 1 shows that insurance company is inefficient. According to CCR model, nine of the insurance companies are efficient and the mean of efficiency is 0.81 that means the inputs should be reduced at level 19 %. According to BCC model, fifteen of insurance companies are efficient and the mean of efficiency is 0.90 that means the inputs should be reduced at level 10 %.

It is assumed that inefficient DMUs can be achieved at the same level of efficient insurance companies in DEA. For this purpose, it should be computed how much input quantities reduced and how much output amounts increased to improve the efficiency of inefficient DMUs as to efficient DMUs. For example, in Table 2 AIG is not efficient. Hence, some changes should be made using intensity values of efficient DMUs in reference sets related to AIG. As seen from Table 2, AXA OYAK, EUREKO and YAPI KREDİ are reference insurance companies for AIG and the intensity values of these are 0.02, 0.02 and 0.2 respectively. Accordingly, the input values and output values, which are required as to AIG be effective, are computed from Table 1 and Table 2 as below:

Number Agents: 0.02 (1452) + 0.02 (119) +0.2 (711) = 174
Number of Brokers: 0.02 (33) + 0.02 (38) +0.2 (24) = 6
Fixed Assets: 0.02 (32600134) + 0.02 (2306771) +0.2 (719326) = 842003.3
Shareholders'Equity: 0.02 (352910426.8) + 0.02 (94995703.18) +0.2 (25558045.86) = 14069732
Investment Incomes: 0.02 (115685481.4) + 0.02 (9692422.83) +0.2 (5034278.84) =3514414
Premiums: 0.02 (1129744758) + 0.02 (415466359.4) +0.2 (628142638.6) =156532750

Same computations can be made for the other inefficient insurance companies From Table 2 and Table 3.

The efficiency levels of insurance companies are found utilizing the super efficiency model in EMS program. The results of super efficiency model are obtained as in Table 4.

Table 4: The results of Super Efficiency model

CCR Model				**BCC Model**	
	DMUs	Efficiency		DMUs	Efficiency
1	AIG	0.5578	1	AIG	0.8340
2	AKSİGORTA	0.5251	2	AKSİGORTA	0.7175
3	**ANADOLU**	**1.0408**	**3**	**ANADOLU**	**Big value**
4	ANKARA	0.5764	4	ANKARA	0.7162
5	**AVIVA**	**1.5211**	**5**	**AVIVA**	**1.6997**
6	**AXA OYAK**	**1.5242**	**6**	**AXA OYAK**	**1.5943**
7	**BAŞAK GROUPAMA**	**1.3420**	**7**	**BAŞAK GROUPAMA**	**1.3713**
8	BİRLİK	0.7065	**8**	**BİRLİK**	**2.3788**
9	ERGOİSVİÇRE	0.5796	9	ERGOİSVİÇRE	0.5920
10	**EUREKO**	**3.2067**	**10**	**EUREKO**	**3.7378**
11	**FİBA**	**1.4500**	**11**	**FİBA**	**1.5393**
12	GENERALİ	0.4932	12	GENERALİ	0.6845
13	GÜNEŞ	0.6317	13	GÜNEŞ	0.6320
14	GÜVEN	0.6706	14	GÜVEN	0.9135
15	HDI	0.9075	**15**	**HDI**	**1.1836**
16	HÜR	0.9753	**16**	**HÜR**	**2.0126**
17	**IŞIK**	**1.3787**	**17**	**IŞIK**	**1.6081**
18	KOC ALLIANZ	0.8453	**18**	**KOC ALLIANZ**	**3.9202**
19	LIBERTY	0.5593	19	LIBERTY	0.9065
20	**RAY**	**Big value**	20	**RAY**	**Big value**
21	TEB	0.9204	**21**	**TEB**	**1.9031**
22	T. GENEL	0.7750	22	T. GENEL	0.7960
23	**YAPI KREDİ**	**2.4317**	**23**	**YAPI KREDİ**	**9.1631**

As seen from table 4, the most efficient insurance company is RAY, the second efficient company is EUREKO and the third efficient company is YAPI KREDİ according to CCR, while the most efficient companies are RAY and ANADOLU, the second efficient company is YAPI KREDİ and the third efficient company is KOC ALLIANZ. The most efficient insurance company is RAY according to both CCR and BCC models.

5. Concluding Remarks

Parallel to global insurance market, there are two main insurance groups, life and non-life according to Turkish Insurance Regulation. In this study, the technical efficiencies of 23 non-life insurance

companies in 2007, which are active in Turkey, are examined. For this purpose, we benefited from Data Envelopment Analysis which facilitates to examine different input-output components and which is a non-parametric method. As inputs; the number of agents, the number of brokers, fixed assets, shareholders' equity and as outputs; the investment incomes, premiums received are used. Empirical results show that according to CCR model the most efficient insurance companies are RAY, EUREKO and YAPI KREDI, respectively. However according to BCC model, RAY and ANADOLU insurance companies come first, the second one YAPI KREDI and the third one is KOC ALLIANZ. As a consequence of this study, in 2007 in Turkey the most efficient insurance company is RAY according to both CCR and BCC models.

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Impact of Information and Interactive Communication Technologies (ICT) on Relationship Personalization - Has Privacy Become a Commodity?

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Abstract

Purpose: The purpose of this paper is to see if information and interactive communication technologies will be able to actually enable true interaction and personalization with consumers. Precondition for automatization, true interaction and relationship personalization is the exchange of information (knowledge) with each other (company and consumer). With this in mind – privacy is for sure an important concept. Although, consumers are generally concerned about their privacy – the question arises: Has privacy become a commodity? Can companies "buy" consumers' privacy and get the needed information for relationship personalization? So, this paper analyzes what information are consumers willing to give (and for what compensation) – as a necessary precondition for ICT implementation in marketing.

Methodology: For this paper we have used on-line survey on convenient sample of Internet users in Croatia (n=1.083). Respondents were encouraged to fill out the on-line questionnaire through:

- viral marketing
- banner / link on the Croatian only search portal www.pogodak.hr
- banners / links on web pages of different companies
- posts on different Croatian forums

Findings: Two main hypotheses that are researched in this paper are: Consumers are willing to provide information about themselves to companies (H1). Consumers expect a compensation for the personal information they provide to companies (H2). As it turns out, consumers do not have a problem with providing personal information to companies, but expect a certain compensation (analyzed in this paper) for it. Thus both H1 and H2 are accepted.

Implications: These findings have implications on the how can companies motivate consumers to provide information (cost-effectively) for interactive marketing communication and the development of personalized relationships. They give insight into what consumers perceive as their adequate benefit for developing the interactive personalized relationships with companies.

Keywords

Privacy, personalization, interactivity, relationship marketing, ICT, communications, technology

Introduction

Interactive marketing communication and relationship personalization present some of the most recent developments in the field of marketing communication and marketing in general (Vlasic, 2005a). Technology developments (both software and hardware) have enabled cost effective interactive communication and thus cost effective management of personalized relationships with each consumer individually. Thus, if adequately implemented interactive communication enabling relationship personalization could result in substantial savings for companies and in significant satisfaction increase for consumers.

Due to these facts, this paper analyzes if consumer privacy has become a commodity – ready to be "sold" on market for adequate compensation. This is closely related to the concepts of interactive marketing communication, relationship personalization and consumer privacy – which are further defined.

Conceptualizations of Interactive Marketing Communication

Interactive marketing communication is one of the most intensively developing fields in marketing, and does not represent a short-term hit but rather a long-term strategy which includes a change of business philosophy where consumers are becoming partners (Rodriguez Peraldo and Barwise, 2005). Deigton and Grayson have in 1995 envisaged that non-interactive marketing communication will start to evolve into interactive communication with consumers which, supported by digital monitoring and management of interactions, will enable maintenance of dialogue and relationship with each consumer individually with lower costs (Deighton and Grayson, 1995).

Definitions of interactive marketing communication are numerous. Computer Science dictionary (Panian, 2005) defines it as a communication where sources exchange roles of transmitter and receiver. One of the most relevant basic definitions was given by Deighton and Blattberg who define it as a possibility for people and businesses to communicate directly regardless of space and time constraints (Blattberg and Deighton, 1998). This aspect is also analyzed by Hoey who stresses the possibility of direct communication without time-space constraints as the main characteristic and advantage of interactive marketing communication (Hoey, 1998). From a sociological point of view, interactive marketing communication represents a culmination of information society which surpasses machines and automatization as a development stimulus (Patterson, 1998).

Some authors stress the measurability as an important aspect of interactive marketing communication where there is a feedback enabling the quantification of results of every single communications effort (Marowitz and Schmittlein, 1998). In addition, it is defined as a marketing system which uses one or more media in order to achieve measurable responses or transactions on any given location, where measurability of responses represents the main difference in comparison to traditional communication.

Some authors analyze the interactive marketing communication from the aspect of implementation, and point out that it enables small and medium size companies to equivalently compete with the big companies which have incomparable budgets for communication purposes (di Talamo 1994) because it enables communication on narrow segmented markets as well as mass markets (Young, 1993), and is adequate both for domestic and foreign markets.

Interactive marketing communication can also be viewed from the aspect of communication and information control. Thus, Steuer defines interactivity as strength of impact of each individual party

on format and content in real time (Liu and Shrum, 2005). This aspect is also stressed by other authors (Lockenby, 2005) pointing that interactivity is basically the possibility to control and influence information, where information is not presented linearly but rather, their flow depends on activities of both consumer and company. Sohn and Lockenby (Lockenby, 2005) suggest that interactivity is a concept dependent on processes where each individual takes an active role in socio-communication process and thus influences the interactivity of communication. Interactivity can also be defined as a degree of influence from included participants on each other, communication media, message and the synchronization of these, with three main dimensions: active control, two-way communication and synchronization (Liu and Shrum, 2005). Attention should be given to such definitions due to the fact that interactivity enables certain pleasures like convenience, diversity, relationship, intellectual challenges with a very important aspect of control of communication and relationships.

Literature also includes definitions which closely analyze personalization of relationships and interactive marketing communication, and imply that interactive marketing communication is a system in which personalized information based on personal information on consumers and their preferences are instantaneously present (Olson and Widing, 2002; Ariely, 2000; Habul and Trifts, 2000). IBM stresses that interactive marketing has become a critical factor of personalization of experiences, and thus of business success (Anderson, 2000).

The simplest and most comprehensive definition of interactive marketing communication as a base for interactive marketing and relationship personalization defines it as any method which enables prospect or consumer to give instantaneous feedback through the same or different medium of the original message through: orders, requests for additional information, purchases, etc. including most simple form (i.e. 0800 numbers), through more complex forms (i.e. audio and video text) to most complex ones (i.e. interactive TV and virtual reality) (Ryan, 2001).

After thorough analysis of mentioned definitions, it is possible to point out most important **concepts related to interactive marketing communication**:

- Interactive marketing communication includes at least two parties who have a capability of communication and information control
- Interactive marketing communication includes two-way communication, that is a dialogue
- Interactive marketing communication includes personalization of communication, that is adaptation of communication form and content to each consumer individually
- Interactive marketing communication implies a possibility of momentary feedback from all included parties through the same medium or different ones
- Interactive marketing communication abolishes time-space constraints
- Interactive marketing communication enables precise measurability of results
- Interactive marketing communication can be initiated through non-interactive media

Conceptualizations of Relationship Personalization

Relationship personalization represents development and maintenance of long-term profitable relationships between companies and consumers based on mutual understanding and cognition along with the concept of added value. In such relations company personalizes every aspect of relationship with a consumer including marketing communication, product, price and place. Thus, personalized marketing provides experiences for a known consumer (Stone and Jacobs, 2001). In further text, connected terms to personalization will be presented.

Customization results in the development of products and services customized to consumers' needs and wants. As such, it represents an important part of relationship personalization. Collaborative customization is a result of the development of interactivity resulting in added value through interactive relationship between consumers and companies (Gilmore and Pina, 1997). Besides this type of customization, companies develop so called mass customization where they produce variable and adaptive products and services at cost of mass production (Wind and Rangaswamy, 2001). As such it represents a transitional type toward full customization at comparable costs which is enabled by new technologies (Baker et al., 1998). Due to such development mass production, and even mass customization, lose their main comparative advantage – cost reduction with customization becoming an optimum solution. So, consumers do not have to make compromises, while at the same time companies do not have to invest their liquid assets for the production with questionable results.

Database marketing, unlike relationship personalization, is focused on the company with no, or very limited, personalization of offering. Relationship marketing, unlike database marketing, is based on long-term relationships which are result of needs satisfaction and not of contact frequency and short-term transactional orientation which are stressed in database marketing (Baker et al., 1998). Thus, database marketing uses basic information on consumers to customize the communication, but disregards the customization of other aspects of marketing.

Other interrelated concepts to relationship personalization include precision marketing which, through technological platforms and data analysis methods enables specialized and personalized approach to every consumer (Zabin and Brebach, 2004). It is also possible to define it as technology enabled process of acquisition and management of information on consumers, and analysis of data in order to obtain strategic information which could be used to develop more efficient and profitable interactions with consumers (Zabin and Brebach, 2004). Precision marketing, unlike relationship personalization, aims to develop precise and customized relationship, but it ignores the development of long-term relationships and long-term profit requirements.

Other concepts are one-to-one marketing and relationship marketing which represent most closely related concepts to relationship personalization. With the technological advances, some authors have renamed relationship marketing into technologicalship marketing in order to stress the importance of technology in marketing (Zinedin, 2000).

All the mentioned concepts are related to relationship personalization, but relationship personalization also includes and important concept of knowledge exchange which results in added value for all parties involved. Knowledge exchange concept requires trust and acquaintance between consumers and companies. True relationship personalization requires managerial as well as emotional competencies from companies (Pones and O'Brien Kelly, 2000).

Personalization includes all mentioned concepts, but also incorporates some additional factors:

- Knowledge exchange

- Stressing the intangible aspects which add value
- Increased consumers' expectations caused by interaction and personalization
- Cost factor
- Reduction of choice complexity due to personalization

Thus, relationship personalization can be defined as a marketing conception which assumes relationship development between consumers and companies, based on mutual understanding, developed and continuous knowledge exchange through interactive communication with a goal of achieving added value for all parties involved.

Consumer Privacy

Consumer privacy could be defined as a right not to be disturbed, right to anonymity, right not to be under surveillance, and a right for control of information usage the companies have on them (Gattiker et al.). Although, today there is a great concern for privacy – which was recently „lost", the truth is that anonymity is just a concept of today's world (Deighton, 2005). Strangers (anonymous people) were very rare sociological category in the past, and were considered to be dangerous. This has started to change only with the development of metropolitan cities in 19th century and mass transport development (Deighton, 2005). At that time, personal acquaintance was only being developed among very few close friends / family members; for all other purposes, identification was developed through personal documentation (i.e. passports, IDs, etc.).

Today, consumers have become more self-aware, and are willing to cooperate with companies – aware of their importance for modern production / „servuction" processes. It is implausible that some companies were still (in 20th century) able to make profits by developing generic products, even profiting from harmful products. Modern business practices take special care of consumer protection and delight. Consumer protection is more and more precisely legislatively defined – both at country level, and at international level (international conventions). In addition, since it is important for companies to maintain / develop consumers' trust, many informal regulations were developed: codexes of different associations, as well as of companies themselves. Consumer privacy was well influenced by consumerism and newly developed information and interactive communication technologies – enabling direct communication between all stakeholders independently.

Basic consumer rights could be defined as (Previsic and Ozretic Dosen, 2004):

- Right to choose freely – the right to choose products he/she wants to buy, companies he/she wants to do business with, time at which he/she wants to develop contact. This right, although logical, is very often violated through contracted commitment.
- Right to be informed – due to the development of ICT, companies cannot withhold certain information from some stakeholders (i.e. consumers). The possibility for consumer deception is being reduced to a minimum.
- Right to be heard – ICT also has a great impact on this consumer right enabling momentary feedback and interactive communication. This was recognized not only as a benefit to consumers, but also as a good possibility to develop long-term interactive personalized relationships between companies and their consumers.
- Right to safety – this right is mostly legislatively defined

Although ICT helped practice some of the consumers' rights more actively, it has led to a new field of possible consumer privacy violation. Due to technology development, companies can collect and analyze great amount of information – developing knowledge which could give them insight into

consumer's actions which even consumers themselves might not be aware of. Thus, a possibility (right) to disconnect will start to present a status symbol.

However, in relation to consumer privacy, it is not the information that companies have which endangers consumers, but the way companies use them. Example is the Personal Emergency Response Systems (PERS) which, based on information collected, enables adequate medical help – however in case of misuse of such information consumer privacy could be seriously endangered (Tomsen and Faith, 2003).

Possibilities of information misuses present potentially the greatest threats to consumers' privacy – thus influencing consumers' willingness to give personal information, endangering the process of interactive marketing (Rodriguez Perlado and Barwise, 2005). This information forces companies to look after consumer privacy through development and implementation of the mentioned company privacy codexes (Stone and Jacobs, 2001; Carol 2002). Legislation sets the privacy protection framework which is just the starting point for true partnership and trust development between companies and consumers.

Privacy could also be defined as a right to be free from unwanted interruptions or as a right to be left alone (Roznowski, 2003). Privacy was one of the first concerns of Internet developers. They have noted that Internet can flourish only if all stakeholders respect information privacy – control of conditions under which information is collected, presented and used (Carol, 2002). In addition, they have recommended that all the information which is collected needs to be stated along with the reasoning and terms of use; what efforts are being made to ensure secrecy, integrity and quality of information; consequences of not providing information; adequate compensation for information provided.

Very often consumer privacy is threatened due to misperceptions of companies that profit maximization and consumer protection are two conquering and mutually negatively correlated goals (Phelps et al., 2001). However, consumer protection and profits present complementary goals common to both consumers and companies (Culnan and Armstrong, 1999).

It is not just important to get consumers to provide information. More importantly, provided information needs to be correct. Since consumers want to have control over the information companies have on them and the way they use them. If consumers are not assured that company will protect their rights, they tend to provide wrong information - and thus incur extra costs to companies (cost of information acquisition, storage, analysis, and wrong conclusions resulting in misplaced actions) (Shenan and Hoy, 1999). Thus, it is cost effective for companies to make extra efforts on ensuring consumer trust.

Even if company ensures customers that their information will be treated „with respect“, the question arises – what do consumers expect in return for provided information. Thus, this paper analyzes the most important „motivators“ which could motivate consumers to give certain personal information.

Research Methodology

The aim of this paper is to analyze what consumers expect in return for their private information. Thus, two hypotheses were set:

H_1:	Consumers are willing to provide information about themselves to companies.
H_2:	Consumers expect a compensation for the personal information they provide to companies.

The research was done through a web survey on the convenient sample of Internet users. Respondents were encouraged to fill out the on-line questionnaire through:

- viral marketing
- banner / link on the Croatian only search portal www.pogodak.hr
- banners / links on web pages of different companies
- posts on different Croatian forums

Sample structure:

Gender	# of respondents	%
Male	357	33
Female	726	67
Total	1083	100

Age	# of respondents	%
24 and under	706	65,2
25 – 34	202	18,7
35 – 44	28	2,6
45 – 54	9	0,8
55 – 64	6	0,6
65 +	1	0,1
Total	952	87,9
Did not reply	131	12,1
Total	1083	100

For definition of expected compensation – focus group was used with 10 participans aging from 15 to 50, male:female = 50:50).

Analysis and Results

Possibility for interactive marketing communication and relationship personalization was thoroughly researched before (Vlasic, 2005; Vlasic and Kesic, 2006). Unfortunately, not much research was done concerning general attitudes to information sharing for marketing purposes. It is well known that information on consumers is the most important marketing resource, especially now that consumers are more demanding, and companies have smaller profit margins (pushing them toward reducing costs through production of personalized products for known buyers).

That is why we have analyzed what compensation do consumers expect for certain “personal” information they provide. Personal information was chosen based on one focus group (10 individuals aging 15 to 50, 50% male). The same procedure was used for choosing the possible adequate compensation options. Thus, consumers were asked what they would require in return for their:

- name
- date of birth
- weight
- height
- address
- fixed telephone number
- cell phone number
- e-mail
- income
- information on family members
- needs and wants I want to satisfy

Offered compensation included:

- Personalization of offering and communication to me
- Adequate financial compensation
- Inclusion in contests
- Adequate discounts
- Free products / gifts
- Other types of compensation
- I would give this information without compensation
- I would never give this information

	Personalization of offering and communication to me	Adequate financial compensation	Inclusion in contests	Adequate discounts	Free products / gifts	Other types of compensation	I would give this information without compensation	I would never give this information
Name	(1) 41,8 %	(5) 23,8 %	(2) 39,7 %	(3) 34,3 %	(4) 30,8 %	(7) 13,0 %	(6) 21,5 %	7,1 %
Date of birth	(1) 38,0 %	(6) 16,4 %	(4) 23,4 %	(3) 24,2 %	(5) 20,4 %	(7) 9,5 %	(2) 36,6 %	4,5 %
Weight	(2) 27,4 %	(6) 12,3 %	(5) 15,1 %	(4) 15,9 %	(3) 17,0 %	(7) 7,8 %	(1) 32,2 %	17,2 %
Height	(2) 28,3 %	(6) 12,9 %	(5) 15,4 %	(3) 16,9 %	(4) 16,4 %	(7) 8,0 %	(1) 35,4 %	13,5 %
Address	(2) 27,9 %	(5) 20,4 %	(1) 34,6 %	(4) 24,2 %	(3) 26,0 %	(6) 10,6 %	(7) 9,7 %	19,2 %
Fixed telephone number	(2) 23,5 %	(5) 17,7 %	(1) 28,9 %	(3) 19,6 %	(4) 19,3 %	(6) 9,0 %	(7) 7,2 %	26,9 %
Cell phone number	(2) 26,2 %	(5) 19,9 %	(1) 30,5 %	(4) 20,3 %	(3) 22,6 %	(6) 9,9 %	(7) 8,2 %	23,5 %
E-mail	(1) 34,3 %	(6) 19,2 %	(2) 30,4 %	(4) 23,8 %	(3) 24,6 %	(7) 12,2 %	(5) 22,0 %	8,8 %
Income	(1) 17,6 %	(2) 13,9 %	(5) 9,3 %	(3) 13,1 %	(4) 10,4 %	(6) 7,2 %	(6) 7,2 %	46,5 %
Information on family members	(1) 16,8 %	(3) 12,6 %	(5) 10,0 %	(2) 13,4 %	(4) 10,6 %	(7) 5,6 %	(6) 6,4 %	49,5 %
Needs and wants I want to satisfy	(1) 37,2 %	(5) 15,4 %	(6) 15,3 %	(3) 19,5 %	(4) 18,2 %	(7) 12,1 %	(2) 22,9 %	13,1 %

	Test Value = 0.5					
	t	df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference	
					Lower	Upper
Name	54,454	1082	,000	,428	,41	,44
Date of birth	59,823	1082	,000	,438	,42	,45
Weight	23,581	1082	,000	,291	,27	,32
Height	27,257	1082	,000	,319	,30	,34
Address	22,693	1082	,000	,284	,26	,31
Fixed telephone number	15,067	1082	,000	,208	,18	,24
Cell phone number	18,968	1082	,000	,250	,22	,28
E-mail	42,574	1082	,000	,396	,38	,41
Income	,881	1082	,378	,013	-,02	,04
Information on family members	-,820	1082	,412	-,012	-,04	,02

	Are willing to provide this information	Are not willing to provide this information
Name	92,8 %	7,2 %
Date of birth	93,8 %	6,2 %
Weight	79,1 %	20,9 %
Height	81,9 %	18,1 %
Address	78,4 %	21,6 %
Fixed telephone number	70,8 %	29,2 %
Cell phone number	75,0 %	25,0 %
E-mail	89,6 %	10,4 %
Income	51,3 %	48,7 %
Information on family members	48,8 %	51,2 %
Needs and wants I want to satisfy	100 %	0,0 %

Results clearly show that consumers are willing to provide their information to companies; especially name, date of birth, and e-mail contacts. Consumer also feel comfortable sharing their information on: weight, height, address, fixed telephone number, cell phone number, needs and wants I want to satisfy.

The only problem consumers have is with sharing their information on family members (the greatest problem) and on their income. These results show that consumers perceive these information to be the most critical. However, since there is no statistical significance in the negative direction, companies could even motivate consumers to provide such information by raising the level of trust. Because, all other information does not necessarily imply the existence of trust – consumers are much more willing to share that information. However, information on income and family assert trust and thus require the most effort by companies. So, it is up to companies to make a cost-benefit analysis if such information would give greater knowledge of consumers – and thus

greater profits, or if it does not pay off to develop such closeness with consumers where they would trust companies enough to provide income and family information.

	Average number of information respondents believe this is adequate compensation*	Average rang according to table above**	Ranking of compensations***
Personalization of offering and communication to me	3,19	1,45	1
Adequate financial compensation	1,85	4,91	6
Inclusion in contests	2,53	3,36	3
Adequate discounts	2,25	3,27	2
Free products / gifts	2,16	3,72	4
Other types of compensation	1,05	6,64	7
I would give this information without compensation	2,09	4,55	5

* it is better to have higher numbers (number of information respondents believe this is adequate compensation); ** it is better to have lower numbers (ranking); *** rankings were calculated using both indicators

Off the offered compensations, "other types of compensation" ranked last – which implies that tested compensation possibilities incorporated all major possibilities for consumers. It is very significant that "personalization of offering and communication to me" ranked first. It is obvious that consumers and companies share the same goal – development of relationship (which includes knowledge of each other) – in order to develop personalization as defined in this paper.

"Inclusion in contests" presents very specific type of consumer motivation (very easily conducted) for providing personal information. Thus, it is very beneficial for companies to organize contests, but the contests need to be developed in such a way that consumers are "forced" to provide correct information (i.e. that in case they win a prize, they will be contacted by post, e-mail, and cell phone – which makes it important for them to put down correct information when entering the contests). However, many companies still today fail to develop adequate contests – they concentrate on short-term sales increase through getting people to send a certain number of packagings. However, it would be much more beneficial for them to endure on getting the consumer information – and develop a long term personalized relationships with "branded customers".

"Adequate discounts" were ranked third, while "adequate financial compensation" ranked sixth. From this it could be concluded that consumers do not necessarily require financial compensation when thinking of prices. Rather, they expect to get something (discount) in return momentarily. This has great implications on customer loyalty programs which usually provide rewards in "cash" – enable consumers to buy certain products for the certain number of points they have collected (in Croatia this is the only option). It is clear that consumers would prefer personalized discounts on certain products they purchase – which could be a joint promotional action by different producers and retailers, increasing true consumer loyalty: both to retailer and to certain brands.

"Free products / gifts" ranked fourth. This could be rooted deeply in Croatian culture – where people always like to receive gifts and to give gifts to others. However, companies need to make sure that provided gifts are useful to consumers, but simultaneously are well branded in order to keep the brand "close to consumer". Such actions have been well developed by beer producers providing branded fridges and pipes to consumers who purchase a certain amount of beer (and are

members of certain beer club). This brings the brand in consumers' homes – and they proudly share it with friends - which has great impact on relationship strengthening.

Fifth place was taken by "I would give this information without compensation". What is really indicative is that this ranked above "adequate financial compensation". Consumers are willing to provide information on themselves – even without compensation if they are provided with adequate reasoning.

Thus, from all mentioned it could be concluded that companies need to communicate to consumers possible benefits from relationship personalization in order to ensure them that their information will just be used for providing better (customized) products / services with certain rewards (contests, discounts, gifts).

	Anonymous communication (companies do not know information about me)	Non-anonymous communication (companies do know information about me)	I do not want to communicate like this
Communication personally with an employee	25,0 %	70,9 %	4,1 %
Communication through e-mail	51,9 %	44,6 %	3,6%
Communication through web sites	76,2 %	16,8 %	7,0 %
Communication through radio	62,5 %	18,0 %	19,5 %
Communication using mobile phone	36,7 %	47,6 %	15,8 %
Communication using fixed phone	36,5 %	49,9 %	13,6 %
Communication on events	36,8 %	56,3 %	6,9 %
Communication through catalogs	54,4 %	24,7 %	20,9 %
Communication through traditional mail	36,1 %	42,1 %	21,8 %

In the research we have also analyzed in what types of communication with companies do consumers wand to be "branded" – so companies have enough knowledge of them. It turns out that consumers wish to be recognized (non-anonymous) when communicating:

- with employees
- using mobile phone
- using fixed phone
- on events organized by companies
- through traditional mail (with a certain reserve - because of small difference between the responses)

On the other side, consumers strictly want to stay anonymous when communication through web sites, radio and catalogs. This could be so because consumers want to be able to search for content of their interest on web sites without being recognized and tracked (which presents a real threat because of which consumers skip some "tricky" web sites). Radio is still perceived as mostly a one-way medium where most consumers (except for ones taking part in radio contests) want to stay anonymous and just be "voyeurs" listening to other people. Catalogs present a way of communication where consumers also want to stay anonymous – making it the best for catalogs to

be distributed in crowded areas giving a possibility for consumers to pick them up and contact a company on their own initiative, without being pressured by company producing catalogs.

E-mail presents a “tricky” way of communication – with approximately the same number of people wanting to be anonymous and those wanting to be recognized. This could be so depending on the type of information people receive through e-mail. If information is spam, it is clear that consumers want to be unrecognizable. However, if offering (information) is personalized, consumers have interest in providing information and maintaining communication.

For further analysis we wanted to analyze what company specific characteristics influence consumers to provide information.

	Test Value = 2					
				Mean Difference	95% Confidence Interval of the Difference	
	t	df	Sig. (2-tailed)	*	Lower	Upper
Large company	,000	1177	1,000	,000	-,03	,03
Small company	8,053	1176	,000	,135	,10	,17
Government owned company	1,524	1172	,128	,029	-,01	,07
Private company	6,099	1171	,000	,107	,07	,14
Domestic company	11,150	1169	,000	,177	,15	,21
Foreign company	,921	1169	,357	,015	-,02	,05
Monopolist	-13,070	1174	,000	-,243	-,28	-,21
Modern company	17,908	1172	,000	,309	,27	,34

* 1 = I do not want to provide personal information; 3 = I do want to provide information.

These results show that consumers are much more willing to provide information to small, domestic, private, modern companies. This could be explained by the strengths of influence consumer could have on a certain company (especially in case of misuse of the information provided).

Thus, small company appreciates each consumer more – and is interested to keep doing business with them. In addition, in smaller companies there is often personal acquaintance present between employees (even the owner) and customers.

Private companies and domestic companies are trusted more – because such companies depend directly on satisfaction of every consumer and each employee has strict responsibilities to owner(s). Thus, it is in their interest that consumers develop long-term relationships (which implies trust) in order to succeed on the market alongside large multinational companies.

Last company related factor is company’s modernity. Consumers perceive modern companies to be more reliable – because they are used to high competition and free market situation (which has started developing in Croatia in 1990’s).

In case of large / government owned / foreign company, consumers have not shown statistical significance. Thus, it could be concluded that such companies need to put in much more effort in ensuring consumers’ trust – and that consumers grade such companies on case-by-case bases.

The only thing that respondents found to be completely repelling (of the company specific characteristics) was the monopolistic situation of a company. In such situation, company has a monopoly and ensured profits enabling it to be irresponsible in relation to consumers (at least in the short run) – making consumers concerned for their privacy.

Conclusion and Implications

Since relationship personalization and interactive communication, enabled by great ICT advances, have become a must, this paper has great implications on consumers' willingness to provide personal information. Besides the specific analysis done in this paper, it was previously concluded that consumers do want to have personalized relationships – but that it is industry dependent (Vlasic and Kesic, 2006). Thus, consumers strictly do want personalized relationships with:

- Health organizations
- Education industry
- Amusement industry
- Banks
- Research agencies
- Cosmetics industry
- Tourist industry
- Producers of durable goods
- Producers of industrial goods
- Producers of consumer goods
- Telecoms

In addition, analysis was done concering factors which influence consumers' willingness to start interaction and develop personalized relationships (Vlasic, 2006). Thus, most important factors which influence consumers to start interactive communication with companies include: company's reputation, adequate compensation, and perceived loyalty towar that company. For relationship personalization, consumers are mostly influenced by: reputation, loyalty, personal contact, well defined legislature, interactivity of communication, prior experiences and trust.

With all mentioned taken into account, some very indicative implications could be concluded:

- companies need to be aware of the industry they are in and about general consumer perceptions toward that industry
- companies should work on:
    - reputation
    - adequate compensation
    - consumers' loyalty
    - personalized contacts
    - legislature development (both through laws and codexes)
    - enabling interactivity of communication
    - ensuring adequare consumer satisfaction (even delight) with prior experiences
    - ensuring consumers' trust

Analyisis clearly shows that privacy has become commodity which consumers are willing to trade with companies for adequate compensation. Both H1 and H2 are accepted. However, companies need to be aware of some guiding principles. Certain information is "easily traded", like:

- name
- date of birth

- weight
- height
- address
- fixed telephone number
- cell phone number
- e-mail
- needs and want consumers want to satisfy

For some information (weight and height), consumers even do not necessarily require compensation – while for most others personalization is the most desirable form of compensation. In return for address and telephone numbers (fixed and mobile), consumers mostly expect to be included in certain contests.

The overall ranking of possible compensations clearly suggests that companies should:

- adequately personalize offering and communication according to their knowledge of the consumer
- offer adequate discounts – which are implemented immediately
- enable consumers to enter contests by providing information (with clear incentive for providing correct information)
- provide free products / gifts to consumers

In addition, certain advantage (easier access to consumer information) is given to small, private, domestic, modern companies for all the above mentioned possible reasons. Also, consumers are more willing to provide information to companies which use personal communication (with an employee), events, fixed and mobile telephones and traditional mail.

With all mentioned in mind, adequate databases could be created and ICT could enable true interactive personalized relationships with each customer individually – creating a utopian approach to marketing activities.

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Applying Marketing Research in Marketing Strategy Formation: The Case of Secondary Education in Croatia

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Abstract

The 21st century is characterized by significant and rapid changes in all spheres of social life, as well as in education as one of the most important bearer of these changes. Today, knowledge on a global scale doubles in a year, and monitoring these changes implies the existence of adequate systems which are ready to accept and use these changes and to keep pace with them for the purpose of growth and progress. In the priority plans and activities of Ministry of science, education and sports and relevant national and European documents in the field of constructing knowledge society, school system in general has to assert itself as a place of education and training, but also as an organization that continuously learns and adapts to demands and needs of its customers.

The role of marketing approach, which has been neglected so far, needs to be asserted in the mentioned framework, even though certain secondary school institutions successfully implement it on an intuitive level by applying ad-hoc measures and marketing management activities. Public sector, and education as its part, cannot remain outside of modern trends in management and performance methods if their goal is to achieve better results, and the adjustment to concrete customer needs certainly has a special significance in mentioned processes. Namely, education needs to be oriented towards *the development of sustainable human capital*, as is expected by European priorities of organizational development for educational sector in Croatia. Therefore, it is of special importance to assert marketing research activities in order that forming performance strategy of educational institutions, defining stakeholders, processes and implementation elements is based on clear priorities and concrete needs of Croatian citizens, economy and other relevant participants. The unreadiness of participants in secondary education process, who are supposed to apply new methods of management and marketing performance, can have harmful effects on the success of previously described processes, monitoring new knowledge and approaches and efficacy in the market of "public" institutions.

On the basis of stated starting points of research, this paper addresses the following goals: (1) the analysis of existing practice of marketing research and its systematic implementation in the formation of marketing strategies of secondary schools in Croatia has been theoretically and empirically established; (2) model formation of systematic application of marketing research in the integral process of secondary school marketing; (3) empirical assessment of the previously mentioned model. Afore-mentioned goals were empirically assessed on the sample of secondary school headmasters in Croatia. Primary data gathering was performed by a method of deep interview with experts and a survey method, which used a specially designed survey questionnaire as an instrument for implementing the empirical part of the research. Secondary school headmasters in the Republic of Croatia were chosen as the examinees. An appropriate sample was used for the research, it included 34 examinees and it was performed on the annual assembly for secondary school headmasters held in Šibenik in March 2008. The instrument of the research included closed and (to a lesser extent) open questions, formed and structured in a manner adapted to be analyzed by a statistical package SPSS. The research started from the following hypotheses: (1) existing practice and marketing research tools in Croatian secondary schools are partial and based on intuitive and ad-hoc approaches; (2) there is a need for clear and systematic implementation of marketing research which has a significant potential for improving the success of strategic and operative performance of secondary schools and its remote units as the determinants of overall potential for achieving marketing efficacy. This paper states the need to adapt and assert marketing in secondary schools by using modern trends where school should be recognized as a place of education and training, but also as an organization which continuously learns and adapts to the demands and needs of its customers.

Marketing is not only advertising and sale as we often perceive it, but it is associated with understanding and satisfying customer needs. The conducted research has shown the existence of the unreadiness of participants in the process of secondary school education to apply new methods of management and marketing performance which can have harmful effects on the efficacy of all described processes, monitoring new knowledge and approaches and efficacy in the “market“ of public institutions. Significant contribution of this work lies in empirical assessment of marketing research model which confirms the stated hypotheses. Marketing research model suitable to conditions in the environment has been formed and optimized for individual implementation in secondary schools in Croatia. This model was empirically evaluated on the sample of all secondary school headmasters in Croatia, therefore confirming the hypotheses on the basis of the research. The results suggest that the existing practice and marketing research tools in Croatian secondary schools are partial and based on intuitive and ad-hoc approaches. The research also provided results which imply that in the field of marketing research in secondary school education there is great space for improvement which should eventually contribute to significant enhancement of capacity and more quality activity of schools. Research results empirically substantiate a great potential for applying marketing research in marketing strategy formation.

In the future, secondary schools will have to use marketing tools increasingly. Every improvement in marketing knowledge and skills of all school employees, including management, teachers and technical staff, represents a prerequisite for it. Therefore, there is great responsibility on decision makers like the Ministry, state agencies and other stakeholders on one hand, and school management and guilds on the other hand. Possible areas for the improvement of marketing activity are relations to internal and external public, which include different information activities, improving communication with students, teachers, employees, decision makers and especially local community. Second possible area of marketing activity is a display of results of external evaluation and school self-evaluation which can represent an excellent basis for creating information and communication activities with the environment. Third important area is the promotion of new and modernized

curricula compatible to the needs and demands of labor market. Promoting new curricula can have a long-term effect on school image which thus can be recognized as a bearer of change and new values required for the development of an individual and society. All this has a purpose of attracting the best students from elementary schools, school positioning and consequently improving the quality of the institution itself, but also contributing to the development of society and local community where the school operates.

Key words

Marketing research, marketing strategy, secondary education, Croatia

Conceptualizing Trade Show Visitors' Purchase Behavior

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Abstract

This research paper examines the factors that contribute to visitors' purchase behavior when attending trade shows. Trade shows have become an increasingly attractive channel for practitioners to meet potential buyers. However, few studies have conceptualized non-industrial buyers' purchase behavior during these events. After reviewing both consumer and tourism literature, this study proposes a model to examine trade show visitors' buying behavior. To examine this model, 738 tourism trade show visitors are recruited. The results show that variety-seeking intention and economic value directly influence visitors' product purchase behavior. In addition, price sensitivity can affect economic value and variety-seeking intention. Nevertheless, contrary to existing literature, service quality (i.e., high and low) will not moderate visitors' buying processes. The implications of this study are discussed within consumer and trade show management literature.

Keywords

Trade shows, purchase behavior, economic value, price sensitivity, service quality

An Algorithm to Match Consumer's Preferences to Product Advertising in Social Media (Facebook) Environment

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Abstract

In global increasing market where competition among firms on consumer's attitude and purchase intention turns to be more difficult, there is a strong demand to understand consumer's product preferences. Moreover, fitting lucrative products to consumers is still considered as a hard task. In order to match the product attributes to consumer's preferences, there is a need for suitable client market segmentation.

Recently, online social networks are considered among marketers as a very popular and efficient marketing tool, especially where young people are chosen as the target audience. This new environment is ideal for EC (electronic commerce), and for implementation of various marketing tools. Among the many social networks, ''Facebook.com" (or in short "Facebook"), is ranked as the biggest, widest and the most active and efficient one. This is the reason why this social media has become a popular marketing platform for advertisers. Nevertheless, Facebook limits marketers to a very narrow group of consumer's attributes (such as the demographic one), thus the target audience is mainly considered as "general" and specific segmented groups which may be exposed to a "tailored" advertising campaign is quire rare.

This phenomenon leads to the situation, where Facebook users are exposed to non effective advertising campaigns which are not always relevant to their preferences towards the product. This study presents how to deal with this problem by using "Facebook" as a social marketing network in a more effective way. The study exhibits how the social media can be utilized to enlarge the specific targeting group by matching consumer's attributes such as demographic, psycho-graphic and behavioral ones with the product attributes (i.e. the augmented product). Next, it is shown how an identification and utilization of social leaders for each product category increases the consumer's purchase intention and the advertising signal or effect. Exposure of limited set of potential users on the targeted group is carried out over the network with minimum cost.

The study methodology implements as computerized questionnaire that collects demographic, psycho-graphic and behavioral data from users, this data is used to compose a user profile based on the "VALS questionnaire scales". The profile is next used to match consumer's attributes to advertised product where classification and forecasting algorithms are utilized. Results show a significant success in matching the consumer's product preferences to the product attribute compared to existing and

conventional advertising methodologies. Moreover, the study results reveal that efficient usage of social leaders over the media increases consumer's purchase intentions and as such the potential sales rate rises. In conclusion, the study exhibits a new approach to marketing practitioners by using conventional marketing and advertising tools along with data mining and computer algorithms.

Keywords

Product endorsement, product design, data mining algorithms, advertising, social media

1. Introduction

The Global competition in social networks is gaining momentum in the recent years. Hence, identifying consumer's preferences to products especially in such media has turned to be a hard task. One of the challenges in marketing is matching product to the consumer's preferences. To make this adjustment it is necessary to find the right target audience by market segmentation parameters such as demographic parameters, psychographic and behavioral. In the recent years, online social networks (OSN) are gaining popularity among users of the Internet, thanks to the simplicity of managing relationships between communities and network information. This social environment is considered as a fertile ground for electronic trading and various marketing methods.

Since 2009, Facebook, the famous social network contains over 250 million active users, where the average user has approximately 120 members. Nevertheless, Facebook, which is considered as the largest social network and the most active one limits retailers to a limited number of consumer's parameters thus blocking marketers to increase their potential targeted audience and in consequence decrease sales.

This study presents a novel method that enable resellers to better "reach" the target audience by including additional data considering their consumers (demographic, psychographic and behavioral) in addition to product attributes, hence creating an optimal match between the suggested product and the consumer's profile. This method implicates data mining techniques in order to classify consumer's preferences as well as usage of viral marketing as an effective means to convey the message on the social network to the target audience. The paper is organized as follows:

The first chapter presents how marketers create market segments by using the "VALS" model (Appendix 4), in addition the virtual world of social network is presented. Next, a comparison of consumer's data type and consumer's preferences to different types of products (product design) is presented. In addition some popular methods for internet advertising in social networks based on recommender systems are presented.

The Second chapter presents the methodology where consumer's data collection was conducted. In addition questionnaires design and methodology of collecting and processing consumer's data is described.

The third chapter presents the results obtained by using various prediction algorithms to match product's preferences to consumer's profile in social networks, based on classification techniques (K-Means and EM).

The fourth chapter presents the discussion and the conclusions; finally the last chapter presents the managerial implications of this study as well as summarizes the constraints and limitations of the study and suggests some future study directions.

Consumer Behavior

Analysis of consumer purchasing decisions are not uncommon Engel et al. (1968); Howard and Sheth (1969); Nicosia (1966) being among the seminal works in the area), and a body of knowledge has developed. Many factors such as social and cultural allow to segment consumers into homogenous groups with common denominator according to their preferences regarded different products.

Many studies support the opinion that there is a difference in the culture of internet consumption due to the variance in consumer's profile. This attitude is articulated in the following way:

Consumers rarely weight up all the costs and benefits of choices. Instead, purchasing decisions may be made automatically, habitually, or be heavily influenced by an individual's emotions or the behavior of others. This also means that consumers tend not to use all of the information available to them when shopping. Instead, people are more likely to read information when they perceive a benefit from doing so. In addition, Consumers use mental short-cuts to help speed up decision-making. These short-cuts can distort consumer's decisions. Short-cuts can include relying on labels or brand names that are recognized, and being influenced by the way in which information is presented and the context in which a decision is made. Moreover, consumers respond more to losses than gains. This means people are more reluctant to give something up or suffer loss than they are motivated by benefits of equal value. This aversion to loss has a significant impact on the way in which people interpret information and can lead to consumers avoiding making choices altogether. Consumers value products much more once they own them; this value can vary over time, and can be affected by the previous cost of the product and the emotional attachment someone places on a product. This makes people reluctant to trade in old products, even when it would be cost-effective to replace them. Finally, consumers are heavily influenced by other people. This might take the form of an indirect influence, for example from seeing neighbors or friends buying a product, or a more direct, explicit influence, for example when a salesperson persuades someone to buy a certain product. Nearly all consumption choices are subject to some kind of social influence. In other words, consumers use products to make a statement about themselves to the environment, products meet far more than just a functional need; they make a statement about a person's identity and about the type of person they are and would like to be. One of the most important lessons from marketing is that people buy products for very different reasons; while some people may be motivated by concern for the environment, many others will not.

Consumers Behavior in social networks

Social media platforms have completely changed the nature of the interaction between brands and their customers, directly impacting upon the contemporary consumer decision process. Today, we can divide social media into 6 groups: social networks (Facebook and LinkedIn are the best examples), blogs, wikis (Wikipedia, the best-known), podcasts (iTunes), forums, content communities (YouTube or Flickr) and microblogging (Twitter).

For the brands, social media appears as a way to reach new customers and to reflect their feelings (Appendix 1-3). This explains why companies are currently working on "Social Strategies" to define the degree of interactivity that they want to have with their customers. Social media will help the consumer to make a decision. They'll often consult public opinion to reinforce their purchasing decision. Thanks to technologies such as smart phones or tablets, customers do not need their home computers, accessing social media everywhere. With such easy access to content, it's clear why print medias are currently facing an important crisis that is mirrored by the decline of the music industry caused largely by piracy but also by social digital channels. Companies can then adapt themselves to these new technologies and benefit from social media. But the relation between the marketers and the consumers has now changed.

The use of social media in recent years has increased rapidly especially by teenagers and middle aged users to communicate with each other and spend leisure time. This current trend and change makes people spend more time for simultaneous communication with friends, establish friendships and spend a lot of time with computer. As a result, the rapid rise of the usage of social media tools affects. Consumer behaviors inevitably since there is seen consumption related interactions in these platforms.

Consumption related behaviors in social media can be taken place; before consumption to decrease perceived risks and simplify purchasing or after consumption to share satisfaction/dissatisfaction from products with friends or companies.

It is possible to classify the consumption related behaviors in social media as; influencing consumers especially when viral marketing strategy is conducted (Pedro, 2005), this strategy which is based on "Consumer's word of mouth" has become a fertile ground for study among marketing experts in the arena of social media.

Common Advertising techniques in social networks

As consumer use of and time spent on social media sites increases, the opportunities for effective advertising become more attractive to companies in search of customers to connect with. Hence, with the grow of social network, a company should participate and engage with communities of interest. This leads to complex decisions: How to use an effective advertising within relevant social channels to create awareness, keep a brand top of mind or to suggest timely and relevant offers. For marketing practitioners, effective advertising on social media sites, has recently turned to be one of the most important study arenas.

Recommender systems as marketing decision support tools

The goal of recommender systems is to generate meaningful recommendations to a collection of users for items or products that might interest them. Suggestions for books on "Amazon", or movies on "Netflix", are real-world examples of the operation of industry strength recommender systems. Recommendation engines depend on the domain and the particular characteristics of the data available. For example, movie watchers on Netflix frequently provide ratings on a scale of 1 (disliked) to 5 (liked). Such a data source records the quality of interactions between users and items. Additionally, the system may have access to user-specific and item-specific profile attributes such as demographics and product descriptions, respectively.

Recommender systems differ in the way they analyze such data sources to develop notions of affinity between users and items, which can be used to identify well-matched pairs Collaborative Filtering systems analyze historical interactions alone, while Content-based Filtering systems are based on profile attributes as well.

Optimal Product Design

The typical approach to the problem of product design is that each product has a number of attributes and each attribute has a number of levels. The larger the number of attributes and levels of the product, the higher the level of difficulty in designing it since the number of combinations that are required to satisfy the demands of the consumers increases (Alexouda 2003; Balakrishnan and Jacob 1995; 1996). Based on consumer utility data, as the designers of the product, the marketing people have to find the most suitable combination of the levels of the product and its attributes so that it can succeed in a competitive environment that offers additional product combinations. Several heuristic methods have been suggested in recent years to overcome this problem, among them the genetic algorithms method.

In this study, comparative analysis of different methods for product design was done in order to find an optimal solution for matching consumer's profile to different product attributes.

2. Methodology

The approach of this study is composed of three stages.

Stage I:
A preliminary study was conducted among 102 "Facebook" users in the age of 20-30 (undergraduate students) to identify their belonging to specific segment according to the famous "VALS" questionnaire.

Stage II:
A computerized questionnaire was used to assess the importance of the characteristics several products to which a different level of involvement was attributed (Zaichowsky, 1985). The questionnaire used adaptive conjoint analysis as in Dahan and Hauser (2000) (ref: figure 2). The implementation of the adaptive conjoint analysis was conducted as follows. At the outset each participant was asked to grade the products being examined in descending order of importance for eight of nine possible attributes that were presented in the list they were given. Each participant was then asked to grade the minimal level of product attributes chosen by him in the previous stage. In the third stage, the participant was presented with a series of possible pairs of products and asked to grade the product that he preferred in each series. Finally, the part-worth values were extracted and the utility allotted to each level of the attribute was assessed.

Stage III:
In order to find the optimal matching between consumer profile and the presented product with the help of several learning algorithm, two groups of data for optimization were used: A Training Set and a Test Set. These two groups of data were examined by means of machine learning with four types of algorithms: Conjunctive Rule, Decision Table, Naïve Bayes, Bayes Net and DTNB. The following products were tested: Computer laptop, Sport shoe, Perfume, Car, Beer and Soap. In addition each participant in the study was identified as a social leader according to Dooren et al (2006).

Figure 1: Adaptive conjoint analysis application

3. Results

Stage I

Figure 2 represents the distribution of 8 segments of consumers as a product of the "VALS" questionnaire analysis. 42% of the participants in the study were identified as strivers. People that like trends and fun, intend to buy in an impulsive manner and in the beginning of their career development. The other dominant segments are: Innovators and experiences (16%) and achievers (10%). Table 1 represents the common interest of different types of areas by the study participants. It is seen that the most prevalent reason to use "Facebook" is: common interest.

Figure 2: Distribution of participants according to primary "VALS" value

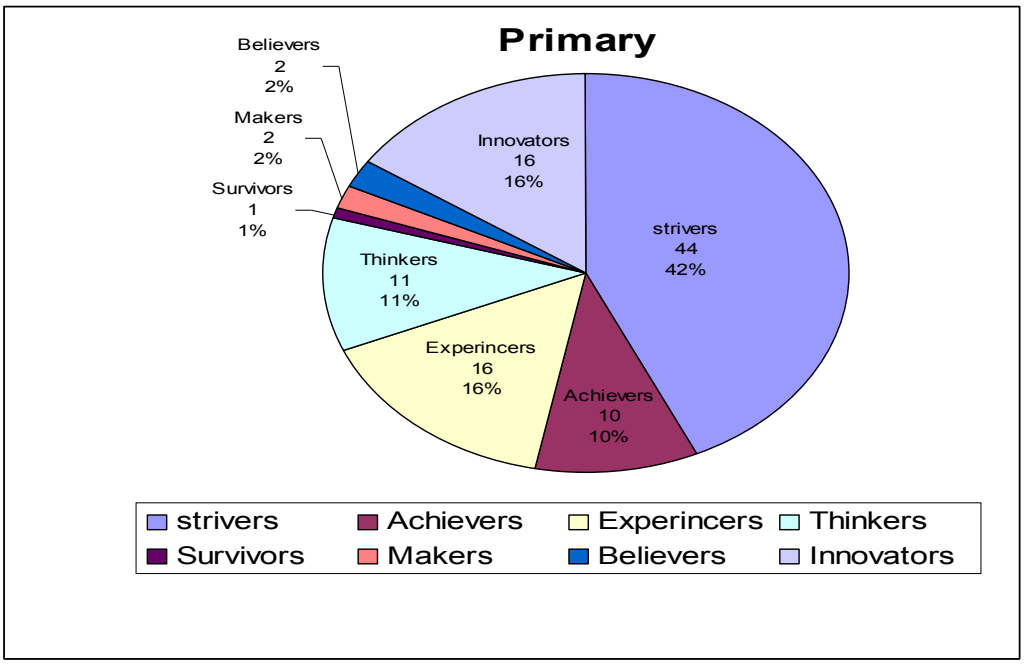

Table 1: Cumulative interests in social networks by respondents

Group Type Name	Third Most Popular Group Type	Second Most Popular Group Type	Most Popular Group Type
unknown	**50**	**48**	48
Common Interest	**4**	**11**	30
Just for Fun	**12**	**13**	8
Student Groups	**5**	**8**	7
Entertainment & Arts	**8**	**6**	6
Internet & Technology	**4**	**0**	1
Music	**3**	**2**	1
Organizations	**12**	**13**	1
Geography	**1**	**1**	**0**
Sports & Recreation	**2**	**0**	**0**
Business	**1**	**0**	**0**

Stage II and Stage III

Table 2 represents the matching success to 6 products where two clustering models were used: K-Means and EM (after analysis of part-worth utility values from each product) during the learning phase. The following data was found after analysis: The EM algorithm in conjunction with Naïve bayes was found as ideal for profile segmentation to the Laptop, The EM algorithm in conjunction with Bayes Net was found as ideal for profile segmentation to the Shoe product, The EM algorithm in conjunction with Naïve bayes was found as ideal for profile segmentation to the Perfume product, The K-Means algorithm in conjunction with Bayes net was found as ideal for profile segmentation to the Car product, The K-Means algorithm in conjunction with Bayes Net was found as ideal for profile segmentation to the Beer product, The K-Menas algorithm in conjunction with Bayes Net was found as ideal for profile segmentation to the soap product. Finally the accuracy of several prediction methods to match optimal consumer profile to products has found that K-Means algorithm with conjunction of Bayes Net or DTNB enables to predict (or match) consumer's profile to product attributes. For the products: Car and Laptop it was found that DTNB is better performed rather than the Bayes Net that is outperformed for the other examined products.

Table 3 presents the main attributes of evaluated products features by consumers that are considered as important. The products are taken by marketers within a "Facebook" home page that includes product advertisements.

Table 2: Segmentation Prediction (in %): Product vs. Classification Method

Product vs. Classification method	Soap	Beer	Car	NaiveBayes **51%**	Shoe	Laptop
EM	BayesNet 25%	NaiveBayes **67%**	NaiveBayes **48%**	DTNB **93%**	NaiveBayes **54%**	NaiveBayes 45%
Kmeans	BayesNet **77%**	BayesNet **64%**	BayesNet 74%		BayesNet 64%	DTNB **80%**

Table 3: Main attributes of product with a different involvement level

Attributes of Product to be Promoted	**Computer**	**Sports Shoe**	**Perfume**	**Automobile**	**Soap**	**Beer**
1	Weight	Comfort	Fragrance	Safety	Scent	Taste
2	Screen Size	Weight	Price	Reliability	Price	Price
3	Price	Price	Form	Price	Moisture	% Alcohol
4	Processor	Design	Bottle Design	Design	Composition	Clarity

4. Discussion and Conclusions

The results of this study show a connection between psycho-graphic attributes and product preferences. The study found that there are fewer attributes related to consumer's profile that must be considered as valuable when marketers consider advertising in social networks.

The study shows that for products with high involvement it is suggested to use deterministic algorithms when matching consumer's attributes to product is taken place, in addition for low involvement ones it is suggested to use "non-deterministic" algorithms in order to find the match (the optimal product attributes) that best suited consumer's preferences.

In addition it was found that there is no correlation between the number of product attributes and the prediction algorithm itself, thus it is possible to eliminate or increase the number of product attributes

when it is presented a social media. Moreover, the study strengths the fact that it is possible to predict consumer's preferences to advertised products in social media.

5. Limitations and Future Study

Although a "tailored" application to receive consumer's preferences was used in this study, today "Facebook" does not allow a free access to consumer's data due to security and business reasons. This limitation is definitely one of the biggest obstacles in usage of data from social networks for marketing analysis. In farther study it is suggested to enlarge the prediction methods to more involvement as well as experimental products and to use empirical questionnaires to collect data consumer's data such as attitudes towards advertised products in social networks.

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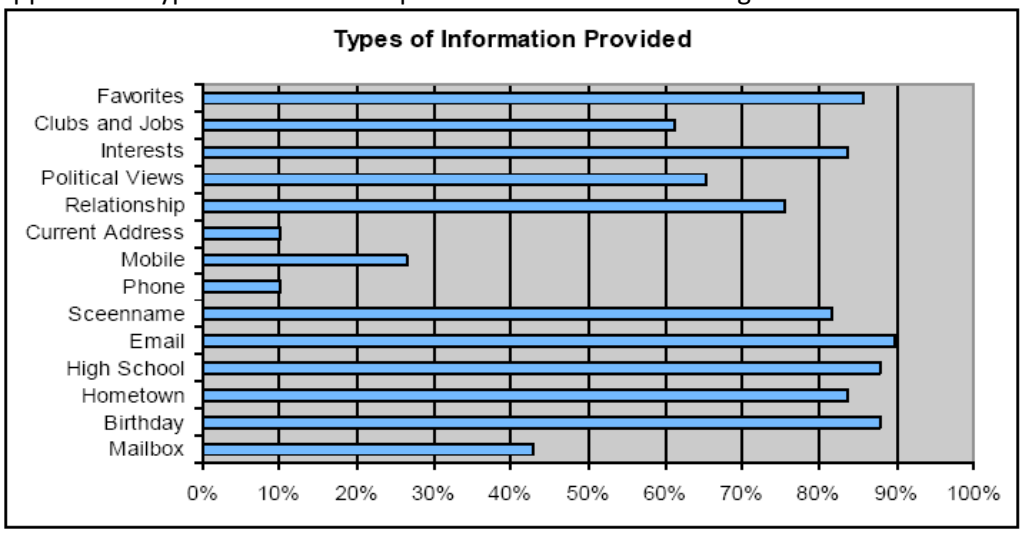
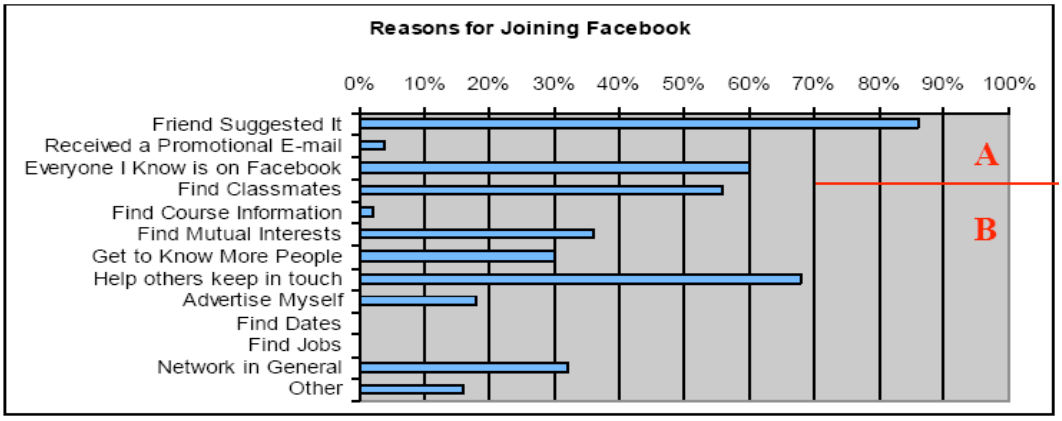
Appendices

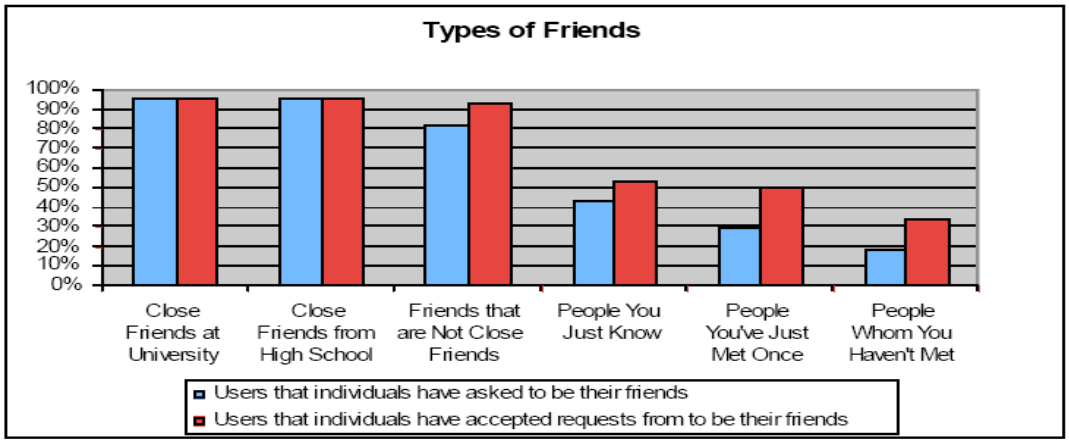
Appendix 1: Types of information provided in social networking



Appendix 2: Reasons of joining the social media – "Facebook"



Appendix 3: Percentage of different types of Facebook users that surveyed participants initiated a friend request and accepted request form.



Appendix 4: The VALS Questionnaire.

VALS™ Survey

Having trouble with the survey? Check out the Survey Help / VALS™ FAQ page!

Have you taken this survey before? ◯ Yes ◯ No

1. I am often interested in theories.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

2. I like outrageous people and things.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

3. I like a lot of variety in my life.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

4. I love to make things I can use everyday.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

5. I follow the latest trends and fashions.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

6. Just as the Bible says, the world literally was created in six days.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

7. I like being in charge of a group.
◯ Mostly disagree ◯ Somewhat disagree ◯ Somewhat agree ◯ Mostly agree

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