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Tel: +381 11 220 30 61

Fax: +381 11 220 30 47

E-mail: imilutinovic@megatrend.edu.rs

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THE GUEST EDITOR'S WORD

One of the frequently quoted slogans of the European Union is that 'culture is not a luxury; culture means life itself.' In other words, culture is one of the pillars of economic development of the modern world, either because of its social significance and impact (of art), or because of its economic potential (creative industries). Cultural issues are topical worldwide, and in this issue of 'Megatrend Review' the authors of the various scientific fields and different parts of the world think creatively about the problems and paths of the world culture and art.

In a separate part dedicated to a thematic field entitled 'The Economy of Culture and Media', professor Francois Colbert from HEC Montreal, the great guru of marketing and management in culture and art, deals with the crisis of funding art institutions due to the reduced cultural demand, and his colleagues professor Dennis Rich from Chicago, speaks about the Baumol's disease', the crisis as a way of living in the performing arts, first diagnosed by professor William Baumol forty years ago. The guest editor Smiljka Isaković's paper is also dedicated to the crisis and a possible strategy of a future development in culture and art of Serbia. Another 'crisis' paper comes from Bratislava - Maria Tajtakova, Stefan Jacques and Peter Filo describe the reduction of active audience due to recession and lower investment in marketing of cultural organizations. Yun Tai shows through specific data how the nonprofit organizations in American culture fight for audiences, which has been a huge and growing problem in the whole world for decades, while her colleague Marta Bakucz analyzes the political, cultural and economic results of the year of 2010 for the city of Pecs, the European Capital of Culture for that year. Milena Gnjatović and Ana Gnjatović deal with the festivals in Serbia, their economic and crisis restrictions and artistic achievements.

World economic problems have limited many human activities lately, mostly in the field of the so-called unprofitable ones. However we hope that it is exactly thanks to the often neglected art and culture that we shall be able to overcome the social upheaval and, so far, the most profound social changes within which we lose the points of social and psychological support on which the civilization has always rested, and which are caused by the financial crisis at the global level.

Assistant Professor Smiljka Isaković, PhD

SNEŽANA GRK, PHD, PRINCIPAL RESEARCH FELLOW*
Institute of Social Sciences, Belgrade

SERBIA – SO CLOSE, YET SO FAR AWAY FROM EUROPE**

Summary

The future of the West Balkans lies in Europe. The project of the united Europe is a peace project that promises brighter future that must be achieved, since it is, above all, a geographic, historical and political imperative. Yet, the question is when this process will be fulfilled, since the European Union has been debilitated by the enlargement. Serbia, which has taken steps towards joining, is losing its pace due to both internal economic and social difficulties and external as well. If we listen to the speeches of the ruling authorities, we might get the impression that Serbia is just about to join the European Union, yet in fact it is so far away from fulfilling this European dream.

Key words: *strategy, reforms, economic development, macroeconomic trends, integrations, crisis*

JEL classification: F53, O19

1. Introduction

Joining the European Union is the state project, but in Serbia from the beginning it has been marked by economic interests and strategies. Looking at it from this time perspective it seems that all the previous strategies in Serbia were wrong. The current model of economic growth is unsustainable. It is indicated by the macroeconomic parameters that are quite worrying.

Serbian citizens feel most the burden of living, because increases in prices are much bigger than the ones shown by the official statistics. The combination of low income and very high prices, primarily of food, on daily basis degrades the condition of the population in Serbia. Poverty grows, and an increasing number of the unemployed conduces to it as well. Serbian economy is in a very difficult situation.

* E-mail: idnsg@eunet.rs

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Unbearable economic situation in Serbia has compelled Serbian government to design the strategic document of Serbian economic development for a period from 2010 to 2020. This document was designed according to the document adopted by the European Union with the title *New Lisbon*. The document of the European Union consists of the exact guidelines i.e. strategic development directions of the Union in the next ten years.

This paper refers to the strategy *Europe 2020* and the strategy *Serbia 2020*, and also to the reasons why the outlined projections will not be realized in the country. The statistics data used in this paper are the official public statistics data. However, in the case of some macroeconomic parameters the unreliability of the official statistics data shades all the future predictions of economic currents in Serbia.

Using the unreliable data of the public statistics, Serbian officials have spoken in public many times explaining that Serbia went through 2009 and 2010 better than all the countries in the region with the lowest decrease in economic activity. The public was misled to believe that Serbia got out of the crisis. The reality is completely different. It was probably because they wanted to show to Europe and the world the situation in Serbia was much better than the real one.

2. The most important principles of the document *Europe 2020*

The aim of the agenda *Europe 2020* adopted by the European commission (EC)¹ is the economic programme, which primarily refers to improving development and employment of European citizens, it also includes digital economy development, advocating the usage of the fast Internet, or creating better climate for business activities of small and middle companies.

This strategy supervenes *Lisbon agenda*², whose main goal was to make Europe “the most dynamic and competitive economy in the world based on knowledge”. The aims in this document were economic changes, and economy of society, knowledge and the environment were emphasized as the most significant. The aims from *Lisbon agenda* that the European Union promoted have not been mostly achieved.

The new strategy *Europe 2020*, whose maker is the the European Commission, is focused on “the strategy for smart, sustainable and inclusive growth and jobs”. The growth that the EU should aspire to (smart, sustainable and inclusive) is possible to realize only by increasing the level of knowledge, improving education system, promoting lifelong learning, using digital economy, saving resources, modernizing the industry and promoting energetic efficiency. The

¹ The agenda *Europe 2020* adopted during a summit on 11 February 2011, and package of measures officially presented on 3 March 2011

² The document refers to the strategy of economic growth from 2000 to 2010.

strategy encompasses the targets regarding demography, globalization, climate changes and other problems that might cause new crises.

The creation of the new strategy *Europe 2020* was mostly due to the world economic crisis, which in 2009 decreased the gross domestic product (GDP) by four percent, and cut industrial production to the level of the 1990's, and left 23 million people without job, i.e. ten percent of the active demographics. The new strategy should link better the national economies of 27 EU members in order to lessen the differences in development and unemployment and hinder new financial crises. The European Commission emphasizes that national aims should be harmonized with European, thanks to the dialogue with the Commission, while *Europe 2020* has no budget, because the goal is not to “pump money” as they say, but to take advantage of the existing resources.

Let us take a short overview of the main principles of the document *Europe 2020*.

One of the key initiatives is starting “economic governance in Europe”, which assumes the following targets:

- devote more attention to unemployment, primarily to social aspects;
- harmonise economic policies of the Member States;
- initiating fiscal stability program;
- conforming to the provisions of the Stability and Growth Pact and conducting reforms in accordance with them.

Of course, monitoring the implementation of the measures in many domains has not fallen behind. Thus the following principles are mentioned:

- organize numerous summits of the Union devoted to the topic of “economic governance”;
- the highest possible level of devotion of all the Member States;
- reward the governments of the States that fulfill their liabilities.

Some targets regarding control of the States are also outlined, and they are:

- control of the implementation of the fiscal stabilization program in the Member States;
- making suggestions regarding national programs to the Member States;
- sending public warnings to the States that do not fulfill their liabilities.

The targets defined by the European Commission as the “urgent measures” that should be implemented as soon as possible are:

- increase the employment rate of the demographics aged from 20 to 64 from the current 69% to 75 %;
- reduce greenhouse gases that cause greenhouse effect by at least 20% comparing to the level in 1990;
- improve energetic efficiency by 20%;

- reach 20% share of its energy from renewable sources;
- reduce the rate of the Europeans who leave school early from 15% to 10%;
- increase the number of highly-educated Europeans;
- increase the R&D investments to 3% of the EU GDP;
- reduce the number of the Europeans living below national poverty lines by 25%, which would improve living conditions of 20 million people.

3. The most important principles of the document *Serbia 2020*

Competing in creating an economic growth model for the period until 2020, mainly the same economists have created three models (projections). We will concentrate on the document *Serbian Development Strategy until 2020*, which gathered and was promoted by the leading experts and which is created according to the model of the document *Europe 2020*.

The document³ about the development concept, made by the leading experts should be used for, as it is stated, “the bases of all other strategies in the Republic of Serbia, patterned on the EU”. According to the experts in the government, the given concept of development should provide “basic elements for future financial EU support for Serbia”.

In the strategic document *Serbia 2020* the authors of the model point out that Serbian economy has its specificities, but also political and social climate is more specific in Serbia in comparison with the other countries in Europe, thus the targets and plans for their achievement are adjusted to this region, and all this in order to harmonize development of Serbia with the EU development. The following fields stand out as the most important: spatial planning, demographic development, infrastructure, ecology, economic growth, knowledge economy, energetics, social politics, defence, international relations, European integrations.

The document states the preconditions and targets of the development of Serbia till 2020. The preconditions of the development are the reforms of: constitution and laws, justice, public administration and security system, as well as the construction of the infrastructure and defining spatial planning of Serbia. While the targets of the development are:

- *increase of employment* (65% of the population aged from 20 to 64 employed);
- *improvement of human capital* (less than 15% early leave school; less than 25% of the 15 year olds insufficiently functionally literate; 30% of the demographics aged from 30 to 34 with high education);

³ Strategic document *Serbia 2020* (the document has 20 pages), available on 21 December 2010.

- *investing in knowledge and technology* (two percent of the GDP annually – a half from the private sector – in R&D; 6 percent of the GDP in education development);
- *growth based on export and rational use of energy* (60% of the GDP growth from the sector which produces exchangeable goods and services; 30% of total investment share in the GDP; 40% higher energetic efficiency with 20% energy from renewable sources);
- *social inclusion and reduction of poverty* (20% less people at risk of poverty or approximately 250,000).

The strategic document *Serbia 2020* states that the concept of the development of Serbia in the next ten years should include all social and economic aspects, define a clear social policy of the country in the next decade and enable Serbia to become the factor of stability and security in the region.

For the achievement of the set targets it is necessary to change political, legal and economic environment, while the concept of development should be in accordance with the strategy *Europe 2020*.

The creators of the mentioned document give the exact diagnosis of the biggest problems in Serbia, so they say they are: economic crisis, low level of education and investment in human capital, research and technological development, falling behind in the aspect of infrastructure quality; depopulation and demographic state.

The stated reforms are divided into two groups: institutional and those referring to the construction of the infrastructure and defining spatial development of Serbia. The institutional reforms include, among others, abolishment of imperative business tenure and blank resignations, i.e. the change of electoral system, then improving efficiency and responsibility of the executive authorities, creation of modern and efficient justice and legal system.

Decentralization process should, according to this concept, “be based on the traditional economic and geographic wholes and specific characteristics of certain areas in Serbia” and add to more even regional development. The list of the areas that are to be reformed includes the security system in the aspect of fighting organized criminal and corruption.

Everything presented above in the document *Serbia 2020* is well conceived, but a big question is if it is feasible to realize.

4. Insubstantial model of Serbian economic growth

The previous model of Serbian economic growth was wrong. Following that model the country got into an economic and financial crisis much before the world financial crisis began. The world economic crisis additionally revealed

all the weaknesses of the model and confirmed its insustainability. The model of Serbian economic growth was functional thanks to the huge foreign capital inflow. For example, in a period from 2001 to 2008 foreign capital inflow was 128 billion RSD out of which approximately 30 billion was remittances, 26 billion was the country's net debit, 16 billion was foreign direct investments (FDI), four billion was donation, about three billion was income from privatization and 49 billion was export. This foreign capital inflow provided relatively high GDP, growth of feasible salaries and pensions, i.e. living standard, creating an illusion about good life in the country.

When the crisis began in the world, foreign capital inflow into Serbia ceased. The model weaknesses resulted in modest GDP growth, inflation increase, export drop, unemployment and poverty growth, fall in the standard of living. Let us view some of the most important macroeconomic parameters.

The GDP in 2010 was increased by 1.8 %⁴ and it was the result of export. Namely, export growth rate (in millions of euros) in 2010 was 18.8 %⁵ comparing to the previous year. The predicted GDP growth rate of three percent in 2011 is unsustainable due to less export and slower development of the country now. However, it is unsustainable also because of the fact that the value of the nominal GDP in 2009 was smaller than the one calculated in the state budget for 2010 and the budget estimate for 2011. Namely, according to the statistics data, Serbia had bigger fall⁶ of economic activities in the region.

The competitiveness of the economy is low. The industry is hardly functional. The present industry share in the GDP of 17.6% is quite modest. Paradoxically, the industry has been neglected for many years and it is only now, when the country is still in the crisis, reindustrialization has been spoken of as the solution for saving the national economy from chaos. Companies are collapsing. The discouraging data show that about 80,000 companies are in different state of blockade, and there are almost 66,000 companies with blocked bank accounts, which means they are not financially able to do business. Those companies are potential candidates for bankruptcy. Currently, almost 22,000 companies are ready for liquidation. Since the beginning of 2011 till the end of April 2011, about 5,500 companies went bankrupt. The estimate of the public institutions⁷ is there are almost 105,000 people employed in them.

In the last years very low investment inflow into Serbia is recorded. Since the investment inflow was low, loans were more raised. The highest loan expansion

⁴ Source: NBS, available on 23 April 2011.

⁵ Source: Statistical Office of the Republic of Serbia, available on 28 April 2011.

⁶ Romania (minus 7,1); Montenegro (minus 7,0); Hungary (minus 6,3); Serbia (minus 6,2); Croatia (minus 5,8); Bulgaria (minus 5,0); Bosnia and Herzegovina (minus 3,4); Macedonia (minus 0,7), and Albania in 2009 had growth of 2.8 %. (Source: State statistics of the mentioned countries, available on 9 May 2011).

⁷ Source: Solidarity Fund, available on 30 April 2011.

is recorded from 2004 to 2007, when the GDP grew at high rates (on average 5.9%). Since 2008, when raising loans was lower, lower economic development was also recorded. Typically, growth was recorded only in those sectors directly connected with the banking sector.

Today, only speculative capital comes into the country. Healthy investments seldom enter Serbia. In 2010, only 1.1 billion euros of direct foreign investments (or 1.5 billion USD)⁸ entered the country. Investment share in the GDP in 2010 was 21.9 %.⁹ The expectations that this share will be 21.7% in 2011, and in a five-year period from 2012 to 2016 on average 22.5 %¹⁰, suggest that we should not hope for significant investments. In other words, for Serbia with weak economy the most important is to attract investors – which are for Serbia, of course, quite difficult. That requires regulated economic environment. As long as the infrastructure in the country is weak and investors have no confidence to invest because of high risk level – Serbia cannot move forward.

It is hardly possible that the credit rating of the country, currently of BB⁻¹¹, will be improved, which suggests that investment will be lower, and reviving economy will be slow.

5. Inflation, budget deficit and debts – threat for the country

Three specially worrying parameters are: inflation, budget deficit and debts. Serbian National Bank¹² will hardly keep inflation at the target level of 4.5 plus-minus 1.5 percent in 2011. The predictions of MMF were that the inflation in Serbia in 2011 would be 6.0%, and by the end of 2016 every year the inflation would increase at the rate of 4%. Yet, this prediction of MMF is completely unsustainable.

In the whole region Serbia had a record inflation rate in 2010 (10.3%). The inflation continued to grow and already in April 2011 reached 17.7%, while in May it was 13.4 %.¹³

⁸ Source: NBS, 28 April 2010.

⁹ Source: MMF, *World Economic Outlook*, available on 23 April 2011.

¹⁰ The author's calculation based on the data of MMF (Source: MMF, *World Economic Outlook*, available on 23 April 2011).

¹¹ Source: Fitch, available on 7 July 2011.

¹² Aware of the fact that he cannot keep inflation in the planned range, the governor of NBS sent an open letter (12 April 2011) to the premier of Serbian government stating the reasons of the inflation deviations from the target levels. Since August 2010 the Central Banka adopted restrictive measures by successively raising the reference rate from 8 to 12.5% and changing the decisions about compulsory reserves. The executive Board of NBS had a session on 7 June 2011 and decided to reduce the reference interest rate to 11.75%. Future movements of the reference interest rate will depend on realizing risk, especially in the field of fiscal policy.

¹³ Source: NBS, available on 5 July 2011.

Apart from constraining the inflation, Serbian government had a problem in 2011 to retain the budget deficit¹⁴ at the level of 4.1% of the GDP and not causing the budget rebalance. The prediction of the deficit in fiscal rules is unsustainable, since the starting point is the estimated fall of the GDP by 3.1% in 2009. Even with the new corrected data for the GDP, the prediction about the country's development till 2020 is unsustainable.

Anyway the data are catastrophic and a way to cover financial losses in the budget will be sought for. Probably, it will be with new trials to sell the most profitable companies or with new borrowings.

The country should avoid getting into long-term debt¹⁵. Borrowing is not acceptable, but it is the simplest solution for politicians.¹⁶ They do it at the expense of future generations. The countries that borrow are in the power of bankers and international financial institutions.

Serbia has become a highly indebted¹⁷ country and has already entered the world debt crisis. The share of total Serbian external debt in the GDP grows. By the end of 2010 it was 82.5%.¹⁸ The external debt of the public sector and private sector proportionally grow in the GDP. It is interesting that the information of Serbian public debt i.e. its share in the GDP (41.5 %¹⁹) is different from the one published by MMF (44.0 %²⁰). Therefore MMF had to send a warning message that Serbian public debt was reaching 45% of the GDP, and that is the maximum limit defined by the fiscal rules. It stands to reason, if the fiscal rules are not obeyed, Serbia will not be able to pay its external debt, which reached 23 billion euros.²¹

6. Reality of economic living

The process of changes in Serbia lasts for too long and heads in a different direction from the expected one. It most affects people: there is an increasing number of people who do not work, the poor in public kitchens, pensioners. Serbian social picture shows alarming data.

¹⁴ The budget for 2011 plans the income into the State Treasury of 724.4 billion RSD and expenditures of 844.9 billion, thus the deficit would be 120.5 billion RSD (Source: Ministry of Finance of the Republic of Serbia, available on 10 February 2011).

¹⁵ See: S. Grk, "Srbija i Evropska unija – krize posle krize", *Srpska politička misao*, no. 2/2011, Institut za političke studije, Beograd, 2011.

¹⁶ Debt is most likely due to the forthcoming elections.

¹⁷ A highly indebted country is the one with external debt of 80% of its GDP.

¹⁸ Source: NBS, available on 28 April 2011.

¹⁹ Source: Ministry of Finance of the Republic of Serbia, available on 19 January 2011.

²⁰ Source: MMF, available on 16 February 2011.

²¹ Source: NBS, available on 7 July 2011.

The social profile²² of Serbia looks like this: the population is 7,320,807, the number of the employed 1,795,775, employment rate is 36.24 %, average age is 41.24 years, birth rate is – 4.6 %, mortality rate 14.2 %, average gross salary is 47,382 RSD (or average net salary 34,009 RSD, in January 2011).

Since the end of 2008, when the crisis in the country became huge, till the end of 2010, which means - for only two years – in Serbia almost 400,000²³ people lost jobs, of that 200,000 really lost jobs and the other 200,000 refers to those who ceased to work in gray economy.

The transition, unsuccessful privatization and economic crisis have led to the fact that nowadays in Serbia more than 1.3 million people are hardly surviving. The data²⁴ are horrific: more than 700,000 people in Serbia live under the poverty line, 728,653 are unemployed, 373,902 are pensioners whose pensions are under 11,000 RSD, and approximately 353,000 live with less than 8,000 RSD per month, 178,786 people receive social welfare (even 40% of them are in Vojvodina), almost 50,000 people eat in national kitchens, of that 6,000 children.

But, according to other estimates²⁵ the number of the unemployed has reached a million, approximately 650,000 employees receive salary on regular basis, while 130,000 work but do not receive salary, and more than two million citizens are extremely poor – even 80,000 people eat in national kitchens.

It is catastrophic that almost 95,000 of unemployed people are more than 55 year old, and that population stratum can hardly find job, while 21,353 people among them do not have right anymore to receive compensation from the state's employment office. It means they are all potential users of the social welfare. Further fall in the standard of living will make Serbian social map darker. For greater part of the population in the country, hard life will become even harder. In Serbia even in 2016 every fifth citizen will be unemployed. The fact that about 1.8 million of employed people with an average salary that is the lowest on Bal-

²² Source: Statistical Office of the Republic of Serbia, available on 23 April 2011.

²³ Source: Albert Jager, MMF's mission chief (revealed the data in media, available on 16 February 2011). However the data of Statistical Office of the Republic of Serbia are drastically different from the MMF's data. According to the official statistics since the beginning of the global crisis in 2008 till the end of 2010 in Serbia unemployment rose from 14 to 20%, i.e. more than 100,000 people lost jobs. (Source: Statistical Office of the Republic of Serbia, available on 16 February 2011).

²⁴ Source: Ministry of Labour and Social Policy of the Republic of Serbia, available on 23 April 2011. godine.

²⁵ See: S. Grk, "Srbija i Evropska unija – krize posle krize", *Srpska politička misao*, no. 2/2011, Institut za političke studije, Beograd, 2011.

kans, have to support 1.6 million of pensioners, is sufficient to conclude how wrong national policies²⁶ were- demographic²⁷, employment, social.

In order to make sure that this conclusion is correct, it is necessary to analyse average salaries in the region, average pensions and annual purchasing power (all given in euros) and conclude that according to these indicators Serbia is at the bottom line among the other countries in the region. See Table 1.

Table 1: Average salary (net), pensions and purchasing power in January 2011

Countries	Average salary (in euros)	Average pension (in euros)	Purchasing power – annually (in euros)
Slovenia	936	–	–
Croatia	725	298	4,808
Montenegro	460	255	3,206
Bosnia and Herzegovina	400	170	2,435
Bulgaria	335	145	2,618
Macedonia	330	115	2,492
Serbia	320	210	3,033

Source: Agency, GFK, *Danas*, available on 30 April – 3 May 2011.

Notice: Serbian purchasing power is four times smaller than the one of an average EU citizen.

However, an average salary in Serbia in March 2011 was 35,777 RSD²⁸ (almost 355 euros according to the middle rate²⁹) and was less in reality³⁰ than in the previous month, and considerably less than a year ago. Gross salary also fell in practice³¹ (it was 49,633 RSD).

²⁶ Serbian government should be worried about the unsustainable proportion of the number of pensioners and the unemployed on one hand, and the employed on the other hand. In Serbia 1.1 employee goes on 1 pensioner. In Europe three employees go on one pensioner, and the European Commission is quite worried about this proportion.

²⁷ See: S. Grk, “Reforma penzionog sistema u Srbiji – u senci privrednog rasta i nepovoljne demografske strukture”, *Srpska politička misao*, no. 1/2011, Institut za političke studije, Beograd, 2011.

²⁸ Source: Statistical Office of the Republic of Serbia, available on 27 April 2011.

²⁹ The average salary in euros in Serbia rose in March because the exchange rate became weaker, i.e. the domestic currency became stronger. Thus by the end of January 2011, according to the official middle rate of NBS, one euro passed as 105.14 RSD, while by the end of March 2011 one euro passed as 100.5675 RSD.

³⁰ It was really lower by 1.9% than in February 2011, and by 6.4% lower than in March 2010 (Source: Statistical Office of the Republic of Serbia, available on 27 April 2011).

³¹ Comparing to February 2011 for two, and to March 2010 for 6.4% (Source: Statistical Office of the Republic of Serbia, available on 27 April 2011).

For the sake of comparison, using the statistics data of some countries, let us view the course of salaries in the surrounding countries. In February 2011, an average net salary in Croatia was 5,242 kunas (about 718 euros), and minimal salary was 2,814 kunas. One euro passes as about 7.3 kunas. An average net salary in Slovenia in February was 969.92 euros. An average net salary in Montenegro in February was 506 euros. Macedonian Statistics Institute revealed only in March the data for January 2011. According to them an average net salary in Macedonia in January was 21,029 denars (about 342 euros). One euro in Macedonia passes as 61.5 denars.³² According to the data of the state's statistics, in April 2011 an average salary in Serbia was 394.4 euros³³, which was the result of stronger dinar in that period.

Serbia has another side as well – a bright side. In Serbia the number of the rich grows. According to the data of the Tax Administration³⁴ for 2010, average salaries of the employees in financial intermediation exceeded 1,000 euros, more exactly 103,000 RSD, and that was for almost 69,000 RSD higher than the average salary in Serbia. Some bankers could earn fantastic monthly salaries (almost 15,000 euros), but some professors at faculties did not fall behind either (the biggest salary of 167 million was declared by a professor of economic sciences³⁵). Apart from professors who are richer and richer, the airline employees have also excellent salaries (an average salary in March 2010 was 107,300 RSD): air traffic controllers have from 2,000 to 3,000 euros; pilotes from 3,000 to 3,500 euros; auditors to 2,000 euros; doctors from 700 to 1,800 euros; managers up to 2,000 euros. Also public officials do not fall behind. More than two thousand³⁶ public officials considerably increased their property and income in 2010, comparing to 2009, in spite of the fact that their salaries were frozen in that period.

Comparing the gray picture of Serbian reality with the bright picture, one gets an impression that such a state in Serbia is the result of neglectful demeanor of the political elite, which has not created good social policy in the country on time, nor the strategy of economic development of the country. The political elite allowed, even provided the climate where personal interests (power and wealth) of an individual overwhelm the existential ones.

Certain individuals in the authorities (from the previous regime, but also the current one) are directly responsible for expensive state, red tape, regula-

³² Source: *Danas*, available on 27 April 2011.

³³ Source: Statistical Office of the Republic of Serbia, available on 1 June 2011.

³⁴ The highest income of 167 million RSD was declared by a professor of economic sciences, 140 million by a private entrepreneur, 80 million by a lawyer, 60 million by a banker (Source: Tax Administration, available on 8 May 2011).

³⁵ The author of the paper asks a question: Is it possible to earn enormous amounts in education? What quality of knowledge students get? How can some professors have time to keep up with contemporary literature, prepare lectures and write scientific papers?

³⁶ Source: Anti-Corruption Agency, available on 11 February 2011.

tions, bribe and corruption. Unfortunately, as it has been so far, nobody responsible will be punished.

7. What is more payable for an individual – corruption or education?

Some people, according to the above given data, would answer – corruption. Corruption is the most noticeable in the countries in transition. Serbia is among those countries. The corruption index in Serbia in 2010 was 3.5. With this index Serbia is on the unenviable 78. place on the global corruption list of 178 countries, according to the data of the *Transparency International*. In the region Croatia and Macedonia have quite higher index, but also quite lower corruption, Bulgaria, Romania and Montenegro have somewhat higher, while Albania and B&H are below Serbia. See the Table 2.

Table 2: *Corruption index*

Country	2008	2009	2010
Croatia	4.4	4.1	4.1
Macedonia	3.6	3.8	4.1
Montenegro	3.4	3.9	3.7
Romania	3.8	3.8	3.7
Bulgaria	3.6	3.8	3.6
Serbia	3.4	3.5	3.5
Albania	3.4	3.2	3.3
Bosnia and Herzegovina	3.2	3.0	3.2

Source: *Transparency International, available on 27 March 2011.*

Political parties in Serbia are the main source of corruption. Doubtful ways of financing political parties, secrecy of financing, public procurement, intransparency of spending money of taxpayers, appointing only the party-eligible to public positions, the pressure of the governing structures on the justice, as well as the blockade of the institutions have added to the fact that Serbia has not made progress in fighting corruption for several year in a row. The given corruption index indicates there is a hard systematic problem in Serbia.

Since the corruption is in all pores of social life, the contradictoriness expressed in the fact Serbia has numerous institutions of high-education and graduate schools, but very small percentage of the highly-educated, should not be surprising. 65% of the population has elementary and secondary education,

4% has a certificate from a college, while it is catastrophic that there is only 6 %³⁷ of highly-educated citizens.

Many acquire high education and leave the country because they cannot find jobs, and many who enter graduate schools and do not finish them, manage to find jobs due to good connections. So, formal education is not a guarantee for employment, or good salary. It is at the same time the reason for huge “brain drain” from the country.

Common sense says that some things in Serbia must change. Otherwise, Serbia will never achieve its European dream. The country has to deal seriously with the key factor of unemployment fall and poverty in the state, and that is education. This thesis is present in the EU as well. Therefore, it got a significant place (already mentioned in the paper) in the strategic document *Europe 2020*. Serbia has also highlighted this target as a priority in its strategic document till 2020.

Serbia is the only country in Europe where in the last 15 years the number of the highly-educated has decreased. With 3.8% of the gross domestic product assigned to education, Serbia is among the countries with the lowest investment in education in Europe. Therefore we must permanently work on reducing unemployment and poverty, constant education of individuals or “lifelong education”.

The picture of Serbia in the next 10-15 years mostly depend on the amount of investment in education, science and technology – because they are the main driving force behind economic growth and development of every country. UNESCO recommends public expenditures for education should be 6%, which is a standard for the member states of the OECD. If more funds from the budget are not assigned to education and science, Serbia will have to “import” highly-educated labour in fifteen years, and maybe even sooner.

8. Instead of the conclusion: Serbia is far away from Europe

Serbia is still far away from Europe. It will remain far away as long as the politicians who promote the path to Europe justify their wrong movements as the requirements of the European Commission.

Serbia has to meet all the requirements the European Commission had set to the other EU members before they became the Member States. The most important criteria for joining the EU are: inflation rate below 1.5% of the average one in three EU countries with the lowest retail prices; nominal interest rate on the state’s securities maximum 2% above the average interest rate in three EU most advantageous states; budget deficit below 3% of the GDP; public debt below 60% of the GDP; complying to the exchange rate mechanism (ERM) for at least two years before joining the EU.

³⁷ The data refer to 2007. Updated reliable official data have not been released.

Serbia has to be ready to be completely reformed. The economy, justice, public administration, education, healthcare, pension system are to be reformed.

Primarily, Serbia as a country has to be regulated. Poor Serbia with huge social problems, corrupted parties or blocked justice will not be welcome in the European Union. So, Serbia has to change really and to accept European values.

The best way to eliminate the fear of the Member States, they have because of the wars and war crimes, corruption and criminal, or illegal trafficking – is by finalizing the cooperation with the Hague tribunal, improving the rating on the list monitored by the Transparency International, and constantly informing the public about what Serbia has done in the area of fighting criminal. Apart from that, Serbia will have to minimize the number of people seeking asylum in the EU states. Unless the number of the asylum seekers in the EU falls, the suspension of the visa-free regime will follow, i.e. introducing Schengen visas. The warning of Belgium should be seriously taken, because according to the new data of the European statistical office Eurostat, Serbia is on the third position on the rankings of the asylum applicants in the EU. Afghanistan and Russia are the only above Serbia on the list. The reaction of Europe caused by the fear of asylum seekers inflow is totally understandable, because some of its Member States are still in the crisis, and it is exposed to the migratory wave from the North Africa.

In addition to all the mentioned reasons that make Serbia farther from the EU, there is one more, and it is – not knowing its own borders. Or, maybe Serbia knows its own borders. Looking from the current perspective, one gets an impression that all the events in the last three years have changed the slogan “Europe without borders”. Borders are very important, and the EU has been debilitated by enlargement. Some states think that the EU, after the entrance of Croatia, should not expand on the West Balkans, because the Union is already big.

No matter how much Serbian officials try to adjust the development strategy *Serbia 2020* to the strategy *Europe 2020*, and to bid the date of joining the EU – the reality is completely different. It will take a lot of time, and maybe Europe will change completely by then. It seems as if a new map of the European Union is being drawn.

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PROFESSOR NATAŠA BOGAVAC CVETKOVIĆ, PhD

Graduate School of Business Studies, Megatrend University, Belgrade

PROFESSOR TATJANA DRAGIČEVIĆ RADIČEVIĆ, PhD

Graduate School of Business Economics, Valjevo, Megatrend University, Belgrade

RANKA MITROVIĆ

Graduate School of Business Studies, Megatrend University, Belgrade

ENTREPRENEURIAL ENVIRONMENT – OPPORTUNITIES AND LIMITATIONS

Summary

The aim of the paper, due to the characteristics of domestic entrepreneurial environment, is to stress the importance of small and medium-sized enterprises as the way to overcome the crisis. Unlike developed countries and successful countries in transition, where small family businesses, i.e. small and medium-sized enterprises are the factors of economic and social balance, however, slowness in the implementation of fundamental reform initiatives and growing social tensions have adverse effect on displaying creative business initiatives and sustainable status of SMEs in Serbia.

Key words: *small and medium-sized enterprises, entrepreneurial environment, reforms*

JEL classification: L25, P31

1. Introduction

Following positive and negative experiences of countries in transition, it is possible to conclude that Serbia cannot improve its economy in the long term without thorough restructuring and integration into the global economy. There is a widespread opinion that the successful process of transition cannot be achieved without creating encouraging business environment that should provide the conditions for entrepreneurship, foreign capital inflows and links with international financial institutions.

* E-mail: nacasn@hotmail.com

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Unlike developed countries, and successful countries in transition, where small family businesses, i.e. small and medium-sized employers are the factors of economic and social balance – the lack of political will, slowness in implementing fundamental reform initiatives and growing social tensions have adverse effect on the survival and development of small and medium-sized enterprises (SMEs) in Serbia.

The importance of small enterprises in the social and economic development of any country, regardless of the level of development, can be seen in a number of examples in the recent past. Functioning of the modern world economy is directly dependent on small private enterprises. The importance of small and medium-sized enterprises for the European Union and member states has been increasing all the time, as confirmed by practical policies implemented by the European Commission and member states. The social importance of small and medium-sized enterprises is reflected in the fact that they constitute the backbone of employment, job creation and they are key players in creating and maintaining well-being and regional communities. Thus, the welfare of small and medium-sized enterprises is a key element for the future growth of the EU economy, but also for creating so-called knowledge economy. In Europe, small and medium-sized enterprises account for 99.8% of the total number of companies, employ 67.1% of workers in private sector. Furthermore, in 2011 the European Investment Bank funded small and medium-sized enterprises with approximately 30 billion euros.

Small and medium-sized enterprises played a key role in the economic transition of our country. The consequence of restructuring large, financially ruined economic system was the relocation of labor, capital and other resources in the area of greater efficiency and competitiveness. Small private businesses were key elements in the process of transition and privatization. The importance of this sector is best illustrated by the fact that Serbia has approximately 303,000 businesses and that among them there are about 1,800 medium-sized enterprises and a small number of large systems. Additionally, from the rest of that number more than 95% of all the businesses are micro enterprises (up to 10 employees). This group consists of more than 270,000 private entrepreneurs and microeconomic companies.

The starting point for the development of entrepreneurship in Serbia is somewhat different from other transition economies. A substantial number of small enterprises in Serbia have been operating since the eighties, so they do not represent a novelty in our economy. In recent years the sector of small businesses has showed a lack of business dynamism. In Serbia, according to official data, there is continued stagnation or even reduction in the number of small and medium-sized enterprises. Regarding development of entrepreneurship in the regions in Serbia, there are certain areas with stronger entrepreneurial tradition. High degree of market flexibility and low operating costs are significant fea-

tures for competitive advantage for small businesses. They are often a source of innovation and as such contribute to accelerated economic development. Entrepreneurial initiative, profitability of capital investment, innovation and creativity are the main features of these companies. In order to examine the real relationship between business politics of enterprises and their innovative activities, Republican Bureau of Statistics has conducted a survey on innovative activities of small and medium-sized businesses in the Republic of Serbia for the period 2008-2010¹ based on the sample of 3,982 businesses. An innovative businesses entity is defined as an entity that during this period introduced product or process innovation, innovation in the organization or marketing innovation [19].²

Table 1: *The share of businesses according to the size (based on the number of employees)*

	Total	Innovators	Businesses which have not innovated	The share of innovators (%)
Total	12.141	5.812	6.329	47.9
Small businesses	9.347	4.143	5.204	44.3
Middle-size business	2.237	1.280	957	57.2
Big businesses	557	389	167	69.8
Manufacturing businesses	4.141	2.314	1.827	55.9
Service businesses	8.000	3.498	4.502	43.7

Source: Republican Bureau of Statistics: Announcement IA01, number 347, year LXI, 2011.

The research has shown that the share of businesses with at least one of these types of innovations amounts to approximately 47%. This study provided the data on the activities of businesses regarding the innovation of products/services, innovation processes, innovations in the organization of a business entity and innovation in marketing. The size of business entities is a key factor for their innovative activities. Almost 70% of large businesses are innovative, more than a half of medium businesses and more than a third of small businesses. Innovative activities are more present in manufacturing businesses, where more than half of the businesses introduced innovation, while more than 40% of enterprises introduced innovations in service businesses.

An important factor that makes the situation more complicated concerns the relationship between small enterprises, grey economy and state-owned sector. In such conditions, the activity of many registered and unregistered small businesses naturally gravitate towards grey economy, including the systems for withdrawal and direction of funds and subsidies from the official sector. The

¹ The reference year was 2010.

² http://webrzs.stat.gov.rs/WebSite/repository/documents/00/00/55/83/IA01_2010_srb.pdf

Ministry of Finance of the Republic of Serbia applies a dual strategy. It intends to reduce the size of grey economy and limit subsidies to government and social sector, while at the same time improve conditions for operating legitimate private business enterprises of small and medium sizes.

Small and medium-sized enterprises in Serbia are the most affected by the crisis and are currently in a very difficult position. They cannot adjust well enough to the situation, therefore, the financial crisis which has lasted for several years, has almost used up all of their resources. SMEs need to raise aggressively competitiveness of their products and services to be able to export them, especially if one takes into account the fact that more than 99% of the overall economy of the Republic of Serbia consists of small and medium-sized enterprises. About two-thirds of the total number of employees work in this sector, it is two-thirds of the total turnover in the economy and as such participates in the creation of approximately 60% of gross national product of Serbia. Therefore, SMEs are the generators of development of Serbia. This part of economy has a lot of problems that have not been solved, but accumulated, such as large presence of grey emission and money flow, then insolvency since the obligations of these companies are settled within 120 to 180 days, insufficient purchasing power of consumers, raising of cost inputs, lack of working capital, inappropriate loans, strong competition, high taxes etc. Entrepreneurs have pointed out three most serious problems ranked according to severity with which they are faced when establishing and running their companies. The biggest problems of entrepreneurs are: low purchasing power, lack of working capital and loans and high costs of production materials. A particular problem relates to poor expanding of activities and the inability to purchase new equipment, which is certainly related to the low liquidity and profitability.

2. SMEs in the region and in Serbia

Economic progress and development of the Republic of Serbia needs to develop competitive knowledge-based economies, new technologies and innovation. In achieving this goal, entrepreneurship needs to make important contribution to economic and social development, particularly important for countries in transition, such as the Republic of Serbia.³

In addition, particularly important is the willingness of SMEs to quickly conquer the market of the European Union, adopt the required standards and reduce the difference in the level of development. The exchange of experience in the implemented reforms is an opportunity to improve national and regional competitiveness. According to the new report of the World Bank and IFC, the

³ Vlada RS: *Strategija razvoja konkurentnih i inovativnih malih i srednjih preduzeća za period od 2008. do 2013. godine*, "Službeni glasnik RS", no. 55/05, 71/05 - ispravka, 101/07, 65/08.

reform of business regulation across Southeast Europe has contributed to significant savings to local entrepreneurs. The other document *Doing Business in Southeast Europe 2011*⁴ analyzes the operations in the largest cities in the neighboring countries⁵. The above report shows the benefits and difficulties that arise for the local entrepreneurs in these countries when they start work. *Doing Business* examines business regulations, small and medium local companies in 183 countries around the world, measures and monitors changes in regulations affecting 10 areas of business: setting up business, obtaining building permits, obtaining electricity, registering property, granting of loans, protecting investors, paying taxes, export, contract execution and resolving insolvency.⁶

Southeast European countries have continued to implement reforms of business regulations despite the global financial crisis. The results show that in all 19 towns in the report from 2008 there has been improvement in at least one of the four areas that were analyzed at the time: setting up business, obtaining building permits, property registration and contract execution. Throughout the region, the average cost of establishment decreased from 22 to 13 percent of average income per capita. The average time for obtaining building permits and registration of property has been reduced by more than a month.

In all the towns in where the second measurement was carried out *setting up businesses* was facilitated. The most popular *start-up* reform since 2008 has been the introduction of *one-stop shop* system as it can be seen in 10 towns. For example, in Belgrade (Serbia) registration with various agencies is consolidated. Certificate of business registration, tax identification number (TIN), confirmation from Pension Fund and Health Insurance Fund is obtained by the Serbian Registration Agency (SBRA). Meanwhile, the other cities in Serbia that are included in this report are still working on full implementation of one-stop shop system, i.e. registered in pension and health fund are still performed separately. Nevertheless, the period for setting up businesses in all Serbian cities has been significantly reduced, especially in Zrenjanin, where a period of 37 days from 2008 was shortened to 17 days in 2011.

⁴ The operation report in Southeast Europe in 2011 analyzes business regulative from the point of view of local small and medium-sized enterprises. The report is composed with financial support of Swiss Secretary for Economy (SECO), Austrian Government and American Agency for International Development (USAID); www.doingbusiness.org/SEE

⁵ Ex-countries of SFR Yugoslavia (Bosnia and Herzegovina, the Republic of Serbia, Macedonia, Montenegro), Moldavia and Albania.

⁶ The World Bank: *Doing Business 2012 - Doing Business in a More Transparent World*, Regional Profile: Eastern Europe and Central Asia (ECA), Washington, 2012.

Table 2: *It is easier now to do business in all 19 towns where the measures have been carried out in 2008.*

Town, economy	Setting up business	Obtaining building permit	Property registration	Contract execution
Skopje, Macedonia	√	√	√	√
Banja Luka, Bosnia and Herzegovina	√	√	√	√
Vranje, Serbia	√	√	√	×√
Niksic, Montenegro	√	√		
Podgorica, Montenegro	√	√		
Uzice, Serbia	√	√	√	
Sarajevo, Bosnia and Herzegovina	√	√	√	
Bitola, Macedonia	√		√	√
Vlora, Albania	√		√	√
Mostar, Bosnia and Herzegovina	√	√	√	
Pljevlja, Montenegro	√	√		
Kishinev, Moldavia	√		√	√
Tirana, Albania	√		√	√
Belgrade, Serbia	√	×	√	
Skadar, Albania	√			√
Zrenjanin, Serbia	√		√	
Krusevac, Serbia	√			×

√ Reform Report on business that facilitates
 × Reform Report on business which aggravates
 Note: 19 towns, where the measures were carried out in 2008, were ranked according to the number and impact of the reforms.
 At the top of the list are the towns where most reforms were carried out to facilitate business between January 2008 and January 2011 and which achieved the greatest improvement in ranking regarding four topics in the Report on business in which the measurement was carried out in 2008.

Source: An excerpt from the *Doing Business* database (adapted by the author).

The data in the annual *Report on doing business* show that for the establishment of companies in each country in the region the following things must be

considered: the number of procedures, time, costs and minimum starting capital. Having compared these indicators in the region and with the average of the region useful information can be obtained.⁷ Regarding the obtaining of building permits, 9 towns when compared in 2008 and 2011 benefited from the reforms in inventory digitization and the enforcement of new laws on construction and efficient inspection. In Serbia, the Law on planning and construction in 2009 simplified the procedure for obtaining building permits which can be transmitted to investors during the construction. The effect of the new law varies from city to city. For example, in Vranje building permits be obtained in 6 months, which is 3 months faster than in 2008. On the other hand, in Belgrade, the same process lasts almost for a year, that is, 5 months longer than in 2008. The biggest problem in implementing this law is the application of provisions concerning the conversion of “the right of use” to property rights.

The reforms in the area of property registration have brought significant savings in 12 out of 19 compared cities. The governments in the region have digitized land records and made property registration more efficient through the legal and administrative reforms. As a result, the average time to register property in the cities of South East Europe has been reduced to one month since 2008. Similar efforts were undertaken in Serbia. Along with the digitization of cadastral maps, these reforms have reduced the time to register property in major cities.

According to the indicator *property registration* in the Republic of Serbia 6 different procedures, 11 days and 2.8% of gross domestic product per capita are needed. Economies worldwide have facilitated the registration and transfer of assets to entrepreneurs with certain measures such as the computerization of land registration, the introduction of time limits for procedures and the total time to register property. The significant part of the reforms in this area resulted in the reduction of tax on property transfer from 5% to 2.5%. *The execution of the contract* has become faster, cheaper and/or less complicated in 8 out of 19 cities compared in 2008 and 2011. The courts in these cities have implemented administrative and legal reforms in order to reduce time and costs of resolving commercial disputes. In Vranje (Serbia) manually recorded court records and standard files were replaced by electronic ones which are available online. In addition, a computerized system randomly assigns cases to judges, thus preventing errors, corruption and reduces the duration of court proceedings.⁸

In the past decade small and medium-sized enterprises and entrepreneurs (SMEEs) experienced frequent changes, wandering and even “legal loopholes”. SMEEs play an important role in the economy of the Republic of Serbia. As an illustration of the situation in this area it may be noted that the share of this sec-

⁷ The World Bank: *Doing Business 2012 - Doing Business in a More Transparent World*, Regional Profile: Eastern Europe and Central Asia (ECA), Washington, 2012.

⁸ The World Bank: *Doing Business 2012- Doing Business in a More Transparent World*, Regional Profile: Eastern Europe and Central Asia (ECA), Washington, 2012.

tor in 2010 amounted to 99.8% (318,540 companies) out of 319,044 companies. SMEE sector generates 66.4% of employees (814,585), 65.3% of turnover (4,678 billion RSD) and 55.9% of GVA (817, 4 billion RSD) non-financial sector in 2010. SMEE sector employs 45.4% of the total employment, achieves 44.5% of export, 52.3% of import, generates 63.3% of the foreign trade deficit of Serbian economy and accounts for approximately 33% of GDP of the Republic.⁹

The effects of the economic crisis on the development of SMEEs in 2010 compared to 2009 are:

- the increase in the number of SMEEs (for 3,713) is the result of increasing number of entrepreneurs (for 2,439) and micro enterprises (for 1,746), while the number of small businesses decreased by 259, medium business for 213 - which is an indicator of poor economic power of the sector;
- a continuing trend of net effect (the ratio between the number of established and closed companies and shops) - for 10 closed companies there are 10 new ones (28 in 2009), and for 10 closed shops 9 new ones were set up;
- reduction of the number of employees by 57,955 workers (or 6.6%). It is 71.8% of employment reduction in non-financial sector, therefore, the trend of reduced importance of SMEE sector has continued;
- below-average growth in business activity (0.3% versus 12.2% for large enterprises and 4.1% in non-financial sector) influenced the decline in the gross value added by 1.4% (GVA growth of 12, 2%, 3.6% in large firms in non-financial sector);
- lower productivity growth, measured by GAV per employee, compared with non-financial sector (5.7% versus 7.4%, respectively), despite a higher decrease of employment rate (- 6.6% compared to 6.2%, respectively);
- the most unprofitable part of the economy (profitability rate was 36.1% versus 43.0% in large companies and 39.2% in non-financial sector), despite the fact that compared to 2009 the profit of SMEE sector was higher by 8.6%, and profit rate by 10.1%. The highest profitability rate is in small companies (45.9%);
- unchanged sector concentration of SMEEs – *manufacturing industry, wholesale and retail trade, construction and professional, scientific, innovation and technical activities*;
- unchanged regional disparities. Development level of SMEE sector according to the regions in Serbia, measured by GVA indicator per employee, indicates that compared to the most developed area (Belgrade) and the

⁹ Ministarstvo ekonomije i regionalnog razvoja: *Izveštaj o MSP i preduzetništvu u 2010*, Nacionalna agencija za regionalni razvoj, Beograd, 2011.

least developed SMEE sector (Pcinjska) 2.4: 1 (2.3: 1 in 2009), and profitability of 2.1: 1 in 2010 to 2.9: 1 in 2009.¹⁰

The World Bank survey from *Doing Business 2012*, shows a deterioration in the ease of doing business in Serbian economy and Serbia is on the 92nd position in the ranking of 183 countries. Compared to the countries of the region, Serbia has a better position than Bosnia and Herzegovina (125), and lower than Macedonia (22), Montenegro (56), Romania (72) and Croatia (80).¹¹ For setting up business in the Republic of Serbia it takes 7 different procedures, 13 days and 7.8% of gross domestic product per capita. In order to obtain different types of permits (for construction, electricity, telephone, inspection approval or approvals from the other agencies to establish business, etc...), companies are faced with 19 procedures for which it takes 279 days to fulfill.¹² According to the indicator *granting loans*, the Republic of Serbia is on the 24th position, as the result of the credit reform and the new Law on protection of personal data, borrowers have access to their data. Thereby the access to credit information has been improved with the help of the reform.

The Republic of Serbia is among the countries with a complex system of paying taxes and fees – the number of annual payments is 66 (in Sweden only twice), for the preparation, calculation and payment of taxes and other mandatory charges companies spend even 279 hours.

Small and medium-sized enterprises are also the backbone of employment, job creation and important players in creating and maintaining well-being of the region. Creating of encouraging environment for small and medium-sized enterprises is a key prerequisite for future economic growth. The Republic of Serbia is trying to complete the liberalization process and create macroeconomic stability of the economy to overcome the crisis. Solving the accumulated problems in small and medium-sized enterprises is a prerequisite for future economic recovery.

3. Small and medium-sized enterprises – limiting factors

Political conditions and business environment do not seem supportive to SME development in Serbia. Slowness and the lack of fundamental reform initiatives have caused starting transition difficulties to last long, which adds to long-

¹⁰ Ministarstvo ekonomije i regionalnog razvoja: *Izveštaj o MSP i preduzetništvu u 2010*, Nacionalna agencija za regionalni razvoj, Beograd, 2011.

¹¹ Ministarstvo ekonomije i regionalnog razvoja: *Izveštaj o MSP i preduzetništvu u 2010*, Nacionalna agencija za regionalni razvoj, Beograd, 2011.

¹² The World Bank: *Doing Business 2012 - Doing Business in a More Transparent World*, Regional Profile: Eastern Europe and Central Asia (ECA), Washington, 2012.

lasting negative legacy and makes Serbia even more distant from the world integration processes. The number and status of the active business entities in Serbia confirms the fact (300,000 small and approximately 15,000 large companies with 1,200,000 employees), while this number compared to the demographic capacity in developed countries is twice as large. The same situation is with zero economic efficiency of enterprises in Serbia (where expenditures exceed revenues), unlike the situation in developed countries where profitability is above 10%. The problem of economic efficiency is even more complex, because small businesses comprise 95% of the total number of firms and absorb 54% of employees in Serbia. Due to all these reasons Serbia belong to a small group of the least developed European countries.

The entrepreneurial sector of the economy of the Republic of Serbia is facing a real problem called *grey economy*. More serious development of business environment and the stimulation of employment are not possible without combating grey economy, that is, reducing it to the acceptable level for the European Union. According to the World Bank, at the end of 2008, the rate of grey economy in Serbia's GDP amounted to 33.6%. It has further increased in the period of global economic crisis. Permanent working body which deals with economic issues in 2010 initiated the project "Effective suppression of the grey economy" which was, among other things, based on the data obtained from field research (survey).¹³ Grey economy in the Republic of Serbia includes three issues: economic activities in the black market (illegal business entities), black labor (employees who work illegally), and money laundering and financial fraud (illegal transactions, tax evasion, etc...)¹⁴

Grey economy exists in developed countries as well, but its share in the EU is on average 15% of gross domestic product (GDP). In Serbia, however, the level of grey economy is nearly 165% higher than in the EU and causes minimum annual budget loss of 150 billion dinars (1.5 billion euros). Regarding the rate of grey economy, the Republic of Serbia is not the sole example. However, what makes the situation in Serbia even worse compared to the other countries is the large number and high percentage of the population which is engaged in grey economy from the total working-age population. The results obtained from the project "Effective suppression of grey economy" indicate the following:

- 1) approximately 665,000 working-age population is in some way engaged in grey economy (as an additional source of revenue, or as the sole source of income);

¹³ Association of Independent Unions of Serbia and UGS 'Nezavisnost' for the project: 'Efficient reduction of grey economy' conducted a survey of working-age population (employed and unemployed) on the issue of existence and understanding of grey economy in the Republic of Serbia. The research was conducted during May 2010 on the whole territory of Serbia.

¹⁴ Socijalno-ekonomski savet RS, kancelarija Swiss Labour Assistance (SLA) u Srbiji: *Efikasno suzbijanje sive ekonomije*, NIP "Radnička štampa", Beograd, 2010.

- 2) in Serbia grey sector has annual turnover worth more than 4 billion euros, which amounts to approximately 30% of total annual turnover of goods and services;
- 3) black labor in Serbia is most present in construction, trade, tourism and service industry, handicraft and increasingly in small and medium-sized enterprises. There are many causes of black labor in Serbia, and they should primarily be sought in high unemployment rate, especially the high rate of youth unemployment, low incomes and low living standards; uncompleted tax system and poor fiscal control, mild punishments, i.e. low risk compared to expected earnings, insufficiently constructed market mechanisms, institutions and inefficient public administration, the dominance of politics over economics, and others.¹⁵

The survey confirmed that the trade of goods is in the first place in grey zone. In the second place is the construction industry since there is significant number of fictitious companies with one, two or no employees, with no significant assets and initial capital. Services, dominated by small manufacturing services and so-called services in households, take the third place. The service sector has the largest share in grey economy in the EU countries, because even in developed countries, it is difficult to control the providing of services in the black labor market. In the fourth place is the only branch in which the Republic of Serbia has a surplus in foreign trade with foreign countries - agriculture with forestry and water management. Various estimates indicate that every other small farmer in Serbia is in grey area, which, on the one hand, presents a significant loss for the state, but also prevents individual producers to receive certain subsidies from the state or raise loans for businesses, making them associated in the long term with small estates and small volume of production, thus losing the opportunity for development and raising living standards.

A particular problem that hinders the survival of SMEs in the domestic market are numerous monthly, quarterly and annual obligations of legal business entities towards the Republic of Serbia, local self-governments, courts and other public organizations that have the authority to collect certain fees. Significant burden on legitimate business enterprises and entrepreneurs are 56 different obligations relating to VAT (monthly and quarterly), taxes on incomes, contract jobs, royalties, corporate income taxes, utility taxes for firms, other fees, expenses and commissions at all levels, and so on.

Businesses that operate illegally do not have these 56 obligations. It should be further noted that the total number of obligations is even higher depending on the branch of industry of business enterprises and entrepreneurs. The pre-

¹⁵ Socijalno-ekonomski savet RS, kancelarija Swiss Labour Assistance (SLA) u Srbiji: *Efikasno suzbijanje sive ekonomije*, NIP "Radnička štampa", Beograd, 2010.

sented number of obligations illustrates what benefits grey area has in relation to legal entities.

Since the main intention of domestic economic system is to strengthen a system based on the activity and development of capital market and its instruments, primarily the development of market mechanisms, competition, and development and market monitoring of a wide range of financial instruments, the priority in the process of creating a more favorable economic environment should be to find an appropriate way of financing SMEs.

The big problem for the functioning and development of SMEs is the lack of capital. Different stages in the life cycle of companies require different funding sources. There are too little available funds, both domestic and foreign ones. One way of financing, operating largely in the developed market economies, is the financing through private equity funds. These funds buy shares of companies and thus provide capital to establish new businesses, encourage expansion of family firms and improve the efficiency of companies that have a good product or market, but bad management, and need to be reorganized. The package of shares is usually minority one, but the fund has so-called priority shares in making strategic decisions (purchasing of another company, borrowing or reorganization) and its representatives are in the managing board. Therefore, it is not a classic granting of loans, but investment through recapitalization, purchasing of shares or a combination of these two models, with 25-40% share of the fund, and for a period of 3-7 years. After this period, the fund sells its share to a strategic partner or in the stock market. SEAF (Small Enterprise Assistance Funds – the fund which supports small enterprises) only works in countries in transition, which in the last decade invested \$50 million in 175 companies. The prerequisite for the fund investment is a clear business plan and reliable financial information.

Specialized institutions that deal with raising funds and their long-term investment in the capital market, i.e. “business angels” play a special role in further development of SMEs. In the EU, when it comes to financing SMEs, business angels are in the third place. These are individuals who own capital and can have influence on a company and participate actively in its work. This method of funding has rapidly increased, because support network has been created for business angels, which makes project financing for SMEs easier and with their involvement the credibility of companies raise. Such a network would be necessary to create in Serbia as well. Currently, “business angels” are mainly venture capitalist. In former Soviet Union attractive acquisitions have started to be used in cooperation with insurance companies. In 2007 and 2008 in Serbia they acted as private investment funds through recapitalization of private enterprises which were not at stock exchange.

To sum up, in order to overcome the crisis and encourage future economic growth of Serbia grey economy should be reduced and economic environment for small and medium-sized enterprises encouraged. The main causes of unfa-

avorable results in business are caused primarily by unsupportive economic conditions, i.e. high taxes, difficulties in financing development and legal uncertainty. Furthermore, there is poor financial situation of employers in terms of equipment and working capital, mostly caused to long-term impact of poor economic conditions.

4. The chances of creating conditions to improve entrepreneurial environment

The analysis of the current state of domestic economy indicates that the conditions for the development of entrepreneurship in Serbia are more difficult compared to the same conditions in developed as well as in other countries in transition. In order to overcome the existing limits, it is necessary to adopt measures of economic policies that will improve business conditions and the current economic environment. They should include the following things.

- 1) **Suppressing grey economy**, which is most present in agriculture, commerce, crafts and textile industry and presents inappropriate competition to all other business entities which do business legally. By reducing grey economy some funds would be raised to compensate for the lack in Serbia's budget. There has to be tax reform and reduction of unnecessary obligations in economy.
- 2) **Reforming the tax system** by abandoning linear taxation system, reducing tax rates and tax on income by 50% for low-profit industries in which 'grey economy' was largely present in the first two years, as an incentive for legitimate business and employment; the calculation of VAT on the basis of charged business activity rather than merely regarding invoices, which would reduce illiquidity, borrowing and tax evasions. The obligation to pay VAT before due date forces tens of thousands of Serbian companies to get loans from banks at high interest rates of 6% to 30%. Consequently, the state made companies insolvent and since being insolvent for many months in the situation when the average payment periods were 130 days (in 2010) they went bankrupt.
- 3) **Public sector reform** implies reduction of employees through retraining, the abolition of monopolies, the introduction of professional management, reduction of subsidies, anti-corruption in public procurement, elimination of old regulations and the introduction of electronic administration, defining of local utility taxes based on the development of cities and municipalities, reducing the number of state agencies (currently there are 128 in Serbia and 47 in Croatia) etc. Serbian public sector employs 535,000 people or 30.6% of total employment in Serbia, which is almost three times the average in EU countries. By implementing a long-term

transfer of employees from public sector in real sector, according to the estimates of experts in the European Union, the annual excess in budget of one billion euros would be provided, and the money could be used for credit lines of future development bank of Serbia.

- 4) **Increasing employment** through new forms of incentives for job creation, introduction of entrepreneurship and practical work in elementary and secondary schools, the establishment of Education Centre for state officials in local governments who would participate in projects of the UN, the EU and other funds.

The introduction of the order in payment system - In Serbia, until recently there was no law to limit payment period for debt collection, so in the recently published list by Eurostat, the European institute for studies in economy, Serbia with 128 days, which is the average duration of debt payments, was on the last place in Europe after Albania, Bosnia and Herzegovina and Macedonia. In Serbia, it seems that everyone owes everyone, and the economic crisis has further worsened the situation.¹⁶ Many EU countries, as well as those in the region, have found ways to bring order into the debt payment system, either by making specific legislation to regulate it, or with more efficient work of state institutions, especially commercial courts. However, the Serbian government and financial institutions, apart from subsidized loans, failed to introduce any other measures that would make the biggest debtors pay.

Table 3: *Due dates in Europe*

Germany	18 days
France	24 days
Spain	32 days
Greece	37 days
Bulgaria	44 days
Slovenia	39 days
Croatia	34 days
Macedonia	76 days
BIH	104 days
Albania	127 days
Serbia	128 days

Source: <http://www.market-srbija.com/rubrike-u-asopisu/tema/836-ogranjenje-rokova-plaanja/>, Eurostata data, European institute for studies in economy

¹⁶ <http://www.market-srbija.com/rubrike-u-asopisu/tema/836-ogranjenje-rokova-plaanja/>

The latest legislation on payments limit in the Republic of Serbia sets the maximum of 60 days from the date of issuing of the invoice for delivered goods or performed services. For the purpose of effective implementation of the regulation, it is necessary to introduce harsher penalties following the examples of Slovakia, the Czech Republic and other countries that have successfully solved this problem.

- 1) **Support to export activities** through the establishment of Development Bank, the substitution of imported goods with domestic products, encouragement of the creation of strategic partnerships; limiting market liberalization, development of National export plan, gathering smaller manufacturers and product groups, establishing the Central Registry for the imported goods to control the entry of goods at borders and their distribution to warehouses and retail centers, and prevent the parallel accounting and distribution and the existence of the goods in the streets.
- 2) **Creating encouraging development environment through domestic and foreign investments by:** reduction of political and macroeconomic risks, redefining systems of attracting and incentives for foreign investments, simplifying procedures in obtaining building permits and the abolition of fees for the change of the purpose of land for investors in manufacturing, improving general investment climate, encouraging investment through greenfield investments, building a favorable image of Serbia abroad in order to attract new investments and create better conditions for investment.

By applying these measures economic efficiency of employers in Serbia can be raised through the improvement of general economic conditions, combined with raising the competitiveness of small and medium-sized enterprises sector.

5. Conclusion

Companies of various sizes with their roles and characteristics influence each other in the economy. The economy which has an optimal structure of enterprises of different sizes possesses necessary flexibility and adaptability. Such a situation would be vital in the economy of the Republic of Serbia.

The effects of the global crisis caused the deterioration of the entrepreneurial climate - compared to 2009 small and medium-sized enterprises sector has below-average operating results, the number of newly created enterprises has declined and the number of closed small and medium-sized enterprises has increased. The reduction of the number of employees in 2010 to 57,955 workers (or 6.6%) constituted 71.8% reduction of unemployment in non-financial sector,

so the trend of reducing the importance of small and medium-sized enterprises continued.

Small and medium-sized enterprises have suffered extremely difficult time in the recent years in Serbia, therefore, they have largely transferred to grey economy or simultaneously existed in both legal and grey sector. Small and medium-sized enterprises are burdened with many problems, resulting in unsatisfactory quality of products and services, thereby reducing competitiveness in the domestic and foreign markets. Therefore, it is necessary to create supportive business environment for functioning and development of entrepreneurship.

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PROFESSOR MAJA LEVI JAKŠIĆ, PHD*

Faculty of Organizational Sciences, University of Belgrade

ASSISTANT PROFESSOR MILICA JAKŠIĆ, PHD

Graduate School of Business Studies, Megatrend University, Belgrade

ENTREPRENEURSHIP IN THE KNOWLEDGE BASED ECONOMY – THE CASE OF SERBIA

Summary

Theoretically and in practice it has been discovered that, despite the undoubtedly central role that investments in new knowledge play in development, there is still a neglected, missing link to economic growth, employment opportunities and international competitiveness. The research findings clearly point to knowledge and technology entrepreneurship as the “missing link”. Knowledge based economy and society rely strongly on entrepreneurial competencies to achieve overall economic and social development.

The situation in Serbia is presented as the “Serbian paradox” with indicators of investments into fundamental and applied research rising, but direct practical results missing in terms of technological and economic development expressed by innovations and new employment opportunities. It is argued that entrepreneurship increases the “fertility” of the knowledge base building its capacity to generate new technology, innovation and entrepreneurial ventures substantially contributing to the development of economy and society.

Key words: *knowledge entrepreneurship, productivity paradox, innovation, technology, development*

JEL classification: L26, J24

1. Introduction

Economic growth and development is strongly related to technological change and the character of new technologies is radically changing the focus of key development factors. These turnarounds and new paradigms were first detected as paradoxes.

The productivity paradox was detected early, in the 1950s, discovering a new phenomenon: the investments in physical capital were increasing, but the

* E-mail: majal@fon.bg.ac.rs

productivity indicators decreasing.¹ Research in the problem had shown that growing physical capital was not sufficient enough for economic success and growth. Intangible components have been neglected and a new perspective and paradigm was necessary. The Japanese management approaches that emphasize the “soft” elements had proved effective and were pouring in the 1960s into Europe, especially Sweden and Germany. By the mid-1970s, in the United States emerged the shift of focus towards intangible assets. Knowledge, creativity, ideas and knowledge based capabilities and skills were found to have not been given adequate attention, whereas resulting in productivity slowdown, while the physical capital investments were still growing. The common denominator for success was found to be a shift away from the factor of physical capital towards knowledge capital, which generally consists of science, technology, creativity, ideas. The intangibles were given special attention and the approaches to economic development based on knowledge, innovation and technology pointed clearly to a new era of knowledge and competence based competitiveness. The integrative concept of “technology” emerged, consisting of physical and intangible elements. More specifically, the intangible technology components were emphasized as inevitable in economic and business growth. This opened a new perspective in understanding the forces of competitiveness in the detailed analysis of the factors relevant to technological progress and growth.

The productivity paradox of the sixties has evolved as the Swedish paradox in the last decades of the past century. “As measured by the most common benchmarks of knowledge investments, such as R&D, university research, patents, human capital, education, creativity and culture, Sweden has ranked consistently among world leaders. However, following more than a decade a stagnant growth and rising unemployment, concerned policymakers in Sweden started to worry about what they termed as “the Swedish paradox”.² Detecting of the persistent stagnant economic growth despite high levels of knowledge investments for the European context had been termed the European Paradox.³ The new paradox in the 1990s was based on the findings that knowledge capital was lacking knowledge management and entrepreneurship components and that without them it was obviously not capable of creating competitive strength and growth.

The Swedish paradox is detected in the case of Serbia, presented later in this paper, pointing clearly to entrepreneurship as the necessary competence and capacity leading to: 1. opportunity oriented scientific research generating new knowledge, and 2. sustainable exploitation of knowledge and new technology for practical results.

¹ M. N. Bailey, A. K. Chakrabarti, *Innovation and the Productivity Crisis*, Brookings Institution, Washington, 1988, p. 5.

² Z. J. Acs, D. B. Audretsch, R. J. Strom ed., *Entrepreneurship, Growth, and Public Policy*, Cambridge University Press, Cambridge, 2009, p. 7.

³ *Ibidem*

Literature on entrepreneurship, competence based approaches and competitiveness has been growing in dispersed directions, making it difficult to formulate unequivocal policy recommendations. At the same time, policy fashions rather than empirical evidence or well established theory tend to influence policy makers.⁴

In this paper we adopt a design science method to develop models and principles grounded in the body of research evidence and targeted at giving new insight, informing and providing decision support to strategic management at different levels of the economy.

Specifically, the situation in Serbia is presented as the “Serbian paradox” with indicators of investments into fundamental and applied research rising, but direct practical results missing according to traditional technological and economic development indicators.

2. Entrepreneurship Competencies in the Knowledge based Economy

In the eighteenth century the French term *entrepreneur* was first used to describe a “go-between” or a “between-taker”. The entrepreneur served as the go-between and as the active risk taker.⁵ The roots of the term entrepreneur point to the mediator roles and activities, linking together, bridging, acting in between, all of which are in the modern vocabulary found as cooperative, networking and partnering roles and actions. These roles are fulfilled by specific cooperative competencies which are one of the key entrepreneurship competencies. Entrepreneur is not necessarily an innovator, the one that has developed innovation. Often, these are separate activities that need to be linked to create value, develop quality of life and contribute to sustainable development. Establishing entrepreneurial links means creating collaborative relations between different actors that recognize the opportunity, lead innovation, establish partnership relations to realize the opportunity and commercialize the innovation.

The definitions of entrepreneurship vary in scope, focus, research objectives and domains. Entrepreneurship is described by terms “new, innovative, flexible, dynamic, creative and risk taking”.⁶ Special significance and emphasis is, by some authors, given to the perspective of creating new business organization as the environment for entrepreneurship activities. It means creating a spin-off, or spin-out, which encompasses all the necessary preconditions related to new firm creation. “Entrepreneurship is the creation of an innovative economic orga-

⁴ D. C. Mowery, R. R. Nelson, B. N. Sampat, A. A. Ziedonis, *Ivory Tower and Industrial Innovation: University-Industry Technology Transfer Before and After the Bayh-Dole Act*, Stanford Business Books, Stanford, 2004.

⁵ M. K. Coulter, *Entrepreneurship in Action*, Prentice Hall, London, 2001.

⁶ M. K. Coulter, *Entrepreneurship in Action*, Prentice Hall, London, 2001, p. 3.

nization (or network of organizations) for the purpose of gain or growth under conditions of risk and uncertainty.”⁷

In defining entrepreneurship, the stress is also on creativity centered on four issues: 1. the creation of new ventures and organizations, 2. creation of new combinations of goods and services, methods of production, markets and supply chains; 3. creative recognition of new and existing opportunities; 4. creative (cognitive processes, behavior and modes of action) to exploit new and existing opportunities. The most relevant domains of focus of the entrepreneur are described as the focus on change, focus on opportunity and focus on organization wide management.⁸

The process approach is relevant as “entrepreneurship involves the creation of value, the process of starting or growing a new profit-making business, the process of providing a new product or service, and the intentional creation of value through organization by an individual contributor or small group of partners.”⁹ Entrepreneurship is deeply involved in change, in something being new and different, and hence, the main role of entrepreneurs is being “agents of change”.¹⁰ Entrepreneurship involves specific domains of managing change, technology, innovation, creativity, value, risk, opportunity.

Based on Schumpeter’s definition of the entrepreneur as an innovator who “creatively destructs” and Drucker’s definition of the entrepreneur as “someone who maximizes opportunity”, it is argued that opportunity is at the heart of entrepreneurship, encompassing technology and innovation leadership. In this sense, innovation and opportunity are viewed as the two sides of the same coin.

Entrepreneurship as the link between science and technology and the practical new value created for the customers upgrading their living conditions and standards contributing to the overall welfare of the economy and society is represented by the simplified model below.¹¹

Technical world ↔ Technological entrepreneurship ↔ Commercial world

The productivity paradox of the fifties, Swedish and European paradox by the end of the 20th century, the Serbian paradox in first decade of the 21st century, clearly point to the entrepreneurial link as the missing “glue” that puts together the crucial competitive forces in the economy, sector, region, or the firm, together.

The entrepreneurial link is necessary in putting together the strategic and operational aims and goals, in fulfilling the mission and vision demands with

⁷ M. J. Dollinger, *Entrepreneurship*, Prentice Hall, London, 1999, p. 19.

⁸ Ph. A. Wickham, *Strategic Entrepreneurship*, Prentice Hall, New Jersey, 2004.

⁹ M. K. Coulter, *Entrepreneurship in Action*, Prentice Hall, London, 2001, p. 4.

¹⁰ Ph. A. Wickham, *Strategic Entrepreneurship*, Prentice Hall, New Jersey, 2004.

¹¹ J. E. Etlie, *Managing Technological Innovation*, John Wiley&Sons, New York, 2000, p. 95.

innovative response, in enhancing the efficiency and effectiveness of the virtuous circle “science-technology-business-competitiveness”, in building the efficient knowledge base. Fostering entrepreneurship is understood as a means to release currently unexploited opportunities hidden in individuals, shelved technologies and resource combinations.¹² In order to be successful it is to be innovative, but being innovative does not automatically mean new value for the customer and competitiveness. Entrepreneurship is all about using entrepreneurial opportunities as innovations to the point of their creating new, superior value in the economy and society.

The resource-based theory postulates that sustainable competitive advantage is achieved with resources that are: valuable, because they exploit some environmental opportunity; rare, in the sense that there are not enough for all competitors; hard to copy or imitate, and no substitutable with other resources.¹³

Competence based approach goes further focusing on capabilities and competencies, as specific methods, procedures, skills and knowledge developed to combine and use the valuable, rare, hard to copy, no substitutable resources. Competencies are even more valuable by adding specific potentials and capacities to resources and creating the unique competitive profile. “In a way, competence-based theory offers more hope to the entrepreneur than resource-based theory.”¹⁴

Competence based competitiveness emphasizes the role of technology, knowledge and skills, as well as the resulting synergies, as the crucial strengths. The paradigm of key competencies is explicated as the set of technological and organizational capabilities creating the essence of the sustainable competitive power.¹⁵ Competence-based approach to entrepreneurship, or entrepreneurship competencies at the base of competitiveness, combines the external and internal oriented approaches.

3. Knowledge entrepreneurship and development

The knowledge hierarchy model represents traditional relationship between data that is further processed into information which is further processed to create knowledge. In order to achieve economic development, it is important to go a step further and beyond the basic principle of accumulation of knowledge. The next important step would be the capability to put knowledge into practi-

¹² V. A. Gilsing, A. Elco van Burg, G. L. Romme, “Policy principles for the creation and success of corporate and academic spin-offs”, *Technovation*, Vol. 30, Issue 1, 2010, p. 12.

¹³ M. J. Dollinger, *Entrepreneurship*, Prentice Hall, London, 1999, p. 27.

¹⁴ Ph. A. Wickham, *Strategic Entrepreneurship*, Prentice Hall, New Jersey, 2004, p. 38.

¹⁵ R. Sanchez, Aime Heene, Howard Thomas, *Dynamics of Competence based Competition*, Pergamon Press, London, 1996.

cal use to the benefit of society. This is an important addition to the traditional model and this capability is represented by two levels: knowledge management and knowledge entrepreneurship as presented in Figure 1.

Knowledge management represents specific knowledge on how to plan, organize and efficiently use the knowledge base accumulated in the society, economy, company or individuals to create value.

Knowledge entrepreneurship is an additional demand to dynamise/activate the knowledge base in order that it generates innovation and entrepreneurial ventures. Knowledge entrepreneurship stems from the need to extract the finest juices from knowledge base in the form of new technologies and new enterprises contributing to development and competitiveness of economy and society.¹⁶ Knowledge entrepreneurship activates knowledge in the aim to create new value leading to quality of life improvement in all aspects. Entrepreneurial knowledge management, i.e. knowledge entrepreneurship, is knowledge on how to broaden the knowledge base and put science results and growing knowledge base most efficiently and effectively into practical use.

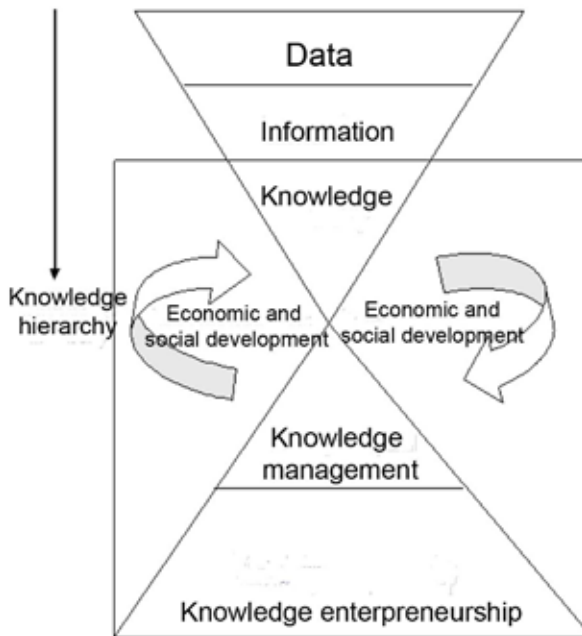
Knowledge entrepreneurship is related to activities at the level of the global international community, national economies, regions, companies and individuals, and more specifically it encompasses:

- developing strong cooperation links, networks, strategic alliances and other forms of bonds and relations, at international and national levels, that synergistically contribute to emergence of new technologies and ventures contributing in a direct way to sustainable business development and growth;
- developing the infrastructure that supports and stimulates innovation and entrepreneurship (creating the effective national innovation system, introducing policy incentives for entrepreneurs, developing education system that stimulates individual creativity, leadership and entrepreneurship, etc.);
- creativity, innovativeness and entrepreneurial culture and climate enhancement in companies with well developed knowledge base;
- motivating individuals to gain further knowledge and qualifications with further developing their capacity to manage their own career oriented at innovation and entrepreneurship.

Knowledge management is represented as an additional level to the three levels present in the traditional model of knowledge hierarchy.¹⁷

¹⁶ M. Levi Jakšić, M. Trifunović, "Leading Innovation based on Knowledge Entrepreneurship", *Proceedings People in Organization, 29th International Conference on Organizational Science Development*, T. Kern, V. Rajković, et al., ed. Univerza v Mariboru, Maribor, 2010, pp. 784-793.

¹⁷ K. A. Pervaiz, D. Ch. Shepherd, *Innovation Management*, Prentice Hall, London, 2010, p. 507.

Figure 1: Knowledge hierarchy and economic and social development

Knowledge entrepreneurship deals with the efficiency and effectiveness of knowledge base dynamics. Knowledge entrepreneurship is oriented at optimizing the sources of knowledge, creating and sustaining the optimal knowledge base and activating all the components of the knowledge base in the effort to create value for the customer. At the company level, it is aimed at providing the right knowledge at the right time in order that the company goals are achieved. The authors present a new model for knowledge hierarchy shown on Figure 1.

Sustainable development principles are the key principles of knowledge entrepreneurship introducing sustainability conditions at the early stages, i.e. idea generation phases, of R&D, all through to the end of technology life cycle.¹⁸

Knowledge management represents a complex game and interweaving of factors such as, human resources, education, training and development, finance and economy, research and development and innovation, information technologies and telecommunication, marketing and brand management.¹⁹

Knowledge entrepreneurship implies strong knowledge base, well developed knowledge management and additional entrepreneurial components to further develop the knowledge base in order to generate more innovation, opportunity and new ventures leading to the economic and social welfare increase which

¹⁸ Levi Jakšić, 2010.

¹⁹ N. Bahra, *Competitive knowledge management*, Palgrave, New York, 2001.

enables more research and development giving rise to new entrepreneurial cycles, often cited as the new waves of development.

Basic tasks of knowledge entrepreneurship are defined in relation to:

- 1) Knowledge filters that are to be inhibited and deactivated. One of the significant roles of knowledge entrepreneurship is to see through the knowledge filter, make it more transparent with a possibility to open the window of opportunity. The knowledge filters are responsible for knowledge based innovations not being generated in a more intensive manner. Knowledge filter is defined as “impeding the spillover of knowledge for commercialization, innovation and ultimately economic growth.”²⁰ The potentials of an idea being developed into innovation and brought to market by entrepreneurial efforts within business in enterprise are assessed and evaluated in different conditions and under different circumstances. The barriers, reluctance to pursue an idea is reported high in incumbent large corporations. The knowledge filters are dense, and many ideas are caught on the filter and detained from developing further. Many examples provide clear evidence on the valuable new ideas being caught in filters, while ultimately they “led to valuable innovations and in some cases triggered entire new industries.”²¹
- 2) Knowledge spillover effects to be actively supported and enhanced. Knowledge entrepreneurship is defined as an effort contributing to the “spillover and commercialization of knowledge and ideas that might otherwise have been abandoned or remained dormant in the corporations and organizations creating those ideas in the first place”. According to the knowledge spillover theory of entrepreneurship, “as the knowledge context increases, entrepreneurship becomes more important because it provides a missing link for economic growth by commercializing investments in knowledge and ideas that might otherwise have remained uncommercialized.”²²
- 3) Knowledge spin-offs to be fully supported by knowledge entrepreneurship as the missing link between scholars and practitioners – scholars to enhance and recognize the practical value of their findings, and policy makers and practitioners to be more informed about these findings. It shortens lead time and gives more quality in products, services and processes.

Knowledge entrepreneurship is viewed as a “conduit” for facilitating the spillover of knowledge required with the entrepreneur who spins-off the knowledge and ideas - takes knowledge that might otherwise have remained uncom-

²⁰ Z. J. Acs, D. B. Audretsch, R. J. Strom ed., *Entrepreneurship, Growth, and Public Policy*, Cambridge University Press, Cambridge, 2009.

²¹ Z. J. Acs, D. B. Audretsch, R. J. Strom ed., op. cit., p. 7.

²² Ibidem

mercialized in the successful high-performing incumbent firm and uses those ideas to launch a new start-up.

Knowledge entrepreneurship is related to the firm that is focused on knowledge as the competitive force, this means that while planning, organizing, motivating, controlling the processes of obtaining, developing and using knowledge in organizations there is a clear strategic vision about the practical values and goals, the pragmatic element of recognizing the significance, relevance of knowledge in creating very concrete results.

“The context of the business model for an innovation is established by the firm’s value proposition, which ultimately drives its business as well as its strategy and technology choice. The value proposition is the business’ *raison d’être* – the justification for committing people and resources to the operations.”²³

Knowledge entrepreneurship is viewed as the integrative process of fostering knowledge in the organization to enable the firm to become champion in all aspects is the missing link within the processes of developing knowledge capacities in:

- generating knowledge – the capacity to create new knowledge results with firm internal capabilities – strategies relying on internal R&D and creativity enhancement within the organization, and
- organizing and implementing knowledge for practical results.

Knowledge entrepreneurship at corporate level is a continuous process and it involves two categories of entrepreneurship: corporate venturing and strategic entrepreneurship. “Corporate venturing refers to a set of entrepreneurial phenomena, through which new businesses are created by, added to, or invested in by an existing corporation....Strategic entrepreneurship refers to a broad array of entrepreneurial phenomena, which may or may not result in new businesses being added to the corporation, in which...innovations are adopted in the firm’s pursuit of competitive advantage.”²⁴

4. The Opportunity, Innovation and Organization Contingencies of Entrepreneurial Processes

The three contingencies of the entrepreneurial process are opportunity, innovation, organization/resources. Entrepreneurial activities in the domain of opportunity identification and exploitation are outward oriented based on the interaction between firms, research institutions, government and other actors that collaborate and drive (contribute to) the innovation process. Entrepreneur-

²³ Westland, J. C.: *Global innovation management*, Palgrave Macmillan, New York, 2008, p. 81.

²⁴ V. K. Narayanan, G. Colarelli O’Connor, *Encyclopedia of Technology and Innovation Management*, John Wiley and Sons, New York, 2010, p. 212.

ial action is based on linkages between these various actors that are essential for turning knowledge into competitive economic advantage.

The successful entrepreneurial venture is usually based on a significant innovation. This might be technological innovation, market innovation, the way something is marketed or distributed, or possibly the way organization is structured or managed, or the way relationships are maintained between organizations.²⁵ Innovation lies at the heart of the entrepreneurial process and is a means to the exploitation of opportunity.

The relation between opportunity and new technology is twofold:

- 1) Opportunity is the input for the R&D process initiative, innovation cycle to begin – opportunity as the starting point for ideas on new technology / innovation;
- 2) New technology/Innovation is the identified opportunity when technological innovation equals opportunity.

In order to bring innovation to the market the activities of number of actors is to be coordinated. This is the function of organization that is created by deciding on different forms depending on a number of factors such as size, rate of growth, industry they operate in, types of products or service they deliver, age of the organization, culture it adopts.

Entrepreneurship as a process is viewed by the crucial activities/operations involved. The entrepreneurial process is the creation of new value through the entrepreneur identifying new opportunities, attracting the resources needed to pursue those opportunities and building and organization to manage those resources.²⁶

The entrepreneurship process is viewed as the following five steps model.

- 1) Identify opportunities. Opportunities are to be found in the space left by others in a market that is still open for new business. “An opportunity is the gap left in a market by those who currently serve it. It represents the potential to serve customers better than they are being served at present. The entrepreneur is responsible for scanning the business landscape for unexploited opportunities or possibilities that something important might be done both differently from the way it is done at the moment and critically better than it is done at the moment. The improved way of doing it is the innovation that entrepreneur presents to the market.”²⁷
- 2) Lead Technology/Innovation. Technology/innovation leadership is broader than innovation management. It involves all the aspects of managing the innovation processes, and also adds a new dimension of technology and innovation entrepreneurship. Technology and innovation

²⁵ Ph. A. Wickham, *Strategic Entrepreneurship*, Prentice Hall, New Jersey, 2004, p. 366.

²⁶ Ph. A. Wickham, op. cit., p. 141.

²⁷ Ph. A. Wickham, op. cit., p. 134.

leadership is focused on the future, business opportunity oriented and concerned with establishing direction, “developing a vision that describes a future state along with a strategy for getting there.”²⁸ While sound innovation management is basically concerned with planning and budgeting innovative action, leading technology and innovation means more - it is concerned also with forecasting future needs and technological trends, looking for opportunities, introducing changes – “often to a dramatic degree”.²⁹

Technology and innovation leadership is based on management and entrepreneurial activities leading to sustainable business development. Based on complexity, dependency and contingency theories, much effort is made to identify and select priorities by relevance criteria attributed to factors influencing the concrete business and the specific situation of different firms.³⁰

- 3) IPR Management Intellectual property rights management deals with planning, coordinating, and control of the innovation process activities, encompassing the application for patent or any other form of protected property rights that are generated from the innovative efforts of the academic sources - universities, public research organizations or companies and the overall technology transfer activities.
- 4) Create new venture (incumbent/new entrant). It means to decide the best form for the business based on technological opportunity and to build new venture capacities to exploit opportunities provided by technological innovation. It is the entrepreneurial operation of creating a new company in the case when the existing company is not the optimal solution for the new venture to develop. It is usually necessary to create new company when dealing with radical new technologies. The two main tracks in relation to new technological opportunities is spin-off firm or licensing to established firm. The spin-off is viewed as corporate or spin-offs from university and public research organizations.
- 5) Operating/sustaining/growing the business. This is an essential task of entrepreneurship. It means managing the business efficiently and effectively within the business life-cycle. It means developing sustainable effective strategies in relation to market, finance, technology, human resources and other key resources. It also means a responsibility to develop the key competencies in the selected business technology area.

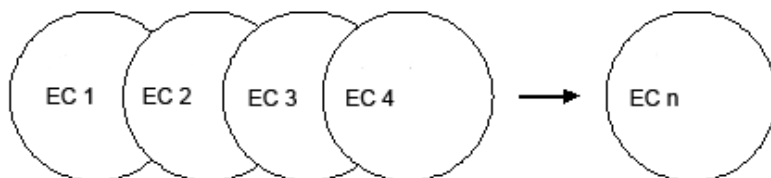
²⁸ B. Burnes, *Managing Change*, Prentice Hall, London, 2009, p. 499.

²⁹ Ibid.

³⁰ D. L. Rainey, *Sustainable Business Development*, Cambridge University Press, Cambridge, 2006, p. 387.

Identifying opportunities is the continuous activity prevailing throughout the entrepreneurship cycle and in a dynamic environment the entrepreneurship process enables the business to survive, change and grow by constant search for opportunities, whereby the entrepreneurial cycle is continued in the future. The continuous growth is represented in Figure 2 as entrepreneurial cycles (EC) succession in the future.

Figure 2: *Successive entrepreneurial cycles - ECs*



5. Innovation indicators - the case of Serbia

Evidence from the case of Serbia clearly points to the very explicit roles of entrepreneurship that are missing in a country where resources are invested in scientific research but not effectuated in the economy and society. The indicators presented below show that although the investments in public R&D have been rising in Serbia, practical results are poor. The links between research phases and concrete development is lacking, innovation lacks entrepreneurship.

In more detail it is shown that there is very low correspondence between fundamental, applied research and patent activity.

5.1. Budgetary funds for science in Serbia and comparative analysis

The European Council has in March 2000 given directive that in Europe the expenditures for R&D are to be increased from 1.9% to the level of 3% of GDP until 2010. Two years later, in Barcelona, an Action plan was adopted related to the increase of funds for R&D.

In Serbia, after a difficult period in the nineties, budgetary expenditure for science increased in gross amounts, from 28 million euro in 2001, to about 100 million euro in 2008. (Table 1)

Table 1: Budgetary R&D expenditures in million euro

Year	2001	2002	2003	2004	2005	2006	2007	2008	2009
R&D expenditure (million euro)	27.9	42.8	60.5	56.9	55.5	68.5	86.3	100	86.2
R&D expenditure in percent of GDP	0.22	0.26	0.35	0.30	0.27	0.29	0.30	0.29	0.28

Source: Budgetary legal act of Republic of Serbia

For international comparisons, budgetary R&D expenditures as percent of GDP in international perspective are presented in Table 2.

Table 2: Expenditures for science in 2007, % of GDP in different countries

Country	Expenditure for science (% of GDP)
Sweden	3.8
Finland	3.5
Japan	3.3
USA	2.6
Germany	2.4
France	2.2
Great Britain	1.7
China	1.4
Spain	1.1
Hungary	0.9
Turkey	0.7
Poland	0.6
Greece	0.5
Serbia	0.3

Distribution of the budget for science and development in Serbia is shown in the next Table 3.

Table 3: *Distribution of the budget for science in Serbia by sectors in 2009*

Sectors of Science (according Serbian government official classification)	Distribution of budget between science by sectors – percent of total budget for science in 2009
1. Fundamental research	50.2%
2. Technological development	39.2%
3. Development of scientific researchers	5.2%
4. International development	5.4%
5. Nuclear and radiation safety	0.4%

Source: MNTR, Serbia

In the document presented in 2010 by the Ministry of science and technological development of the Republic of Serbia, “Strategy of Scientific and Technological Development of the Republic of Serbia”, it is cited that one of the most serious problems of science in Serbia is the fact that a small amount of funds, from mainly one source, invested in scientific research are distributed over more than 1000 projects that were financed by the Ministry in 2009, i.e. 501 projects of fundamental research for which 50,2% of the budget was allocated (see Table 3) and 471 technology development and 129 innovation projects for which 39,2% of the Ministry funds were invested.

5.2. Patent activity in Serbia

According to their main definition and goal, the projects of technological development as result are expected to generate applied technological solutions, patents, pilot plants, new sort innovations, technological advancements and results with direct applicability. In the past period, 2003-2007, in the technological development field, over 3400 technical solutions have been realized. But, in spite of the high number of technical solutions, the number of patent applications from research and development institutions in the period of 2003-2009 has been extremely low, only 54. With these results Serbia has the lowest position in Europe.

The situation seems even worse when it comes to registered patents from public R&D organizations with total of 18 for the period 2003-2008. The structure of patent applications in Serbia is presented in Table 4.

Patents, as indicators of entrepreneurship, show “low patent fertility” of fundamental research institutions, research and development organizations, where most funds are allocated. Companies are in a slightly better position, while the fact that most applications for patents originate from individuals calls for new measures and considerations. One stream of measures are to be expected from the level of the government and ministries that need to develop consistent policy shifting the focus from fund allocating and planning activities to more feedback

and control over the results, as well as to the encouragement of entrepreneurship oriented R&D and new ventures. The entrepreneurship missing link is seen as the new focus that is to overcome the wide gap between scientific research potentials and their practical realization for the benefit of the economy and society.

Table 4: *Structure of patent applications from domestic sources in Serbia*

Source → Year ↓	Institutes and faculties	Companies	Individuals
2003	10	24	346
2004	4	26	466
2005	3	18	351
2006	13	29	390
2007	2	19	376
2008	4	15	370
2009	18	24	198
TOTAL	54	155	2.497

Source: Agency for intellectual property protection of the Republic of Serbia

The Serbian paradox is the situation where the state investments research projects of public research organizations are rising, but the most patent applications come from individuals.

The entrepreneurial roles have been found to be missing at all the levels – at the level of the state that does not provide entrepreneurial guidance and support all through the project phases and is not giving attention to developing national innovation systems as the necessary infrastructure, at the level of R&D institutions lacking entrepreneurial orientation and actions, as well as companies lacking entrepreneurial and innovation leadership in searching for new opportunities and strengthening cooperative, networking entrepreneurial competencies and strengths.

6. New innovation and entrepreneurship model

The case of Serbia generally points to the lack of entrepreneurial links within the scientific research sphere as well as in the relations between R&D and practical developments. The indicators presented for Serbia clearly point to a paradox: investments in fundamental research as percent of total R&D expenditure have had the highest degree - over 50% - in the previous periods, while at the same time patents registered by individuals also had the highest degree. The patent indicators by origin clearly point to the situation where investments in pro-

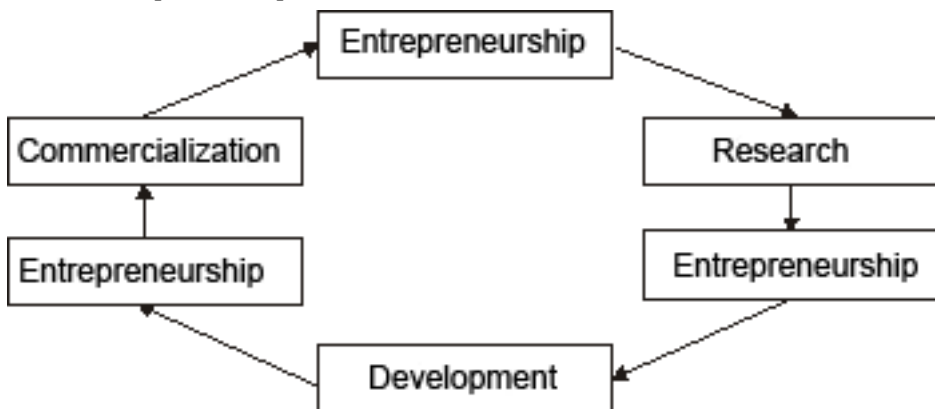
grammed R&D activities have not been “productive” in generating innovation as the key force for entrepreneurship activity. It is concluded that the academia and institutes involved in fundamental research are not bringing new ideas for patenting. So, state policy in funding fundamental research is lacking results in practical, economic breakthroughs and results.

In this paper the theoretical base is developed by viewing technology entrepreneurship through the analysis of entrepreneurial processes and related competencies within the framework of competence-based theory of sustainable competitiveness. Following on Schumpeters approach to entrepreneurship based on technology and innovation, the approach in this paper views entrepreneurial competencies as broader concept that encompasses innovative competencies.

Technological entrepreneurship competencies comprise the development of entrepreneurial climate, capacities to recognize and identify opportunities, lead/manage technology and innovation, create/establish new ventures, lead/manage business for long-term success in the business EoL (End of Life) perspective.

The main findings of the research represented and argued in this paper are that developing knowledge base is not sufficient if entrepreneurial management is lacking. It is argued that knowledge entrepreneurship is the new knowledge level to be introduced in the international/global context, at the level of the national economies, regions, companies. There is a need to develop entrepreneurial competencies in organizations of different types, size, age scope, industry. Knowledge and technology entrepreneurship encompasses innovative processes meaning that the R&D and all other innovative activities are embedded in an overall entrepreneurial network enabling the necessary links and oriented at science results finding their way to practical implementation. Technology entrepreneurship focuses technology and innovation as opportunities in the modern economy giving rise to new entrepreneurial cycles and is a way of surcompassing the current economy crisis.

Figure 2: *Entrepreneurship links within the RDC chain – the new EREDEC chain*



Entrepreneurship is usually viewed as the missing link between innovation and commercialization, while the invention/innovation phases are left out of entrepreneurial consideration. The inclusion of innovation phases within the entrepreneurship model results in the authors presenting a new model where the links between the phases of Research, Development, Commercialization (RDC) are strongly bounded by entrepreneurial cohesion (see Figure 2).

7. Concluding remarks

The main findings of the research represented and argued in this paper are as follows:

- 1) Entrepreneurship competencies represent a unique set of competencies within the knowledge base of the economy creating competitive advantage;
- 2) The entrepreneurship competence approach views entrepreneurial competencies as complex and broad encompassing opportunity, innovation and organization. Entrepreneurial competencies are needed at every level of the economy to be recognized, focused and developed.
- 3) The opportunity domain is at the heart of entrepreneurship and is represented by the competencies that enable opportunity identification that implies opportunity recognition, creation, assessment, selection and realization. Opportunity takes the priority over innovation.
- 4) The case of Serbia generally points to the lack of entrepreneurial links within the scientific research sphere as well as in the relations between R&D and practical developments. The indicators presented for Serbia clearly point to a paradox: investments in fundamental research as percent of total R&D expenditure have had the highest degree - over 50% - in the previous periods, while at the same time patents registered by individuals had had the highest degree. It is concluded that the academia and institutes involved in fundamental research are not bringing new ideas for patenting. So, state policy in funding fundamental research is lacking results in practical, economic breakthroughs and results.
- 5) Knowledge/technology entrepreneurship encompasses innovative processes meaning that the R&D and all other innovative activities are embedded in an overall entrepreneurial network enabling the necessary links and oriented at science results finding their way to practical implementation.
- 6) Entrepreneurship focuses technology and innovation as opportunities in the modern economy giving rise to new entrepreneurial cycles and is a way of surmounting the current economy crisis. Opportunity and new technology are identical in the special case of technology entrepreneurship.

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KATARINA RADOSAVLJEVIĆ, PHD STUDENT*
High School of Business Economics and Entrepreneurship, Belgrade

PERSONAL CONSUMPTION EXPENDITURE IN THE REPUBLIC OF SERBIA FROM 2003 TO 2011

Summary

The two main features of personal consumption expenditure are its share in gross domestic product and the structure of consumption of population by purpose. This paper thoroughly analyses these indicators in the Republic of Serbia in the period from 2003 to 2011. The aim of the paper is to provide an insight into recent events with regard to personal consumption expenditure and compare the standard of living of Serbian citizens with that of the citizens of the neighboring countries. This will give a clear picture of the current position of Serbia.

Key words: *personal consumption expenditure, standard of living, consumption categories, The Republic of Serbia*

JEL classification: E21, P46

1. Introduction

Quantitatively, personal consumption expenditure is the most important component of aggregate demand. Its share in gross domestic product of each country is more than 50%. Absorbing the largest portion of current production, personal consumption expenditure affects structural changes in economy, production, economic growth and development in the long run and tells a lot about quality and standard of living.

Personal consumption expenditure can serve as a comprehensive measure that gives an overall overview of recent events. Although it is not obvious at first sight, when “scratched” a bit deeper, it can be seen that any decision made by government, monetary authorities affect population, i.e. their purchasing power. From that point of view, survey on personal consumption expenditure can be very interesting. The paper mostly deals with trends in personal consumption in Serbia in the 2003–2011 periods. As this is a relatively short period, long-term

* E-mail: radosavljevic.k@gmail.com

trends cannot be defined. The aim is to provide an insight into the previous period. Having in mind that there were numerous factors affecting consumption decisions, only certain events that substantially affected the changes in consumption trends will be presented in the paper. One of the major events that marked this period was the outbreak of economic crisis, which is why we see 2008 as crucial, and we analyze the consequences of the crisis through personal consumption and how citizens and economy reacted to it. The crisis has certainly affected people in various ways (employment, salaries, price rise), it was reflected on product demand, but what we want to point out in this paper is that personal consumption figures were not satisfactory before the crisis.

The paper pays most attention to the following characteristics of personal consumption expenditure:

- share of the total personal consumption expenditure in GDP and
- structure of consumption expenditure by consumption categories.¹

According to this criterion, the paper is divided into two sections. The first one provides information on development of economy, while the second one deals with standard of living. International comparisons in the paper were made with neighboring countries, having in mind similar values of GDP per capita. Although GDP of Serbia is not even close to that of EU member states, these figures are given with the aim to gain a better insight into Serbian economy and an ideal figure Serbia could strive to.

Personal household consumption (PHC) includes expenses of residential households for providing goods and services for satisfying personal needs and wishes, without expenses for capital goods (buying or selling apartments). PHC together with social transfers in subsistence of the state sector (STPC²) and the sector for Non-profit institutions that provide help to households (NPIH) make up real personal consumption (RPC). RPC and collective consumption of the State³ sector make up the final consumption. The structure of data on PHC used in the paper is based on the domestic concept, i.e. items including consumption of residents abroad and non-residents in the country have been left out. The paper will deal with real personal consumption expenditure (RPC) and personal household consumption (PHC). Depending on how a problem needs to be seen, one or another category is used in the paper. In international comparisons made by Eurostat, real personal consumption expenditure is taken into account, and not personal consumption of

¹ Starting from 2003, Statistical Office of the Republic of Serbia publishes data according to Eurostat's Tabular Approach. The classification of personal consumption by purpose has been made according to COICOP (Classification of Individual Consumption by Purpose) and it contains 12 basic categories of consumption that will be covered in the paper.

² STPC refers to the fields of education, health and social insurance and to a lesser extent cultural and sports needs.

³ Collective consumption refers to expenditure for security and defence, maintenance of peace and stability, adoption and enforcement of laws, state administration, etc.

households, as it includes all the goods and services that households used, whether they were paid by the household itself, a state or non-profit institution.

2. Share of personal consumption expenditure in GDP

A large number of authors who studied personal consumption expenditure found the following trends of this index:

- countries with little economic activity and dominant primary sector have a low level of GDP per capita, with a higher relative share of personal consumption expenditure in GDP;
- when a country increases the level of economic activity, the share of personal consumption expenditure in GDP decreases as well as tendency to spend, while its value per capita increases;
- share of personal consumption expenditure remains on the level of approximately 60% of GDP when a country is highly economically developed, while the value of personal consumption per capita significantly increases.

First of all, Serbian GDP needs to be analyzed. The following table shows comparison with neighboring countries with regard to average GDP per capita of the EU countries in the five-year period. We have chosen these countries primarily because their GDP per capita is similar to that of Serbia and because these countries were in the transition period. Serbia is still going through the transition period.

Table 1: Comparison of GDP per capita with the average in the EU countries (GDP in EU-27 = 100⁴), %

COUNTRY/YEAR	2005	2006	2007	2008	2009	2010
European Union (27 countries)	100	100	100	100	100	100
Bulgaria	37	38	40	44	44	44
Hungary	63	63	62	64	65	65
Romania	35	38	42	47	47	46
Slovenia	87	88	88	91	87	85
Montenegro	31	36	40	43	41	41
Croatia	57	58	61	64	64	61
Macedonia	29	30	31	34	36	36
Albania	22	23	23	26	28	28
Bosnia and Herzegovina	25	27	28	30	31	31
Serbia	32	32	33	36	36	35

Source: Eurostat, figures published 12/1/2012.

⁴ Eurostat provides figures in PPS (Purchasing Power Standard) eliminating the differences in the price level in the countries where comparisons are made.

The position of Serbia is not an envious one, as only Albania and Bosnia and Herzegovina are behind it. The situation in Montenegro, Macedonia and Romania is slightly better, while Hungary and Croatia have significantly higher figures. Slovenia definitely sticks out as it is the closest to the EU average. This country is a remarkable example as it fought transition and managed to keep the production on a good level (the level enviable for Serbia, of course). This provides us with sufficient initial information and further analysis will be focused on the share of personal consumption expenditure in GDP.

The following table shows the percentage of share of total real consumption in GDP, in Serbia and the comparison with other neighboring countries. The countries have been sorted according to the ascending share of personal consumption expenditure in 2010, which clearly shows the rank of Serbia. Our country was in penultimate position in this research.

Table 2: Share of real personal consumption expenditure in GDP, comparison with countries in the region (BDP EU-27 = 100), %

COUNTRY/YEAR	2005	2006	2007	2008	2009	2010
Hungary	67.6	66.3	66.6	65.9	66.7	64.4
Croatia	70	68	68.2	68	66.8	67
Slovenia	65.6	63.9	62.8	63.8	67.9	68.4
Bulgaria	77.6	75.8	76.6	74	70.6	69.1
Romania	78.5	77.9	75.3	74	71.9	71.7
European Union (27 countries)	71	70.4	69.6	70.1	72	71.9
Albania	82.7	81.6	84.8	83.9	83.7	80.5
Macedonia	85.2	86.1	83.7	87.4	84.5	82.5
Bosnia and Herzegovina	100.8	95.3	91.1	90.2	87.9	88.8
Serbia	88.7	88.9	89.1	90.1	93.3	92.4
Montenegro	77.9	87.3	97.3	100.7	93.9	92.9

Source: Eurostat, figures published 12/1/2012.

The first thing that draws attention is extremely high share of RPC in domestic product with a permanent growth tendency. In 2009 the percentage was the highest and it amounted 93.3%. This fact is worrying, as it means that other components of gross domestic product – investments, state consumption and net export are very low. Lack of investing activity certainly jeopardizes economy growth and unfavorable effects of weak international trade are well known. The table shows a major change of RPC share in gross domestic product in Serbia after 2008. In the first seven months of 2009, the amount of investments

decreased by more than 20%, while foreign direct investment, shown in American dollars, in the first 7 months, in comparison with the same period in 2008, decreased by as much as 45 %.⁵ It can be the principal reason for growth of share of real personal consumption expenditure in 2009, by 3.2 per cent points. With weak investments, Serbia suffered a serious blow after 2008.

The following tables point out GDP growth rates (table 1.3) and growth rates of real personal consumption expenditure as well as personal consumption of households (table 1.4)

Table 3: GDP growth rates

Year	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Value, constant prices (fixed base 2002) in mill. RSD										
GDP	935552.0	972579.7	996935.5	1094616.1	1160106.5	1215443.0	1290515.8	1351125.0	1311975.4	/
Rates of real growth, fixed base 2002 (previous year=100), %										
GDP	/	4.0	2.5	9.8	6.0	4.8	6.2	4.7	-2.9	1.5

Source: Statistical Office of the Republic of Serbia

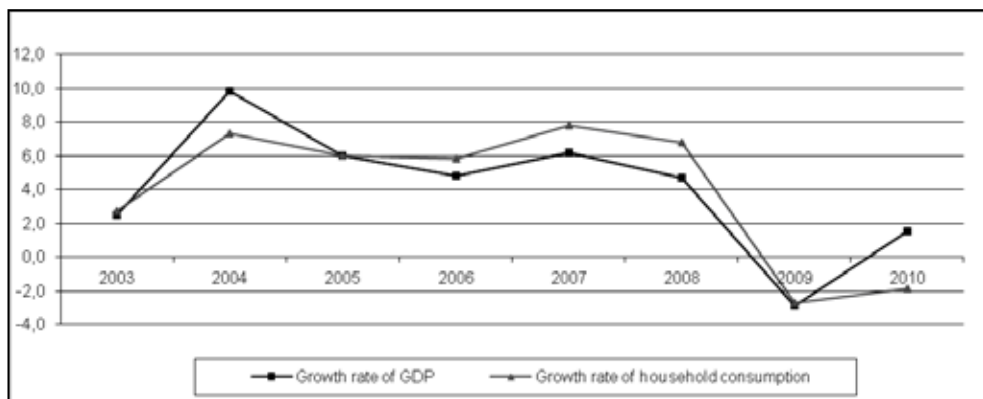
Table 4: Growth rates of RPC and PHC

Real personal consumption and household personal consumption, (previous year = 100), %								
	2003	2004	2005	2006	2007	2008	2009	2010
Real personal consumption	1.9	7.5	5.6	4.9	7.0	5.9	-2.5	/
Household personal consumption	2.7	7.3	6.0	5.8	7.8	6.8	-2.7	-1.9
Social transfers in subsistence of NPID sector	-6.2	23.6	-4.1	8.5	16.6	-2.3	-11.9	/
Social transfers in subsistence of state sector	-3.0	7.6	3.9	-1.8	0.4	1.2	0.6	/

Source: Statistical Office of the Republic of Serbia

Real personal consumption expenditure and personal consumption expenditure have very similar trends; although social transfers affect RPC, these amounts are not large, compared with values of RPC and PC. Whichever type of consumption is analyzed, an abrupt change after 2008 is obvious, which is shown below (graph 1). All these facts imply that household sector, although having weak purchasing power was additionally hit by the crisis.

⁵ M. Kovačević, "Uzroci duboke ekonomske krize u Srbiji", *Škola biznisa*, no. 3/2010.



Graph 1: *GDP and household consumption expenditure trends*

Gross domestic product and household personal consumption, as its largest part, shows the same trends, but the curve of the one is always below the other, meaning that in the years when GDP grew rapidly, household personal consumption expenditure grew more slowly and vice versa. This supports the above-mentioned regularities of these trends, and implies that personal consumption expenditure reacts relatively quickly. A higher growth of GDP means lower growth of personal consumption expenditure, which is in accordance with theoretical assumptions from the beginning of this section. Serbia, of course, cannot boast rapid and high growth of GDP and the surveyed period is not long enough to determine the general trend. Here we want to point out that, if there came about a higher rise in GDP, improvement would be felt relatively quickly. The decisions on changes of fiscal and monetary policy, as well as significant world trends are very shortly reflected on consumption decisions.

3. The structure of personal consumption expenditure in the 2003–2011 period

Theoretic bases necessary to explain this section are well known Engel's laws. Engel found that changes of structure of household consumption depend on changes in personal income. He was the first to notice that, as household income decreases, the percentage of income spent on food increases. The importance of Engel's law is that it represents one of the first functional relations that have been quantified in economics. As income increases, the total expenditure will increase as well, but in different proportions. Spending on food, beverages and basics, i.e. their percentage in the total expenditure will decrease, while the percentage of other categories of consumption will increase, meaning that a certain proportion of income will be available for satisfying the higher needs.

The following overview can be used as a basis for monitoring the percentage share of different consumption categories in Serbia. This table shows that most of the household income is spent on satisfying basic needs, while the coverage of other needs was on a relatively low level.

Table 5: Personal consumption expenditure by purpose in 2003–2011 period⁶

		Household consumption, structure (%)							
Year		2003	2004	2005	2006	2007	2008	2009	2010
0000	Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
0100	Food and soft drinks	31.87	29.43	28.31	27.54	25.95	26.63	26.72	26.56
0200	Alcoholic drinks, tobacco and drugs	6.21	5.85	5.10	5.17	5.07	4.83	5.49	5.37
0300	Clothing and footwear	5.05	4.65	4.65	4.78	5.06	4.96	4.51	4.04
0400	Housing, water, electricity, gas and other fuels	24.19	24.69	24.05	23.19	22.33	21.45	22.94	23.79
0500	Household equipment and maintenance	4.32	4.47	5.10	4.86	5.50	5.60	4.46	4.22
0600	Healthcare	2.66	2.95	3.55	4.05	4.77	4.79	5.06	5.08
0700	Transportation	10.22	11.94	12.25	12.65	12.29	13.05	13.29	13.48
0800	Communication	3.66	3.74	3.91	4.00	4.93	4.64	4.67	4.67
0900	Recreation and culture	3.19	3.82	4.34	4.90	5.49	5.83	5.54	5.16
1000	Education	1.31	1.40	1.48	1.38	1.33	1.23	1.23	1.25
1100	Restaurants and hotels	3.33	3.06	2.94	2.88	2.84	2.54	2.35	2.41
1200	Other personal possessions and other services	4.37	4.43	4.75	5.02	4.98	5.07	4.63	4.74

Source: Statistical Office of the Republic of Serbia

A large share of the ‘food and soft drinks’ category is typical for countries with low income per capita. Besides nutrition, a large portion of income is used for housing (category 04). Another category that a large portion of income is spent on is “transportation”. This category has a tendency of permanent growth in personal consumption expenditure. These are the basic needs that consumers tend to satisfy. These three categories accounted for 64% of total personal household consumption expenditure in 2010.

In order to get an even clearer picture of unfavorable situation in Serbia, we can compare available household income with spending on basic needs. An average monthly income per household in 2010 amounted 47,376 RSD, out of

⁶ The report was based on the Survey on household consumption expenditure where the data on average month expenditure per household were presented.

which 42,418 RSD was spent on personal consumption.⁷ 28,073 RSD (per household per month) was spent on the above-mentioned three categories in 2010, which accounts for about 60 % of monthly income (per household). If we add spending on alcoholic drinks, tobacco and healthcare to this (these categories are also basic needs), the amount reaches 31,713 RSD, i.e. 67% of monthly income is spent on basic needs. Another interesting thing is that oscillations of share in personal consumption of other categories are irrelevant, i.e. their share did not change significantly during the surveyed period. These are the categories from 02 – “alcoholic drinks and drugs”, to category 05 – “household equipment and maintenance”. There are no major changes in spending on education either. During the whole period, item 11 – “restaurants and hotels” had a small share, with the tendency of further drop. On the other hand, there is a significant change in the share of categories 06 – “healthcare”, 07 – “transportation”, 08 – “communication”, 09 – “recreation and culture” during the 2003-2010 period. The share of these categories grew at the expense of the category 01 – “food and drinks”. Does this mean that the standard of living increased? Unfortunately, no! In order to confirm this, price movements and salary rise in this period need to be analyzed. However, the results are not encouraging. The 2003-2011 period has seen a significant rise in prices of housing, utilities and transportation, which is primarily the result of the constant rise in the price of oil and derivatives. We will point out price rise by these categories and some of the events from this period that substantially affected changes in prices.

According to the Quarterly Monitor’s report, based on the retail price index⁸, the price of services increased by 11.1% in 2003 compared to the previous year, which is the highest price rise. This is followed by the rise of industrial non-food products (7.8%), industrial food products with 6%, while the price of agricultural products dropped by 6.4 %.

The situation in 2004 was similar, with the highest rise in price of services (16.1% compared with the previous year), industrial products had the growth rate of 13.5 %, while the prices of goods (12.8% rise) and agricultural products (8.1% rise) marked a significant rise, compared to 2003.

In 2005 the prices of services rose (15.3% rise) more quickly than the prices of goods (10.7%). A high rise in prices of services can be explained by the high rise in prices of transportation and utility services, which depend on oil prices. In 2005 oil price skyrocketed dramatically on the world market, and the price of oil at the end of the year was 87% higher than in December 2004. However, the price of energy in Serbia did not follow this trend and it rose by only 17.4%

⁷ Source: Survey on household consumption expenditure in 2010, taken from the web site of Statistical Office of the Republic of Serbia: www.stat.gov.rs

⁸ Since 2009 Statistical Office of the Republic of Serbia monitored the general rise of prices by the retail price index; after 2009 the methodology was complied with the world standards and since then the retail price index according to COICOP categorization is monitored.

during that period; this discrepancy is a result of administrative price control. Although the country intervened, this was still a major change that resulted in the rise of housing and utility prices by 45% in 2005, compared with the same period of the previous year. At the beginning of 2002, prices that are under the administrative control, especially utilities were significantly below the level. Since then, most of them rose more quickly than the inflation.⁹ This means that, besides the oil price, an important factor of the price of these services is the general price trend.

Prices of energy rose again in 2006, but by the end of the year inflation growth slowed, both because of dinar appreciation and limitation of the growth of prices which are under direct administrative control. Another favourable event was a drop of oil price on the world market at the end of the year, by approximately 20 % after the shock in 2005. This year was characterized by the highest drop in cost of living index by as much as 4 per cent, compared with 2005. However, this state was not realistic. Prices of petrol and electricity remained on the same level (for political reasons), which decreased energy efficiency of economy and jeopardized its competitiveness.¹⁰

2007 was marked by the rise in prices of food and oil, while the inflation reached 10.1% at the end of the year. This was the result of the huge rise in prices of food, agricultural products and tobacco. This increase was a result of the global trend that year, unfavorable weather conditions and a high concentration of ownership in retail and production of food.

After 2007¹¹, Statistical Office of the Republic of Serbia regularly publishes changes of prices by certain categories, so these changes can be seen more clearly. 2006 was taken as a base year, which gives a better insight into the price rise of certain items.

⁹ *Kvartalni monitor*, no. 1, taken from the site: www.fren.org.rs

¹⁰ *Kvartalni monitor*, no. 6, taken from the site: www.fren.org.rs

¹¹ In 2005 Statistical Office of the Republic of Serbia started preparing switching to calculation of inflation by the retail price index and thus the list of products included for calculation of retail price index was extended. Retail price index is calculated according to COICOP classification (Classification of Individual Consumption by Purpose), and is suitable for our analysis.

Table 6: Price change, indexes (prices in 2006 = 100)

COICOP category/year		Jan-07	Jan-08	Jan-09	Jan-10	Jan-11
100	Food and soft drinks	101.1	121.4	136.9	136.7	154.9
200	Alcoholic drinks and tobacco	116.1	130.0	162.0	179.7	207.7
300	Clothing and footwear	103.8	107.4	114.3	122.1	129.4
400	Housing, water, el. energy, gas	101.9	109.8	126.2	130.6	148.6
500	Household equipment and maintenance	100.0	105.9	105.9	114.4	125.0
600	Healthcare	104.9	109.8	116.6	124.1	134.0
700	Transportation	98.0	109.1	107.1	126.7	141.1
800	Communication	101.1	98.9	106.0	110.5	110.8
900	Recreation and culture	103.2	109.7	120.0	128.1	137.5
1000	Education	105.6	110.6	118.5	124.6	140.1
1100	Restaurants and hotels	103.9	111.3	121.5	128.7	138.0
1200	Other personal possessions and services	102.7	108.8	116.0	121.6	132.6

Source: Statistical Office of the Republic of Serbia

In 2008 the prices of food, alcoholic drinks and tobacco rose the most. Oil price declined everywhere in the world this year, which had a favorable effect on slowing the overall inflation in Serbia.

The recession that followed the economic crisis in Serbia in 2009, tamed the inflation, but still the rate of inflation was the highest compared with other countries in the region¹².

2010 was marked by the rise in price of food and drinks, which is shown in the last column of the table. Also, a permanent increase of excise duty on tobacco in the 2006–2011 period resulted in doubled prices of the products from the ‘alcoholic drinks and tobacco’ category at the end of 2010. The rise in the prices of bread, milk, cereals, fruit and vegetables made the price index extremely high in 2010. Although this rise is partly a result of the world trend of price rise after the crisis, the general problem of inflation in Serbia has the structural character.

Before drawing conclusions, another important factor needs to be mentioned. It is real income growth. Unfortunately, salaries in Serbia during this period were not synchronized with the price growth, which is seen in interannual indexes of average gross income¹³ given in the table below.

¹² *Kvartalni monitor*, no. 15, taken from the site: www.fren.org.rs

¹³ *Kvartalni monitor*, no. 23, taken from the site: www.fren.org.rs

Table 7: Monthly income and interannual indexes for the 2004–2011 period

Growth of average gross monthly income, annual indexes							
Year	2004	2005	2006	2007	2008	2009	2010
Indexes (previous year = 100)	111.4	107.1	111.3	114.6	104.8	100.6	101.2

After seeing this overview, we can give an answer to the following question: why did the share of services category rise in the 2003–2011 period? It is now clear that it is the result of the price rise which was not followed by the rise in real income. The consumers, burdened by high prices of housing and utilities and constant increase of transportation and communication services, which was a result of oil price, had to economize on food. This was achieved by buying low quality products, meaning that the quality of nutrition in Serbia worsened during this period. The above mentioned facts show the share in the total expenditure, which is an important indicator of the standard of living and personal consumption in our country. It is also important to monitor its changes from year to year, overall, and by categories. The following table shows indexes of changes in personal consumption expenditure.

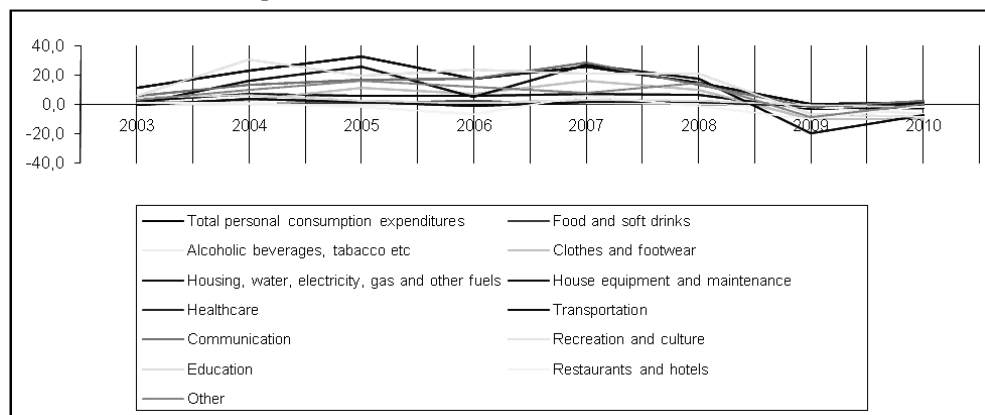
Table 8: Indexes of changes in total personal consumption expenditure and its categories

Household consumption, growth indexes (previous year = 100)									
Year		2003	2004	2005	2006	2007	2008	2009	2010
0000	Total	102.7	107.3	106.0	105.8	107.8	106.8	97.3	98.1
0100	Food and soft drinks	101.6	100.9	101.2	102.9	100.8	100.8	99.4	99.8
0200	Alcoholic drinks, tobacco and drugs	100.0	100.9	100.2	101.1	101.1	100.5	98.4	93.5
0300	Clothing and footwear	100.1	103.2	111.9	107.7	116.3	109.9	90.5	90.0
0400	Housing, water, el. energy, gas and other fuels	100.2	104.2	101.6	99.3	101.9	102.1	98.9	100.0
0500	Household equipment and maintenance	100.8	116.7	126.1	105.2	127.6	117.9	80.3	92.7
0600	Healthcare	111.6	123.5	133.2	117.6	125.9	115.0	100.5	101.0
0700	Transportation	112.4	123.5	104.6	113.7	109.6	112.2	104.4	95.1
0800	Communication	106.1	113.8	116.9	117.8	128.9	113.4	98.3	102.7
0900	Recreation and culture	106.3	130.7	119.6	124.3	121.3	121.3	94.0	91.3
1000	Education	105.0	106.5	102.3	101.0	103.1	102.8	99.8	98.4
1100	Restaurants and hotels	101.2	101.2	98.2	93.7	106.3	99.0	90.0	99.5
1200	Other personal possessions and services	103.4	110.5	116.6	112.3	108.2	115.0	91.4	100.9

Source: Statistical Office of the Republic of Serbia

A major change in all categories occurred between 2007 and 2009, while the most dramatic decline of personal consumption and all its categories was seen after 2008, which is shown in the penultimate column of this table. The following graph illustrates the above-mentioned trends.

Graph 2: Trends in personal consumption expenditure and its categories in the 2003–2010 period



The decrease in consumption of all categories is striking, which is the result of the external shock Serbia suffered after the outbreak of the world economic crisis. This implies that citizens were the first to feel and react to the unfavorable situation in the world that affected our country. People very quickly felt the lack of money because of unemployment, low wages, lack of adjustments to inflation and reacted to it by decrease in consumption of the most of the categories. A slight change can only be seen for the categories of food, drinks, alcoholic drinks and tobacco, i.e. spending on these categories remained almost unchanged during the 2003–2011 period. This is logical, as these needs are basic, and expenditure on them is low in our country. Having in mind the poverty in Serbia, further price drop would be impossible. The largest decrease is seen in spending on clothes and footwear, recreation and culture, restaurants and hotels. Spending on communication also dropped, although it was significantly rising until 2007. All these facts support the above-mentioned- the rise in share of categories 07 and 08 in the total expenditure is not a reflection of the standard of living, but the price rise.

We gain a deeper insight into the standard of living if we compare Serbia with the neighbouring countries in 2010. Indexes of real consumption expenditure volumes are used for this comparison per capita. The columns show certain categories of consumption and how much an average citizen of these countries spends compared to an average EU-27 citizen.

Table 9: The structure of consumption per capita compared to the average in the European Union countries (EU27 = 100) in 2010¹⁴, (%)

COICOP category / country	Bulgaria	Hungary	Romania	Slovenia	Montenegro	Croatia	Macedonia	Albania	BiH	Serbia
Food and soft drinks	48	61	81	91	100	74	93	68	72	70
Alcoholic drinks and tobacco	73	121	38	142	88	97	40	32	66	70
Clothes and footwear	18	23	18	75	25	33	23	21	20	17
Housing, water, el. energy, gas	49	71	50	84	48	74	46	34	42	58
Household equipment and maintenance	52	41	36	88	85	54	21	40	35	23
Healthcare	47	67	42	85	40	68	32	21	27	46
Transportation	46	45	37	96	38	44	23	11	22	32
Communication	64	49	34	97	91	76	53	17	30	70
Recreation and culture	35	55	28	79	18	53	11	10	19	22
Education	78	100	91	91	99	84	90	105	74	81
Restaurants and hotels	35	58	36	70	7	99	20	18	26	11

Source: Eurostat, published 12/1/2012.

This index tells much more about the standard of living, but the analysis should be conducted carefully, as the higher percentage of consumption compared to the EU average does not necessarily mean a higher standard. First, an analyzed category needs to be considered; if it is an item that satisfies basic needs, we cannot be happy about the high percentage compared to the EU, which is the case in Serbia.

The position of Serbia in 2010 was the closest to the EU-27 average in the following categories: food and drinks – 70 % of the EU-27 average; alcoholic drinks and tobacco – 70 % of the average; housing, water, electrical energy, gas and other fuels– 58 %; communication – 70 %; education – 81 %. This can seem encouraging at the first sight, but we have the real picture when we compare the rank of Serbia with other neighbouring countries. Although we still ‘follow’ European trends when it comes to spending on education, only Bosnia and Herzegovina and Bulgaria are behind us. Spending on alcoholic drinks and tobacco is still high, which certainly is not boastful. According to spending on housing, water, electrical energy and gas, Serbia is in the 4th place.

¹⁴ Eurostat provides data in PPS (Purchasing Power Standard), eliminating the effect of prices.

Serbia has the lowest rank for the following categories: clothes and footwear – the last position with only 17 % of the EU average; restaurants and hotels – penultimate place with 11 %; house equipment and maintenance – penultimate place, followed by transportation (7th position), food and drinks (7th position), recreation (6th position), and healthcare (5th position).

An average citizen of Serbia spent five times less on recreation and culture compared to an EU citizen, and 17% out of the amount an average EU citizen spends on clothes and footwear.

Having in mind low GDP per capita and high prices in Serbia, together with the fact that Serbia is compared to its neighbouring countries, not taking into account the standard of living in developed countries, we can conclude that the standard of living in Serbia is generally very low.

The following table shows the change of this index in Serbia in the 2005–2010 period.

Table 10: *Structure of consumption in Serbia in the 2005–2011 period, compared to the EU countries (EU-27 = 100), (%)*

COICOP category / year	2005	2006	2007	2008	2009	2010
Food and soft drinks	80	58	58	68	69	70
Alcoholic drinks and tobacco	60	62	61	69	70	70
Clothes and footwear	16	17	19	21	20	17
Housing, water, el. energy, gas	61	60	59	58	58	58
Household equipment and maintenance	19	20	26	31	26	23
Healthcare	43	45	47	48	47	46
Transportation	23	24	26	31	32	32
Communication	76	85	87	95	94	70
Recreation and culture	15	17	22	25	24	22
Education	80	79	82	81	81	81
Restaurants and hotels	10	11	12	12	11	11

Source: Eurostat, published 12/1/2012.

If we eliminate slight deviations in certain years (e.g. a growth in spending on communication in the 2007–2009 period and a slight increase of transportation expenditure), we can conclude that there are no substantial changes in the examined period, meaning that Serbia made no progress in five years. Also, Serbia did not have a significantly higher standard before the crisis either- citizens have been burdened with continuous rise in prices for years.

This section will be concluded with an overview of real personal consumption expenditure of an average citizen of Serbia compared to an average EU citizen and citizens of neighboring countries.

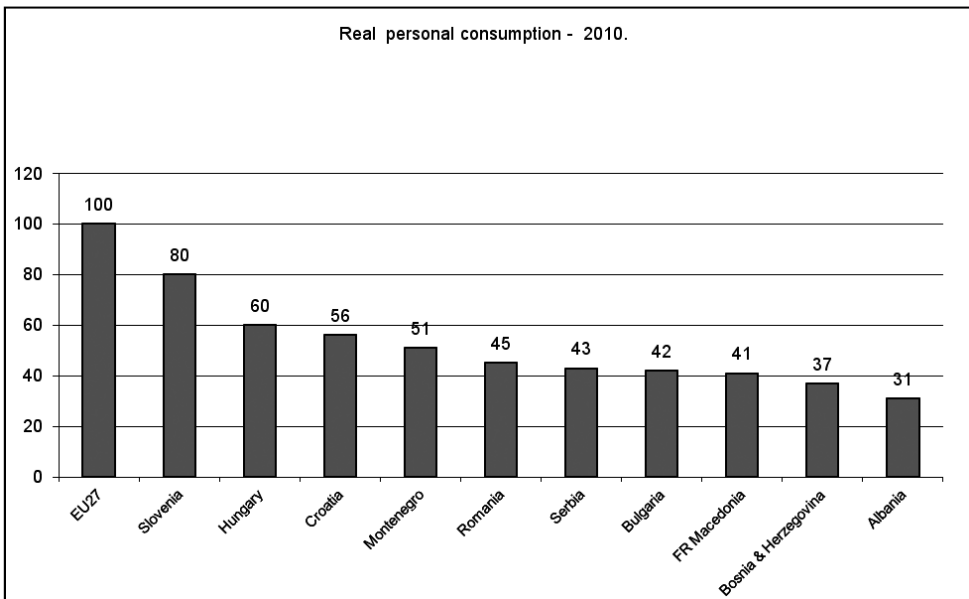
Table 11: Share of RPC per capita compared to the EU member states average (RPC per capita in the EU = 100), (%)

COUNTRY/YEAR	2005	2006	2007	2008	2009	2010
European Union (27 countries)	100	100	100	100	100	100
Bulgaria	39	40	44	45	43	42
Hungary	63	62	62	62	62	60
Romania	38	42	45	49	46	45
Slovenia	79	78	80	82	82	80
Montenegro	31	38	50	54	49	51
Croatia	56	54	57	60	58	56
Macedonia	34	35	36	40	41	41
Albania	26	26	28	29	31	31
Bosnia and Herzegovina	33	34	36	37	37	37
Serbia	38	39	40	44	44	43

Source: Eurostat, published 12/1/2012.

This is yet another measure of standard and our results are pretty bad again. The rank of Serbia in 2010, according to this indicator is shown in the following graph. Being on the weak 7th position, an average consumer in Serbia does not spend a half of the amount of real consumption expenditure of an EU citizen.

Graph 3: Real personal consumption expenditure in Serbia compared to neighboring countries and the EU-27 in 2010.



4. Conclusion

The first section of the paper shows that real consumption expenditure has the largest share in Serbian GDP. The biggest problem arising from this fact is lack of investments and savings-growth and development of economy is impossible without investments. The second part of the paper gives an insight into the standard of living, pointing out that most money is spent on food, drinks, housing, electrical energy and transportation. It seems that at this point, when investments are on a low level in the whole world, the only driving force in our country is demand. A proposal of a solution could be switching of Serbia to primary sectors – agriculture and energetics. As Serbia has a large number of the poor and those who use their income for meeting the basic needs, lowering prices of food, housing and utilities would significantly relieve these two categories of consumers. More money would be available for meeting other needs. If the current spending trend continues, there will be no room for secondary and tertiary sectors, and producers will be forced to leave these sectors because of low demand, which will have long-term consequences. It will take some time for investment measures in agriculture and energetics to yield the desired results. Hitherto, country should tackle the problem of monopoly position of food manufacturers and retail chains, which, if solved, could result in price decrease.

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ASSISTANT MARIJA LAKIĆEVIĆ, M.A.*

*Faculty for Hotel Management and Tourism, Vrnjačka Banja,
University of Kragujevac*

ASSISTANT MILICA ŽAREVAC

*Faculty for Hotel Management and Tourism, Vrnjačka Banja,
University of Kragujevac*

ASSISTANT NEMANJA PANTIĆ

*Faculty for Hotel Management and Tourism, Vrnjačka Banja,
University of Kragujevac*

GASTRONOMIC FESTIVALS IN RURAL REGIONS OF SERBIA

Summary

Gastronomic events have been frequently used as a tool for tourist animation and they could be a strong motive for visits to rural areas. Moreover, in an increasingly competitive world of tourism, each region is in continuous search for unique product in order to differentiate from other destinations. Local, authentic, specific food and gastronomy represent one of the resources capable of attracting visitors. Many other events that are based on habits, folklore and old fashioned ways of doing business contribute to such attraction, as well as the fact that population in Serbia gladly attends such events that are frequently the only drivers of social life. The aim of this paper is to point to the fact that festivals that promote food and beverages have special importance, especially when we take into consideration the fact that with those festivals both urban and rural regions have equal opportunities of becoming well known tourist destinations.

Key words: *food, visitors, tourism, events, rural regions, gastronomic supply*

JEL classification: L83, O14

1. Introduction

A larger number of better organized visits of tourists to rural areas of Serbia began only during the 70s of the last century, although these areas occupy 75% of the total territory in which there is approximately 50% of the population. Due to the natural, ecological and environmental characteristics, rural areas have

* E-mail: marija.lakicevic@kg.ac.rs

become very interesting and promising area for tourism development. Numerous villages provide peace and quiet necessary for the people of highly urbanized industrial centers. If we take into account the increasingly popular 'back to one's roots' concept and the one of 'healthy food' it is clear that the role of rural households has strengthened. In the framework of modern tourism, a need for discovery of new landscapes by food tasting has appeared, and culinary tourism has become very important worldwide¹.

An unavoidable segment of diverse and quality tourist offer of a country, region or a place certainly involves well prepared and organized tourist events. Cultural, economic, artistic, sporting, professional, religious, entertainment and gastronomic events attract potential tourists from home and abroad, especially if they are traditional and if they offer a rich program. The potential of these festivals in total tourist offer is remarkable, because they are complex cultural and social-economic events that attract significant attention of the media and general public. This segment of tourism industry should be specially analyzed, both for creating a positive image and reputation of the local community and its tourist values, and because of the tourism prospects of the whole country, which can be very attractive to visitors - largely owing to a specific cuisine of different rural areas. The cuisine of Serbia is a part of general material culture through which the customs and traditions of the village can be met in the best possible way.

2. General concepts and definitions

The general concept comes from the Latin word *manifestacion* that means public manifestation, display, disclosure, publication, or public expression, economy activity. In the foreign literature and tourism practice this type of tourism is known as *event tourism*, as well as *festivals*. In addition to offering entertainment and information, these events provide numerous contributions to the community². Thus *event tourism* represents a form of tourist offer in which the content of an event associated with the event location represents the tourist value in itself, attracting potential visitors, with implications of a range of the related tourist programs connected with natural and anthropogenic tourist values of the event. Therefore, it is not surprising that today these festivals have become the most widespread type of special modern events, as well as the fastest growing tourist attractions³.

¹ T. Stojanović, S. Čerović, 'Značaj gastronomske ponude za razvoj seoskog turizma Srbije', *Zbornik radova PMF*, no. 56, Geografski institut, Beograd, 2008, pp. 165-176.

² Ž. Bjeljac, *Teorijsko-metodološke osnove manifestacionog turizma*, Beograd, 2006, p. 7.

³ Ž. Bjeljac, N. Čurčić, 'Turističke manifestacije na prostoru zapadnog Pomoravlja', *Glasnik srpskog geografskog društva*, no. 2, 2007.

The words: *gastronomy* and a *gastronome* appeared at the beginning of the 19th century in France and are defined as the art of enjoying food, culinary methods of food preparation, cooking, knowledge on food, enjoying cooking, and thermal processing. Serbian cuisine is formed under the influence of Turkish, Hungarian, Bulgarian and partly oriental cuisine. Serbian cuisine dishes are versatile, what can be linked with religious traditions and frequent fasts⁴. Traditional cuisine can be represented in the tourist industry as:

- 1) a framework for the marketing of cultural and artistic content;
- 2) a content with an independent effect, food tasting, with the aim of familiarizing people with nutrition;
- 3) the factor of attraction of boarding services;
- 4) a framework for education through numerous courses;
- 5) a content of tourist, graphic and visual information (monographs, posters, calendars, cookbooks, etc..)
- 6) services.

In recent years events promoting food such as fairs, festivals, and exhibitions are becoming increasingly popular, and can be held only once or be traditionally repeated. Food festivals are actually services aimed at consumers and characterized by perishability, heterogeneity, intangibility and inseparability⁵. It is believed that their primary function is to allow sponsors, hosts and other investors' high prominence in the market with the corresponding value of the brand and establishing of relationships with clients and consumers⁶. They play an important role in tourism and marketing and have led to the establishing of special professional organizations dealing with them. Also, food and wine tourism is increasingly studied, and is often called gourmet, culinary or gastronomic tourism. *Culinary tourism* is a subset of cultural tourism where culture and history of a particular environment are explored and discovered through food⁷. In other words, culinary tourism is defined as the activity of exploration and discovery of culture and history through food, which contributes to the creation of unforgettable experiences⁸. However, due to the nature of food as products and the everyday role it plays in consumption and economic systems, the events promoting food increasingly coincide with economic, political and social issues,

⁴ M. Protić, *Gastronomija*, Fakultet za turistički i hotelijerski menadžment, Univerzitet 'Singidunum', Beograd, 2011, p. 111.

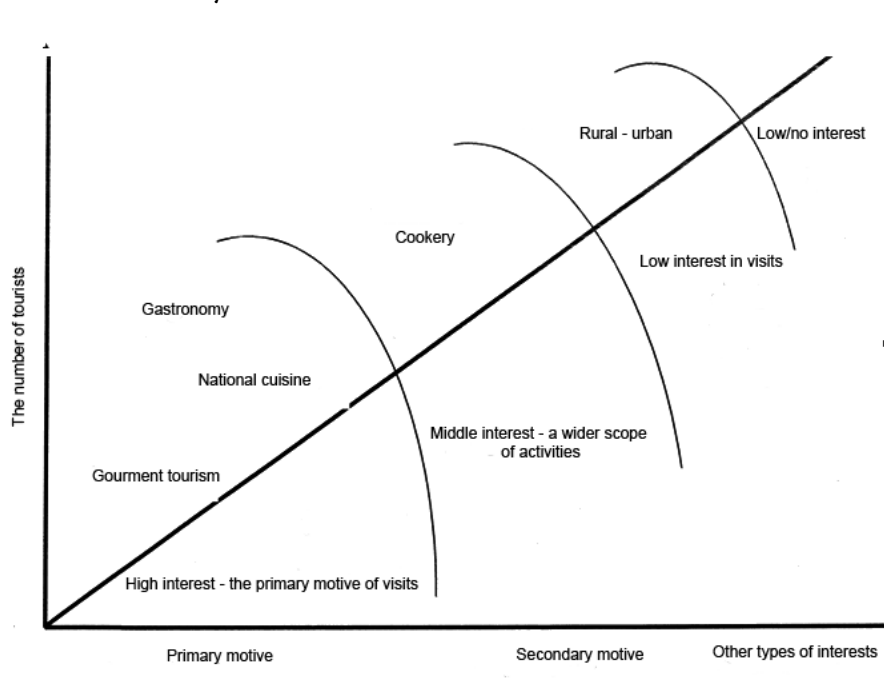
⁵ For more detail see in: C. M. Hall, L. Sharples, *Food and wine festivals and events around the world*, Elsevier, Oxford, 2008, p. 312.

⁶ C. M. Hall, R. D. Mitchel, *Wine Marketing: A Practical Approach*, Butterworth-Heinemann, Oxford, 2008.

⁷ B. Kalenjuk, 'Gastronomski potencijali Vojvodine u funkciji razvoja turizma', *Zbornik radova Departmana za geografiju, turizam i hotelijerstvo*, Novi Sad, no. 40, 2011, p. 180.

⁸ M. N. Long, *Culinary Tourism: A Folkloristic Perspective on Eating and Otherness*, Southern Folklore, 55 (3), 1998, pp. 181-204.

related to the nature of modern agricultural systems, the preservation of rural way of life and communities, as well as concern for food quality. There is general agreement that the number of these events is growing worldwide, although it is very difficult to accurately determine their real number.



Picture 1: *Food as motivation for traveling*⁹

Food tourism is defined as visits to primary and secondary food producers, food festivals, restaurants and specific locations, whereby the key motivating factor of traveling is food tasting and visiting the regions producing food¹⁰. In addition, wine tourism, as a subgroup of food tourism, is defined as a visit to vineyards, wine festivals and wine shows, the primary motivating factor for visitors being wine tasting and visits to the regions in which it is produced. Of course this definition does not mean that any traveling to an event is an example of food tourism; it is the desire to taste a certain type of food or agricultural produce of a particular region that is the main motivation for traveling. In fact, food tourism can be considered an example of gastronomic tourism that attracts consumers

⁹ C. M. Hall, L. Sharples, op. cit., p. 6.

¹⁰ C. M. Hall, R. D. Mitchel, *Wine and food tourism* in Douglas, N., et all *Special Interest Tourism: Context and Cases*, John Wiley and Sons, Australia, 2001, p. 308.

whose interest in food and wine represents a form of a serious vacation (leisure). A number of advantages of these events can be identified:¹¹

- Increased number of visits to a region;
- travelers' staying within a given place or region;
- the economic benefits of attracting the funds of the local economy;
- the increase of employment;
- improving the image of the destination;
- increase community pride and help in creating a sense of community;
- reducing the impact seasons by extending the tourist season;
- adding value to the existing food and rural products;
- providing social, cultural and health benefits.

When studying events that promote food we should consider spending that can not occur without the production, and vice versa. Key factors that determine a visit to an event promoting food from the production point of view are: location, timing, accessibility, attractiveness, space, infrastructure and the event capacity; event planning and programming, promotion and marketing, and the like. From the consumer's point of view it is important to consider: traveling time in relation to the leisure time of potential visitors (time budget), economic budget of visitors and accessibility of events, motivation, past experience, re-visits and the positive recommendations of relatives, friends, and so forth. It is also important to note that visitors to gastronomic events are not a homogenous market, but that different events attract different audiences.

3. Gastronomy and the Events of Rural Serbia

Gastronomy in rural areas is very specific and attractive for tourist demand especially as in the cultural life of the countryside it is perhaps diet that has changed least. This is corroborated by the fact that Serbia is the country of authentic or minimally modified environment and diverse and preserved nature. Therefore the production of healthy, organic food in the countryside can provide a more favorable market position, improved competitiveness and profitability¹². Namely, rural tourism includes a variety of activities, services and contents organized by local people on family farms with the aim of attracting tourists and creating additional value for the tourist product¹³. Guests are presented with traditional hospitality and life values of the local population, so this kind of tourism

¹¹ C. M. Hall, L. Sharples, *Food and wine festivals and events around the world*, Elsevier, Oxford, 2008, p. 6.

¹² T. Stojanović, S. Čerović, op. cit., p. 166.

¹³ S. Đekić, M. Vujičić, "Ograničenja u razvoju održivog ruralnog turizma", *Turizam*, Novi Sad, 2004, pp. 34-35.

represents an important lever of economic development and increase of living standards in rural communities, all on the principles of sustainable development and protection of natural resources¹⁴. Also, access to rural areas as potential tourist destinations requires that in addition to accommodation units much attention should be devoted to gastronomy.

Gastronomic culture is an inseparable part of the cultural heritage of the Serbian people. Foods that are used in the diet, habits and customs related to food preparation and the behaviour at the table are part of the spiritual wealth and heritage of a people, that are handed down from generation to generation. Our country has a remarkably rich and diversified gastronomic culture, as a result of geographical position, influence and contact with other cultures. Food, wine and tourism are closely linked. Gastronomy is an integral part of tourism and, as the tourist offer of a region includes the folklore, traditions and customs, the food of a region is also inseparable from tourism. In the tourist market food is recognized as:

- 1) a part of the local culture that tourists consume;
- 2) a part of tourist promotion;
- 3) a potential component of the local agricultural and economic development;
- 4) a regional factor influenced by the patterns of consumption and the observed desire of tourists¹⁵.

Across the regions, cuisine and the events that take place in rural areas look like this: **Vojvodina** has a number of specific and authentic foods and drinks based on organically grown plants and animals. *Vojvodina cuisine* is considerably different from those of other parts of Serbia due to central European influence, mostly German, Austrian, Hungarian and Slovak. Great importance is given to pastry (breads, strudels, noodles) and meat products made out of the rich stock of cattle and poultry. Nowhere in Europe are there so many different peoples living on such a small area as here. The meetings of various peoples and cultures in this region, their permeation and mutual respect and acceptance have contributed to the wealth that we have today. Archaeological sites, traditional architecture, cultural heritage, authentic costumes, customs, songs, old handicrafts, various culinary specialties and plenty of natural oases make this entire space unique and special. Moving from village to village one can meet numerous ethnic communities that inhabit these areas and nurture their specificity in order to preserve their national identity. It is this rich diversity that makes the highest value of this space and makes the most important prerequisite for tourist promotion¹⁶. One of the biggest culinary events is the 'Sausage Festival' in Turija; it lasts three days and is visited by a few tens of thousands of people. There is also the 'The Prudar Days' tourist event in Irig, which in addition to a rich cultural program,

¹⁴ T. Stojanović, S. Čerović, op. cit., p. 167.

¹⁵ C. M. Hall, R. D. Mitchel, op. cit., p. 308.

¹⁶ www.klubputnika.com/profiles/blogs/bogatstvo-razlicitosti

organizes various other competitions, such as the selection of the best soup, the best Prudar stew, wine and brandy. A very large number of culinary events takes place in Vojvodina: 'The *Kulen*¹⁷ Festival' (The Festival of Kulen from Petrovac), 'The Wild Duck Stew Festival' (Bečej), 'The Days of Cucumbers' (Bačko Selo), 'The Evenings of Mother Mary' in Stapar, 'The Indian Days' in Backi Breg.

Central and Western Serbia is mostly dominated by highland-cattle breeding area, because of which the best known products of the area are milk and meat; this also includes the well-known Zlatibor ham (*prsuta*) and cream cheese, which are traditional Serbian products and are made in a similar way in other Balkan countries. Famous festivals of this region are: 'Dragačevo Brass Festival' which among other values promotes the regional cuisine; then there is the 'The Cabbage Festival' in Mrcajevci which is the competition in preparing and cooking cabbage in a clay pot. The Drina Regatta' is the oldest event of a tourist and recreational character, which tends to show the overall tourist offer of this region. The regatta is the most visited event in the western Serbia and also a central summer event. The recreational downhill that is attended by hundreds of boats and vehicles, trumpets, and a floating bar is accompanied with a barbecue and other specialties of local cuisine.

Due to its natural beauty and environmentally well-preserved landscapes, ethnic and ecological diversity, **Eastern Serbia** is potentially a large and important tourist destination. However, this part of Serbia lags behind the main trends of development of Serbia as a result of economic crisis and unfavorable demographic situation (low birth rate and high emigration). These statements apply to gastronomy, especially for the Vlach minority. In the spring and summer season some villages surrounding Smederevo organize events dedicated to the fruits thriving in the villages, such as "The Strawberry Festival', 'The Peach Days', 'The Blackberry Days, 'The Watermelon Days'. The aim is to show the achievements of production in this way and improve the marketing of fruits. The most important events of this region are: 'The Days of Brestovac Spa' (the preparation of well-known dishes of the region), 'The Meetings of the Bor Villages', 'The Fishermen's nights' (the competition in the preparation of the fish soup in Veliko Gradiste).

Southern Serbia is known as a typical Balkan cuisine, due to the influence of other Balkan peoples (Bulgarians, Turks, Greeks), as well as the abundant use of succulent vegetables, especially peppers after which this region is known. Of course, there is also a well-known barbecue the preparation of which has been inherited from the Arabs. The most famous rural gastronomic events are: 'The Days of Pepper' in the village of Donja Lokošica, 'The Days of Cheese Pie', 'The Days of Burek¹⁸, 'The days of Aspic', 'The Preparation of Fish Soup and Pepper', 'The Preparation of Cracklings'.

¹⁷ 'Kulen' is a special type of sausage.

¹⁸ Burek is a famous type of pie inherited from the Turks.

Gastronomy of the **Southwestern Serbian** region (**Sandzak**) is marked by oriental influence that is adapted to the dry climate. Pies and pastry are made with different additives; this regions is also known for its buckwheat and Pester cheese, as well as oriental sweets: the baklava and kadaif. The well known events are those that are held in honor of honey and fish soup: 'The Days of Sjenica pie', 'The Cheese Festival', etc., all that with the aim of attracting as many visitors as possible.

Speaking in terms of percentage, the largest number of events taking place in Serbia is in Vojvodina (38.9%), a somewhat smaller number in Šumadija and Western Serbia (27.3%), followed by Eastern and Southern Serbia (17.7%), while in Belgrade it is 13.49%, and in Kosovo and Metohija only 2.5%. Across the country, the most common are the folklore events, and their visitors are most attracted by the stew in Vojvodina (The Backa pot - Bac), The Tobacco Cracklings Festival, the Serbian brandy and smoked ham festivals (The Brandy Festival, The Ham Festival, Čajetina), but also the specialties of the Svrlijig cheese and corn flour. Considering the percentage the most common are the tourist events organized once a year (94.9%), every second event lasts from a couple of days to a week (49%), while the half-day events are less common (22.1%) as well as those whose programs last longer than a week (23.5%). For the event organizers summer months are by far the most attractive (34.2%), while in winter only 10.9% of events are held. The conducted research has shown that a pleasant atmosphere, people, and the cuisine leave the most favorable impression on foreign tourists.

4. Further directions of development

It is noticeable that the Serbian gastronomic supply is very rich, but it is necessary to work on its gastronomic image, to unite the supply and protect food products such as tall bread, ham, *ajvar*, cheese, cream cheese and others as national brands. At the Fair of Tourism it was announced that Serbian cuisine is still not competitive on the European and world markets, because in spite of a healthy agricultural production and livestock fund it fails to meet food safety standards required for participation in the global tourist industry¹⁹. The benefits of gastronomic tourism in a certain area are reflected in:

- a) increased demand for agricultural food products and food specialties;
- b) building a brand;
- c) educational opportunities for visitors and residents;
- d) regional and local distribution of consumption;
- e) protection of intellectual property.

Serbia clearly has to work towards developing the whole tourist offer of its rural areas, and therefore the offer of its cuisine, which can be a great motiva-

¹⁹ www.svrlijig.net/forum/gastronomija/srbiji-potreban-gastronomski-imid382, downloaded on March 20 2012.

tion to domestic and foreign tourists to visit the Serbian village. In this sense, there are three approaches to the development of this type of tourism: the first is the nearing of the village and the town, by opening the ethno-restaurants; the second is the development of tourism in rural households, which requires investment because infrastructure and sanitation must be adapted to the high demands of visitors and tourists. The third approach means directing particular rural household owners towards tourism turning it into their primary occupation. This is supported by the fact that 2000 foreign tourists were the guests of the rural households at the expense of the state. Besides the gastronomic supply, visits to farms, plantations, wine and brandy cellars, participation in daily work activities, and the like should be organized for tourists. In that way the rural gourmet product can become a brand that can be tasted, consumed, sold with its properties and designations (an eco-product, a green product with no additives, no chemicals, prepared in the traditional way, and so on).

Also, gastronomy with its activities can be extremely helpful for creating the content of the tourist stay. These could be daily activities, such as participation in food preparation, preparation and production of bread in the rural way, making pie crusts and strudel pastry, preparation of home canned food, brandy distilling, table setting and food serving ... The Group for event organizers was established with the Serbian Chamber of Commerce, within the Association for Tourism. The Group categorizes, evaluates and classifies events and determines the economic effects that events may have. The aim is to identify the profitability of certain events so that they would be financed from the budget, and not only from local administration. It is essential that events should be accompanied by good infrastructure, adequate accommodation capacity of adequate standards in rural areas (i.e. smaller family accommodation capacities), satisfactory quality of catering services and offers, fostering local cuisine, souvenirs, traditional products, etc.

5. Conclusion

The awareness of the need for developing and holding gastronomic events in rural areas is not equally developed in all parts of Serbia. Studies point to the fact that the positive effects of events that tourists create by their visits exceed economic benefits, leading to the strengthening of social capital and significant improvement in quality of life in these areas. Thus, the reliance of many rural communities on event tourism as a major source of revenue has caused the emergence of numerous events and festivals. Yet, huge competition and market saturation have led to failure the key factors of which are: insufficient funding, inadequate promotion, inadequate strategic planning and the incompetence of personnel for this tourist product. It is therefore necessary to improve the quality of events and focus more attention on originality, attractiveness, a well-designed program and contents with the aim of achieving competitive advantage of rural destinations.

From an economic point of view, the importance of holding events in rural areas and their planning, organization and promotion contributes to the possible employment of the population, reduction of the adverse migration flows and the realization of income. Understood in this way they constitute the basis for further development of the economy, reduce regional disparities, and enrich the tourist offer of the countryside, making a destination more significant and attractive for both locals and for numerous visitors.

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PROFESSOR FRANÇOIS COLBERT, PHD*
*The Carmelle and Rémi-Marcoux Chair in Arts Management,
HEC, Montréal, Canada*

FINANCING THE ARTS: SOME ISSUES FOR A MATURE MARKET

Summary

The market for arts and culture suffers an oversupply of works of art. After two decades of rapid growth, demand is now leveling off; this phenomenon started in the 80's. This poses a challenge to granting bodies and to arts organizations. In the cultural sector, one can find what Porter defines as barrier to exit. Artists will choose to starve instead of leaving the field. Every year more companies are created than companies that are disassembled. Parallel to this phenomenon, the jury system used by Arts Councils are judging the grant applicants on artistic excellence defined very narrowly as perpetual run for innovation. In most jurisdictions, companies and artists independently of their age and experience are judged the same than new ventures. One could want to challenge this way of doing. This paper examine three challenges the arts sector is confronting to, the market saturation, the jury system and the aging leaders at the top of artistic organizations created thirty to forty years ago.

Key words: *arts, demand evolution, granting system, transition*

JEL classification: H81, Z11

1. Introduction

In this beginning of the twenty first century, several challenges are confronting the artistic world. Three particular issues will be discussed in this paper: the market saturation in the industrialized countries; the limits of the Arts Councils jury system used by many countries in deciding what art or artists should be encouraged; and the necessity to consider the arts organizations in the long term when replacement at the top will become a real challenge.

The arts and culture world is peculiar for many reasons. Concepts such as *managing discontinuity, intermittent workers, dual management, patrimoniality, and immateriality* are characteristics that pertain to the cultural sector.¹ The sec-

* E-mail: francois.colbert@hec.ca

¹ Y. Édvard, F. Colbert, "Arts Management: A New Discipline Entering the Millenium", *International Journal of Arts Management*, Vol. 2, No. 2, Winter 2000, pp. 4-14.

tor is familiar with producing a continuous flow of new products. The artist does not want to always create a new work of art as soon as he finishes one production; moreover, he or she does not want to be driven by market needs.² The artistic sector is then always in the situation to launch new products; it is a challenging situation; in the traditional sectors of the economy, every entrepreneur or manager knows that launching a new product is a risky business one gets in with heavy precautions and a lot of fear. The arts though are a risky business. Even presenting a well known chef d'oeuvre as the 9th Beethoven Symphony is a new product; indeed, it will be colored by the Maestro style and the uniqueness of the orchestra playing. Applaud from the public, the critics and the funding bodies are not guaranteed.

This situation of stepping from one product to a new one means discontinuity in the production line. A production does not go on forever except for specific cases like Broadway shows. Moreover, companies usually hire different creative workers for every specific production. This situation is more frequent in North America where the concept of State Theatres does not exist and productions are run with a specific number of performances set in advance. A small permanent staff is managing a large number of intermittent workers according to the needs of each production. Companies are all private but registered by Law under a not-for-profit status.

In every artistic organization there are also two heads, the artistic director and the administrative manager. Even when the artistic director bears the name of "general manager", he or she has to work with its twin, the administrative director. The other important actor is the Boards of Trustees who play an important role, a governance role as well as a fund raiser role. As a governing body, members of a Board must make strategic decisions under a great deal of uncertainty.³

As soon as it is created, works of art pertain to the heritage domain of the country of the artist. The value of a work of art, a painting or a piece of music, can fluctuate over time. To put a value on such complex products is quite a challenge, virtually impossible to meet.

Finally, as for a service, the benefits a consumer gets are immaterial.⁴ The contact with a work of art falls into the domain of experience; artistic products are said to be experiential products.⁵ The quality of the experience plays a role in

² B. Jaworski, A. K. Kohli, A. Sahay, "Market-Driven Versus Driving Markets", *Journal of the Academy of Marketing Science*, 28 (1), 2000, pp. 45-54.

³ G. B. Voss, Z. Giraud Voss, "Strategic Orientation and Firm Performance in an Artistic Environment", *Journal of Marketing*, 64 (1), 2000, pp. 67-83.

⁴ B. Gainer, P. Padanyi, "The relationship between market-oriented activities and market-oriented culture: implications for the development of market orientation in nonprofit service organizations", *Journal of Business Research*, 58, 2005, pp. 854-862.

⁵ A. Carù, B. Cova, "How to Facilitate Immersion in a Consumption Experience: Appropriation Operations and Service Elements", *Journal of Consumer Behaviour*, 5, 2006, pp. 4-14.

the satisfaction and the appreciation by the public of the work of art.⁶ Going to a gallery or a theatre or a movie theatre is to live an experience for the consumers. The client cannot test a work of art before actually seeing it. Production and consumption are simultaneous. To know if a film or a play is good, somebody has to see it.⁷ The same way, deciding what is good or bad is a matter of personal tastes, which in turn depends on the past experience of the consumer or where he is coming from.⁸

2. The Models for sustaining the Arts

The literature defines three general models for subsidizing the arts: the architect model, the sponsor model and the facilitator model.⁹ The first model corresponds to what is in use in most of the European countries; a system where decisions are made at the top through, usually, a ministry of culture and, some would say, imposed from top to bottom. Decisions are taken based on a set of objectives decided by government and the means (money) is put behind those objectives. This system is usually articulated through a cultural policy. The government can be a central government but can also be a city or a region. France is often used as the example of the architect model.¹⁰

England or more generally speaking Great Britain is said to be the incarnation of the sponsor model. Created after the Second World War, the Arts Council system was adopted by most of the foreign countries member of the British Dominion. The Puritanism inherited from the Victorian era made impossible

⁶ J. K. Maher, J. C. Clark, D. G. Motley, "Measuring Museum Service Quality in Relationship to Visitor Membership: The Case of a Children's Museum", *International Journal of Arts Management*, Vol. 13, No. 2, Winter 2011, pp. 29-42.

⁷ P. Harrison, "Evaluating Artistic Work: Balancing Competing Perspectives", *Consumption Markets & Culture*, 12 (3), 2009, pp. 265-274.

⁸ W. Atkinson, "The Context and Genesis of Musical Tastes: Omnivorosity Debunked, Bourdieu Buttressed", *Poetics*, 39, 2011, pp. 169-186; P. Bourdieu, *Distinction: A Social Critique of the Judgment of Taste*, Routledge & Kegan Paul, London, 1984; T. C. G. Fisher, S. B. Preece, "Evolution, Extinction, or Status Quo? Canadian Performing Arts Audiences in the 1990s", *Poetics*, 2003, pp. 69-86; J. Gripsrud, J. F. Hovden, Hallvard Moe: "Changing relations: Class, education and cultural capital", *Poetics*, 39, 2011, pp. 507-529; D. B. Holt, "Distinction in America? Recovering Bourdieu's Theory of Tastes from Its Critics", *Poetics*, 25, 1997, pp. 93-120; A. Warde, M. Gay-Cal, "The Anatomy of Cultural Omnivorosity: The Case of the United Kingdom", *Poetics*, 37, 2009, pp. 119-145.

⁹ K. V. Mulcahy, "Cultural Patronage in Comparative Perspective: Public Support for the Arts in France, Germany, Norway and Canada", *Journal of Arts Management Law and Society*, Vol. 27, No. 4, 1998, pp. 247-263.

¹⁰ R. Wargermée, "Les objectifs de la politique culturelle française", *La Politique culturelle de la France*, Programme européen d'évaluation, La Documentation française, 1998, pp. 26-54.

for government during the war to subsidize directly concerts and other performances for the benefits of a suffering population. In a country where theatres were often assimilated to brothels, the State had to find another way to pour money into profane events. A not for profit organization was created to receive government grants and to make possible such concerts. After the war the system was kept through the Arts Council of Britain. But since the State cannot express tastes in the matter of arts, the arts council becomes the solution; arts councils use a system of juries of peers - meaning other artists - to decide on the quality of the artistic propositions. The Canada Council for the Arts for instance uses jury recommendations as quasi decisions that the top management or the governing board of the organization cannot modify or refuse.

Lastly, the facilitator model corresponds to the US way of doing things.¹¹ America prefers to let the citizens decide locally for public domains such as hospitals, schools and cultural goods. To understand how American citizens cherish their way of managing things, one must go back to the American Revolution when the new colony won the war against Britain, and decided they would never again be ruled by a King. The federal government cannot, by Constitution, get involved in health, education and culture. If citizens decide to have an orchestra or a museum, it is not to the federal state to tell them to have one. If wanted by citizens, the population gets organized, raise the necessary funds and create their own cultural organizations. Under such a model a body like the National Endowment for the Arts (NEA) is an anomaly to the American life. It is not a surprise then that the NEA budget is always at stake at the US Congress. The American model is to let things happen but to allow donors - individuals, foundations or corporations - to deduct their donations from their revenues. This possibility is now used for decades in other countries such as Canada who imported the model from USA. It is more and more the case around the world. It is a good way to encourage individuals and corporations to give to the arts. On the dark side, ministers of finance tend not to like this system since they lose control on public expense; a tax deduction is similar to an expense for a Government; moreover, it is a sum the minister does not control because he does not know how much taxes he will not collect in a given year because of those legitimate deductions.

Are the results on market consumption different depending on the model? No, despite heavy investments in the arts, the architect model does not perform better or worst compared to US model where there is almost no public investments; the end result is identical (in United States, performing arts gets no more than 0 to 10% of their revenues from public money, for most of them it is zero public money). In all the industrialized countries, the percentage of the general population going to the arts is equivalent, be it in France, in USA, England, Aus-

¹¹ A. Zimmer, A. Toepler, "Cultural Policies and the Welfare State: Cases of Sweden, Germany, and the United States", *Journal of Arts Management, Law, and Society*, Vol. 26, No. 3, Fall 1996, pp. 167-193.

tralia or elsewhere. It is equally the case for the profile of the consumers, one will find the same socio-demographic profile everywhere - highly educated people in the high arts (theatre, symphonic music, opera, and art museums) compared to a profile close to the general population in the popular art. This profile of the clientele has not varied since fifty years. The only thing that changed is the proportion of the population that now holds a university degree that went up from 5% to 20-25%, increasing the potential market for the arts.¹²

3. First Challenge: Market Saturation

After World War Two, five factors boosted the demand curve for arts and culture to the level we experiment nowadays. The baby-boom effect was the first factor. In a country like Canada for instance, the growth of population was 5 to 6% a year. In the sixties, the effect of this flux of young adults combined with the increase of leisure time (second factor), of real salary (third factor) and the more generalized access to university (fourth factor) played positively on the demand for leisure activities. Add to this the fifth factor, young ladies that made the choice of more education, a career of their own, having a smaller number of children ... later in life ..., plus their natural inclination for arts and culture instead of sports,¹³ and one can understand the rapidly increasing demand curve for cultural products until the eighties. When one adds up all monies spent for arts and cultural products, it realizes, comparing the figure from the same calculation for sport, that demand for culture is surpassing demand for sports since 1975.¹⁴

Parallel to this demand growth, supply was pushed by heavy investments in the arts by governments. In every industrialized country, budgets and cultural policies flourished with the general wealth of society. In the 80's though, the basic factors underlying the demand growth ceased to play.¹⁵ At a time when industrialized countries are struggling to maintain their population level, salaries and leisure time are frozen, and the percentage of citizens getting to higher

¹² F. Colbert, "Entrepreneurship and Leadership in Marketing the Arts", *International Journal of Arts Management*, Vol. 6, No. 1, Fall 2003, pp. 24-35.

¹³ B. Gainer, "Marketing Arts Education: Parental Attitudes Towards Arts Education for Children", *Journal of Arts Management, Law and Society*, Vol. 26, No. 4, 1997, pp. 253-268; R. A. Peterson, R. M. Kern, "Changing Highbrow Taste: From Snob to Omnivore", *American Sociological Review*, Vol. 61, No. 5, October 1996, pp. 900-907.

¹⁴ F. Colbert et al., *Marketing Culture and the Arts*, 3rd Edition, Chair in Arts Management Carmelle and Rémi-Marcoux, HEC, Montréal, 2007; F. Colbert, "Beyond Branding: Contemporary Marketing Challenges for Arts Organizations", *International Journal of Arts Management*, Vol. 12, No. 1, Fall 2009, pp. 14-20.

¹⁵ M. Hume, G. Sullivan Mort, P. W. Liesch, H. Winzar, "Exploring repurchase intention in a performing arts context: who comes? and why do they come back?", *International Journal of Nonprofit and Voluntary Sector Marketing*, 12, 2007, pp. 135-148.

education and the presence of females on the market are stabilizing. As it happens often on any market, supply does not stop increasing. Thousands of young artists are coming out of arts schools, often creating their own company in the absence of any other possibility to work in current organizations. Since in this sector, exit barrier are very strong,¹⁶ meaning actors will remain in business even if the pay is low, very few companies close doors. Every new company created by a young generation of artists on the cultural scene contributes to increase supply. Successful art organizations travel outside their home country; this influx of premium products make life more difficult to new art organizations and to less desirable work of art in the host country. Another important element to take into account is that, despite cultural policies to democratize high art, the socio-demographic profile of the consumers did not change; audiences to high arts are composed of 65 to 90% of university graduates.¹⁷ The highly educated segment of the market remains small at 20-25% of the population depending on the country, while more cultural enterprises are courting it (1).

An illustration of the importance of the oversupply of cultural products on a given market is the case of the number of authors of novels on the Canadian market and what it would take to make them live on their author's fee. A simple calculation goes this way. If every one of the 17,500 Canadian authors of novels could earn the average personal salary of a Canadian counting on the 10% author's fee on the gross sales of their novels, every Canadian family would have to buy 50 Canadian novels per year to make this happens. The Canadian population is far from buying this quantity, even in the very educated sectors of the population, including people from the cultural sector. This example shows how crowded the cultural market is. On any of the art forms and for any country, one could make the same counting and get to the same conclusions.

As a general consequence of this situation, artists complain on their poverty, arts councils and governments receive more and more requests for financial help while budgets for culture do not grow, or do incrementally only. National Arts Organizations lobby for more public and private monies, and arts activists put forward the argument that population do not have enough access to "culture". Of course, in this case, the word "culture" means "high arts". Indeed, the reality is that every citizen has access to a tremendous number of cultural products, and is consuming lots of cultural products every year. Every one listen to music on radio, or watch soaps on television, or read some kind of books, or watch film on the small screen or in movie theatres, go to museums or performing arts, and so on. From the consumer's point of view, the market offers tremendous supply of cultural products that can satisfy any desires. The fact is that for someone living in a large city, it is impossible to see everything proposed, financial means but

¹⁶ M. E. Porter, *Competitive Strategy*, The Free Press, New York, 1980, p. 396.

¹⁷ F. Colbert et al., *Marketing Culture and the Arts*, 3rd Edition, Chair in Arts Management Carmelle and Rémi-Marcoux, HEC, Montréal, 2007.

moreover time do not permit to see all. Choices are made and those choices are often American products made by Hollywood mass production or conglomerates in the entertainment business.

One can criticize the choices of cultural products made by their fellow citizens, but nobody can force anyone to buy what is of no interest to this person. Solution will not come from more government money to fund the same kind of cultural products. There is a limit to the demand growth by the influx of more supply and this limit has been surpassed.

No one will dispute the fact that art is an important asset for a country and its citizens. Even if art is for most people a leisure activity,¹⁸ the production by many artists contributes to the intellectual discourse essential in a democracy. Works of art have their own meanings and destiny and are not meant to fulfill other “productive” ends. Artistic production does not create economic wealth; no sector of the economy that has to be supported year after year in the proportion of 40% or more of their revenues by public funds can be said to contribute to economic wealth. Anyway, high art is not meant to create economic impact while entertainment not supported by public funds may. The level of professional artistic creation has always been proportional to the wealth of a given society. History tells us about great civilizations and their magnificent works of art; all of them were the decision of very rich families or kingdoms. In poor civilizations, people were singing, dancing and painting, but were not investing in works of art.

Of course subsidized artistic production produces economic activities, but any expense made by any actor in a given economy also produces economic activity. No one will dispute the benefit of, for example, artistic education for children,¹⁹ or the artistic activities for the revitalization of neighborhoods,²⁰ but the apology of artistic productions to resolve every problem of a country, like for instance the creative class concept,²¹ rely on no scientific grounds or serious research.

¹⁸ C. Scott, “Branding: Positioning Museums in the 21st Century”, *International Journal of Arts Management*, Vol. 2, No 3, Spring 2000, pp. 35-39.

¹⁹ F. D’Angelo, D. Furia, A. Crociata, A. Castagna, “Education and Culture: Evidence from Live Performing Arts in Italy”, *Procedia Social and Behavioral Sciences*, 9, 2010, pp. 1373-1378; K. Johansson, “Culture for or by the Child? ‘Children Culture’ and Cultural Policy”, *Poetics*, 38, 2010, pp. 386-401; K. Krackman, “The Effect of School-Based Arts Instruction on Attendance at Museums and the Performing Arts”, *Poetics*, 24, 1996, pp. 203-218; I. Nagel, M.-L. Damen, F. Haanstra, “The Arts Course CKV1 and Cultural Participation in the Netherlands”, *Poetics*, 38, 2010, pp. 365-385.

²⁰ L. Bonet, F. Colbert, A. Courchesne, “From Creative Nations to Creative Cities: An Example of Center-Periphery Dynamic in Cultural Policy”, *City, Culture and Society*, Vol. 2, No. 1, March 2011, pp. 3-8.

²¹ R. Florida, *The rise of the creative class. And how it’s transforming work, leisure, 2000.*

4. Second Challenge: The Limits of the Jury of Peers System of Arts Councils

In countries using the “jury of peers” system to make decisions on who will benefit of a grant from the subsidizing body, be it an Arts Council like the one used in the former British colonies (in Canada, New Zealand or Australia for instance) or ministry of cultures, every one notice the influx of new artists or arts organizations applying in greater number each year; parallel to that, the proportion of recipients diminishes if no more money is devoted to the programs. Officers from those grant givers must try to explain the reasons why support is denied to a greater number of complaining people.

The work imposed on the arts council by the jury system is tremendous. Each artistic discipline has its different programs (emerging artists, emerging companies, projects grants, established companies, etc) and for each program a jury is formed. This means dozens of juries and thousands of peers involved every year.

No system is perfect and the one based on juries is not either. In some jurisdictions, every company is judged by the same jury, a new organization as well as a long established one. The notion of equality among everybody was put forward to explain this way of making decisions about grants. This procedure may have been adequate when the sector was in the beginning of its expansion with a few established companies and a lot of new ones. After thirty or forty years of life and successes on a now very sophisticated market, one can the question, like Jacques Rigaud did in 1991,²² whether considering everybody on the same ground is the way to go; one can also propose that if a jury system is useful for a new venture, something beginning, for a mature sector or company, another system should prevail. After forty years of artistic success, the question may not lie anymore on measuring the capacity of an artistic director to conduct a successful season, but it lay on the capacity of an organization to maintain its artistic mission. Maintaining a mission becomes a matter of governance of an artistic organization; the protection and valorization of the repertoire of an artist is of prime importance.

One other problem that can be encountered with the jury system is on defining the concept of quality on which an artist or a company will be judged. In lots of jurisdictions, artistic quality is the main measure to allow a grant. The juries tend to define the “quality of a work of art” as the amount of innovation proposed by the artist in its work, and innovation must be pushing always further the idea of “transgression” in a work of art; on the final, it gets to consider the transgression of the “transgression” as the deliquescence of quality. In other words, preaching for small elite of converted is what is valued. It certainly is very good for the

²² J. Rigaud, “Synthèse de clôture”, *Pouvoirs publics et politiques culturelles: enjeux nationaux*, sous la direction de Mario Beaulac et de Gérard Grandmont, Actes du colloque, Montréal, 17-19 octobre, 1991.

development of a discipline but may let behind the average consumer. Some will say it is to future generations to judge of the importance of a work of art; doing this is asking the current generation to take the risk and the investment implied by creation for a potential appreciation by some future one.²³ Excellence defined as a permanent research for innovation in content and form may be appropriate for some limited number of art organizations or for those artists with great talent or new in the system. Quality of execution, valorizing the repertoire, financial stability and reaching new public should be the mission of most mature companies. The same requirements for all cannot stand in a mature field. If peers cannot refrain to use a short definition of artistic excellence, then may be mature companies who demonstrated constant quality should be judge along a different system. A country like Australia decided some years ago to go this route withdrawing the major organizations from the Australian Arts Council umbrella and giving the responsibility to funding to the appropriate ministry.

5. Third Challenge: Continuity and Succession at the Top

Lots of cultural organizations created in the 70's and the 80's won the challenge of continuity, success and financial stability. Among them, some have changed administrative director or artistic director. Those artists who founded an artistic company and are now in their sixties are like entrepreneurs. They know somebody will have to eventually assume their succession, but this moment always seems far ahead. In United States, Merce Cunningham, the famous choreographer, has planned his departure. He created a Trust to administer his body of works and he is retiring soon preparing in the meantime an orderly closing of the company he founded. Dancers and administrative staff will be dismissed in proper and human order (1).

Unless industrialized countries suddenly face a boom in their population and in their general wealth, the oversupply of cultural products will remain, only aggravated by new and emerging artists and companies eager to find a place on the market. Basic questions must then be raised: should all cultural organizations be kept? At what moment in the career of a successful artist does the preoccupation of a harmonious transition should be considered? Are there instances where the body of artistic work must be protected but not the company it was created for the production of those creations? Who will be responsible to make this repertoire live? Is it necessary or a good thing that new artists create a new structure to produce their work? Should it be the mission of some of the mature organizations? Would it be the time now to plan the future of those mature companies? It is better to prepare now than wait until the current leaders pass away?

²³ Ph. Urfalino, "Les politiques culturelles: mécénat caché et académies invisibles", *L'année sociologique*, No. 39, 1989, pp. 81-109.

The case of a leader passing away happened in Canada with the Jean-Pierre Perreault Dance Company. The founder and choreographer died before any plan for succession was prepared leaving the company in despair. Arts Councils and ministry of Culture must ask themselves those important questions. Getting organized, asking the proper questions and focusing on the most important thing to do is a shared responsibility of the arts organizations and of the funding bodies.

Not only aging artistic directors will have to be replaced in the coming years, a good proportion of managers at the top are also reaching an age where retirement is or must be envisaged. A generation of managers accompanied artistic entrepreneurs, some were present at the foundation of the organization. Again as a governance question, it is better resolved when plans are prepared ahead of time instead of letting things go by themselves until problems that could be foreseen are rising.

6. Conclusion

The current situation in the arts implies a continuous increase of companies on the market that creates a situation impossible to sustain in the long term, especially when we know barrier to exit still continue to prevent a healthy evolution of the field. Governments, citizens/consumers and even the private sector (especially in North America) can no more increase their expenditures in the cultural sector by a large means. The State as well as provinces, regions or municipalities are looking for additional sources of revenues but the taxpayer is no more willing to assume the invoice. When population is aging and health care is eating up an always higher proportion of government budgets, the arts may seem a frill to a lot of citizens. The challenge of maintaining a vivid and creative artistic milieu in a saturated market is real and not easy to meet. To ignore it and to not rethink the model of funding the arts and culture imagined 50 to 60 years ago may mean troubled water for the future. All this aggravated by the necessity of a change at the top of companies both at the artistic and at the administrative levels. Lots of successful arts organizations must now be regarded as precious heritage, but not necessarily their legal structure, but definitely their repertoire.

Note 1: For example, among Contemporary Arts Museums' visitors, 90% to 95% of patrons got a university degree.

Note 2: See: <http://www.merce.org/>

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PROFESSOR J. DENNIS RICH, PHD*
Columbia College Chicago, USA

BAUMOL'S DISEASE IN AMERICA

Summary

In 1966, William J. Baumol and William G. Bowen published *Performing Arts – the Economic Dilemma*. Subtitled *A Study of Problems Common to Theater, Opera, Music and Dance*, in which they assert that for the performing arts in America, crisis is a way of life. Since that time, the economic basis for this crisis has come to be called “Baumol’s Disease.” This paper examines the question, how pervasive is “Baumol’s Disease” in the American Performing Arts. It reviews the “income gap” situation in theatre, orchestral music, dance, and opera over 40-year period. The essay examines reasons why “Baumol’s Disease” continues in America and how it presents both an artistic and managerial challenges and, at the same time, offers opportunities for the performing arts to flourish.

Key words: performing arts, income gap, “Baumol’s Disease”, art funding, earned and contributed income

JEL classification: H81, Z11

In 1966, William J. Baumol and William G. Bowen published *Performing Arts – the Economic Dilemma*. Subtitled *A Study of Problems Common to Theater, Opera, Music and Dance*, the book begins with the statement that “In the performing arts, crisis is apparently a way of life.”¹ In their important work, Professors Baumol and Bowen described a situation in which the productivity of the general economy has risen, historically, at a compound rate of 2.5 percent per year, thus doubling labor productivity every 29 years. At the same time, the productivity of the performing arts has risen very little. Today, just as in Mozart’s time, it takes four instrumentalists to play a quartet. *Hamlet* still requires nineteen actors; and orchestras require 70 or more players to perform, as they have for years.

Nonetheless, and not unreasonably, artists expect their incomes to rise with the rising general standard of living. Since arts productivity is rising slowly or not at all, arts organizations are unable to meet their expenses from earned income. The dynamic of slowly increasing productivity and rapidly increasing

* E-mail: jdennisrich@gmail.com

¹ W. J. Baumol, W. G. Bowen, *Performing Arts – the Economic Dilemma*, The M.I.T. Press, Cambridge – Massachusetts – London, England, 1966; reprint 1967, p. 3; reprint 1967.

costs has created what Baumol and Bowen called the “income gap”² and later “cost disease.”³

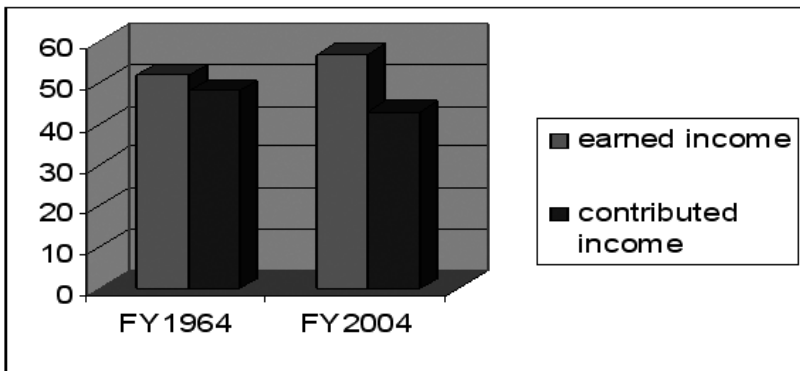
An understanding of this “gap” helped to give rise to both non-profit institutions (especially in the United States) and to arts management as a profession. Professors Baumol and Bowen observed that the income gap is almost universal in the non-commercial performing arts and that financial pressures created by the income gap can be a significant threat to the quality and scale of operations in performing arts institutions.⁴ Further, the economists suggest that in the United States, “these financial pressures are here to stay, and there are fundamental reasons for expecting the income gap to widen steadily with the passage of time.”⁵ Add to this the fact that in the performing arts, government subvention has been minimal, totaling 5% or less of contributed income.

So why not simply raise prices to keep up with costs? Messrs. Baumol and Bowen identify three factors that prevent this:

- 1) the disinclination of individual arts organizations to raise their prices, on moral grounds;
- 2) the place of the arts in the ticket purchaser’s hierarchy of necessities; and
- 3) the forces of competition.⁶

Over the years, Baumol has repeatedly advocated for alleviating, if not curing “cost disease” through higher subsidies for the arts.⁷

Figure 1: *Source League of American Orchestras*



² Ibid., pp. 150-157.

³ H. Abbing, *Let's Forget about the Cost Disease*, verzija iz jula 2005; <http://www.xs4all.nl/~abbing/>

⁴ W. J. Baumol, W. G. Bowen, op. cit., p. 154-157.

⁵ Ibid., pp. 161-162.

⁶ Ibid., p. 172.

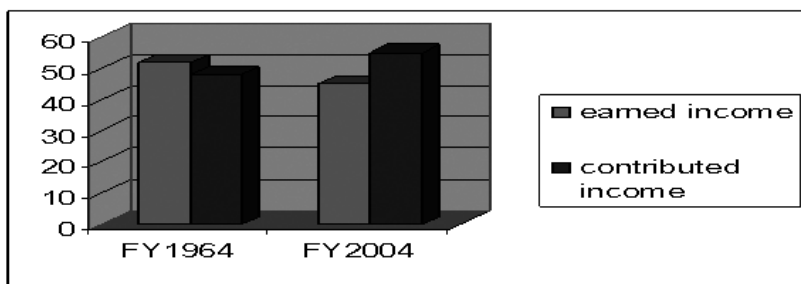
⁷ H. Abbing, op. cit., p. 5.

A key question is whether Professors Baumol and Bowen were correct in their prediction that the income gap, as a percentage of expenditures would continue to widen.

The chart in Figure 1 shows that over a forty-year period, the amount of earned income actually increased from 52% to 57% if one includes endowment income. If you do not count endowment income, the chart shows 45% earned and 55% contributed – still not the “steadily widening income gap that the authors suggest should have occurred over a 40 year period. And, despite the economic downturn, little has changed from 2004 to the present.

Even more interesting, the number of professional orchestras in the United States grew to 350 over the more than forty-year period. Over the past twenty years, of 350 professional orchestras, seventeen were forced to cease operations, a failure rate of 0.2% per year. Still, the Philadelphia Orchestra recently declared bankruptcy. The Detroit Symphony Orchestra is emerging from a bruising, six-month strike, and the orchestras of Honolulu and Syracuse have folded in recent months. Many communities are left wondering, “what’s the prognosis for my local symphony?” Historically most of the communities that lost their orchestra revived it or started a new one⁸.

Figure 2: Source League of American Orchestras
Contributed vs. Earned Income for Orchestras (endowment income viewed as contributed)



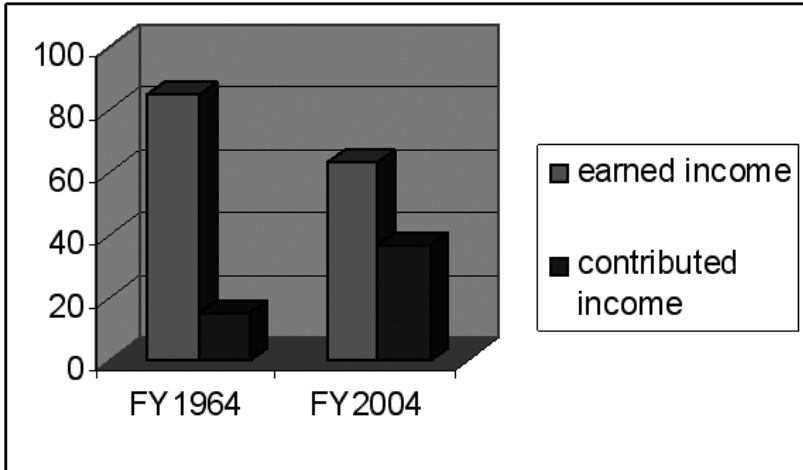
Until recently, it appeared that “cost disease” was in remission. Nationwide orchestral operating revenue rose 8% while expenses rose 7% and orchestral deficits dropped from an average of 2.7% in FY 2002 to 1.1% in FY 2004. However, in 2005, the average orchestra deficit was \$193,000. Just four years later, in 2009, it had skyrocketed to \$697,000. In 2008, 50% of American orchestras reported deficits; the very next year, 2009, that number had increased to 70%.⁹ With the weakened economy, Baumol’s disease seems to be back and stronger than ever.

⁸ Facts and figures regarding symphony orchestras are from the American Symphony Orchestra League’s *Music Matters* available at their website <http://Symphony.org>.

⁹ “Orchestras at a Crossroads,” by Jesse Rosen in Polyphonic.Org, <http://www.polyphonic.org/article.php?id=249&page=1>, accessed on November 1, 2011.

The state of non-profit theatre in the USA suggests that Baumol and Bowen were right when they wrote and are still right today.

Figure 3: Source TCG. *Earned vs. Contributed Income for Theatres*



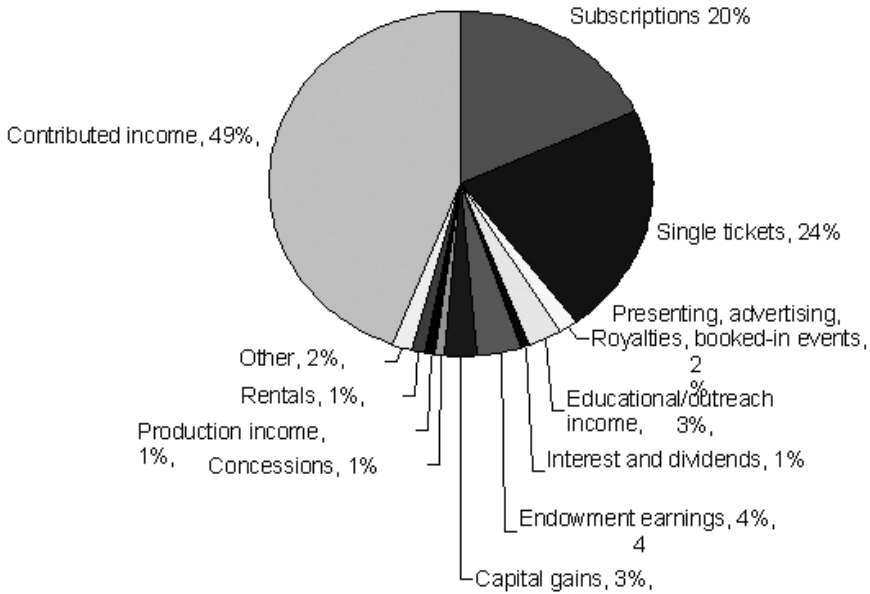
In 1964, the income gap was about 15%; today, looking at TCG trend theatres, the gap is 45%.¹⁰ Still, the number of professional theatres operating in the US has increased substantially over the last forty years. Since 2004, earned income has hovered around 60% of budget. However, if all income is considered, we see that a typical theatre had income from all sources of more than 100% of expenses – even in a difficult economy – a generally healthy condition. This suggests that American theatre managers and governing boards have understood and responded effectively to the income gap.

A distressing trend is the movement towards single ticket sales as the largest source of earned income. Despite an increased income gap, the overall income picture suggests that the theatre in the USA continues to be healthy. During FY 2010, the industry contributed an estimated \$1.90 billion to the economy in the form of direct compensation and payment for services and goods. The research indicates that 31 million patrons attended the theatre and that 119,000 artists, administrators and technical personnel were employed.¹¹ At the same time, it should be noted that the salaries of artists have not kept up with salaries in other sectors of the economy.

¹⁰ Theatre Facts 2004. TCG.org and Theatre Facts 2010, TCG.org.

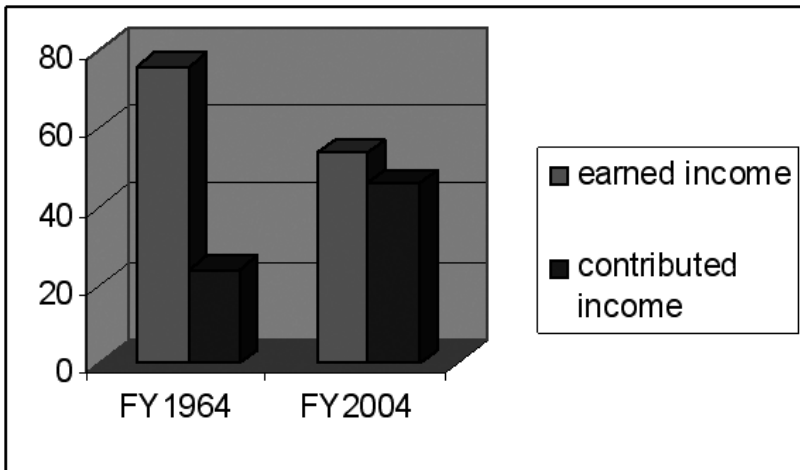
¹¹ Theatre Facts 2010, p. 5.

Figure 4: Theatre Earned and Contributed Income¹²



The condition of Dance is also interesting.

Figure 5: Earned and Contributed Income for Dance



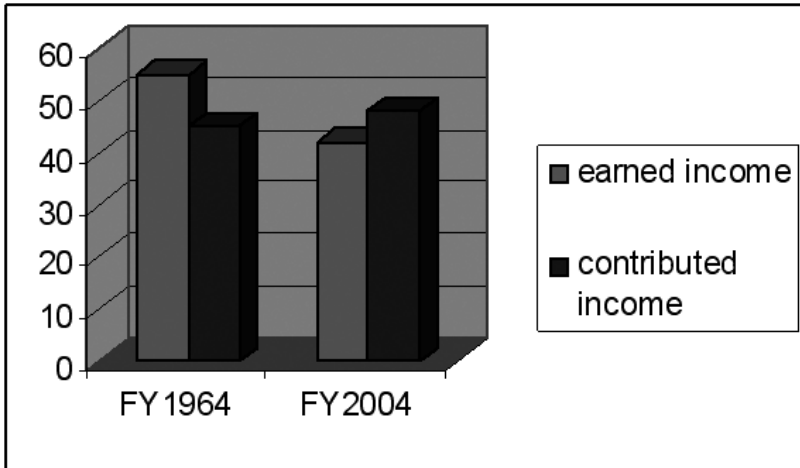
Source: Dance USA

¹² Theatre Facts 2004 and 2010.

As with theatre, the gap has increased over the forty-plus year period since Baumol and Bowen discovered the “disease.”¹³ What the data reveals is that volunteers most closely connected with a dance organization are also the biggest contributors with contributions growing by 69% in the five-year period between 1994 and 1999. Earned income has decreased since 1964, and has held steady at around 50% of budget, with 34% coming from ticket sales.¹⁴

Opera seems to be the only performing art that brings in much less earned than contributed income. In 2002, opera attendance figures show that 6.6 million adults attended at least one opera performance.¹⁵ During the 2009-2010 season, 6.7 million adults attended at least one opera.¹⁶ Here, it would appear that “Baumol’s Disease” is rampant, but there are now 122 professional opera companies in the US and the audience continues to diversify with 11.5% of the opera audience representing ethnic minorities. The opera audience and industry is, despite the income gap, slowly growing.

Figure 6: *Opera Earned and Contributed Income*



Source: *Opera America*

So what does it mean overall? Clearly, the earnings gap is still here and still substantial. While the number of Americans attending live performances has increased in recent years,¹⁷ pay for artists and job security have scarcely improved

¹³ Facts and Figures: Snap Facts March 2004: Field at a Glance – Dance, Danceusa.org.

¹⁴ Facts and Figures: Snapshot of the Field (prepared February 2011) - Field at a Glance -- Dance,”Danceusa.org.

¹⁵ “Quick Facts About Opera,” Operaamerica.org

¹⁶ “Quick Facts About Opera,” Operaamerica.org

¹⁷ “The Performing Arts: Trends and Their Implications,” Rand Research Brief from *The Performing Arts in a New Era* by Kevin McCarthy, et al published by Rand – see <http://>

since 1970. Performing artists continue to dedicate themselves to their art despite this fact. Indeed, many may be counted among the projected 67% of Americans who participate in unpaid hands-on arts activity.¹⁸ So, one reason why the “disease” is rarely life threatening is because arts organizations have managed, to some extent, to control costs. Moreover, if we look at the income gap over time, it appears to fluctuate – sometimes increasing and sometimes decreasing, but never going away.¹⁹

There is a good deal of evidence that some measures undertaken to control cost disease have been at the expense of quality or at least at risk to the quality of performance. These include²⁰:

- 1) Reducing real wage growth
- 2) Choosing productions or pieces that require fewer artists and/or fewer scene changes
- 3) Hiring fewer guest artists
- 4) Avoiding new works to avoid royalty payments to creators
- 5) Cutting Rehearsal times
- 6) Developing productions in low-cost locations
- 7) Producing lavish programs featuring celebrity artists to attract large audiences (blockbusters)
- 8) Producing familiar, traditional programs (“warhorses”) designed to attract large audiences (the “Nutcracker” strategy)
- 9) Tying primary programming to sales of auxiliary products such as T-shirts, collectibles, etc.
- 10) Increasing the number of performances of the same production
- 11) Maximizing the audience per performance by increasing the size of performance venues
- 12) Targeting niche markets that have predictable, loyal audiences
- 13) Financing productions jointly with firms in the for-profit and nonprofit sectors collaborating
- 14) Adopting commercial financing techniques in the non-profit sector such as for-profit subsidiaries or charitable component funds.

According to the Pew Charitable Trust, the income gap is very much present among the American performing arts and nonprofits are subject to the whims of donors and the pressures of the market place. These pressures have increased since the 2008 economic crisis. Still, these very factors may be not only a challenge but also strength.

Rand.org/pubs/research_briefs/RB2504/index1.html.

¹⁸ Informal Arts: Finding Cohesion, Capacity and other Cultural Benefits in Unexpected Places, Research Report to the Chicago Center for Arts Policy at Columbia College, June 2002.

¹⁹ “Financial Situation of Performing Arts Organizations,” Pew Charitable Trusts.

²⁰ *Ibid*, p. 92.

One of the realities of the performing arts in the United States is the diversity of funding sources. Closing the income gap through the generosity of *multiple* funders reduces the concentration of government power and the power of any single funder over the practices of a particular arts institution. A strong private support base gives American arts institutions a freedom of action they would not have if they were dependent upon the government for their funds. It is one of the safeguards in the system guaranteeing artistic freedom.

In addition, because US arts agencies rely so heavily on fundraising, they must cultivate donors' attention and goodwill. The philosophical argument continues, "This means a broader constituency for the arts," and, because of the backing of donors, the artist remains relatively free from the commercial distractions of the market place.

However, the need to cultivate donor good will has meant that as arts institutions grow in the US, they tend to become more conservative. Outside of major US cities, the conformity of repertory increases with institutional size as measured by operating budget and size of house.²¹ While patronage *may* contribute to an institution's financial success, it would appear that it also limits creative opportunities. This situation exists in most cities where, for example, there is only one major theatre.

In larger cities, the market place is not necessarily a commercial force that challenges artistic freedom and pushes towards the greatest aggregation of cultural consumers. When multiple theatres are present (as they are in my city of Chicago, for example), the competition between them seems to encourage creative innovation. In such a situation, competition encourages differentiation as a competitive strategy.²² Not surprising, this suggests that arts agencies in larger markets are less risk averse than those in smaller markets.

It also suggests that Baumol's disease, if it is a disease, is harder to understand than it would first appear. Today, it would appear that large organizations have learned how to treat the "disease" and very small ones are essentially immune to the malady. It is medium sized performing arts institutions that seem most likely to suffer from the consequences of the income gap. That was true in 1964 and remains true today.

If one extends the income gap and "Baumol's Disease" to the entire service sector of a nation's economy – hospitals, public schools, law enforcement, etc. – one can see a difference between all services and the arts. To keep providing the same quality of service to citizens, government needs to raise more money through taxation. Consumers have resisted such increases giving rise to the idea that the "disease" is political. Citizens pay more in taxes, but get only the same

²¹ P. DiMaggio, K. Stenberg, "Why Do Some Theatres Innovate More than Others? An Empirical Analysis", *Poetics*, 14, 1985, pp. 107-122.

²² *Ibid*, p. 116.

service they have always received in return. As a result, citizens express concern and see government as bloated and inefficient.

For the performing arts however, there seems to be an understanding of the need for support beyond ticket purchases. Perhaps it is not a disease but a condition, like a special child in need of extra attention. The performing arts always operate under financial strain, but with a little help from their friends, they continue to produce wonderful artistic product. If Professors Baumol and Bowen were correct in the diagnosis, American managers and governing boards have found effective treatment.

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ASSISTANT PROFESSOR SMILJKA LJ. ISAKOVIĆ, PHD*
Graduate School of Culture and Media, Megatrend University, Belgrade

SERBIAN CULTURE AND ART – WHERE ARE WE AND WHERE ARE WE HEADING?***

Summary

With the adoption of the Law on culture in 2009 a legal basis for more coherent and functional activities in culture and art was created. Serbia still has a decent cultural infrastructure inherited from the previous period, as well as material and human resources that neither transition nor economic crisis managed to destroy. Cultural institutions are still functioning, while audience participation is reduced at the level of global phenomena. The system of financing culture relies mainly on the public sector, while cooperation with the private sector is yet to be developed. So far, the most vulnerable is international cooperation, while the quality of cultural offer and artistic activities are still at a high level. In order to relieve budgetary expenses for culture and art, it is necessary to strengthen the informal networks and cooperation among sectors, i.e. the partnership of all three sectors: public, private and civil society, with clearly defined high artistic criteria.

Key words: culture, art, resources, institutions, partnerships, strategy

JEL classification: Z11, H44

1. Introduction

The new Law on Culture came into force on September 11 2009. It created the legal basis for defining the strategic direction of cultural development of Serbia. Being a factor with the majority of material resources, the public sector in Serbia has the greatest abilities to finance arts, with the aim of enhancing the spiritual and social condition of the nation. It is not easy for the state in the current global economic crisis to finance what belongs to the superstructure or, as it is called, 'consumption'. Several years ago, in 2008 to be more precise, the proposal of the

* E-mail: smiljkais@gmail.com

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Ministry of Culture that the budget funds for culture be increased from 0.76 to 1%, was unanimously supported by the Committee on Culture and Information of the Serbian Assembly. The joint position of the Committee and the Ministry was that, apart from the budgetary support, it is important to stimulate other forms of culture financing, such as tax incentives for donors and sponsors of cultural events. The duty of the state was also underlined concerning the improvement of the position of the artists important for our culture, as well as promoting our culture more over the world. However, of all the proposals almost none was carried out completely, some did not even start, and some will remain only on paper - as proposals. The reasons are varied and they will be discussed in this paper.

2. Cultural infrastructure and the resources

The Republic of Serbia and the City of Belgrade have a general interest in culture, performing cultural activities, but also providing conditions for work and performance to all participants in the culture through their agencies, the Ministry of Culture of Serbia and the Secretariat for Culture of the City of Belgrade. Its foundation is made of material and human resources.

Material resources are not negligible. Theatres, concert halls, cultural centres, monuments and space used for music and performing arts are equally valuable and functioning like anywhere in the world. All of this is the legacy of past generations, left for the future, 'to the benefit' of us all. There was never a problem of 'where', but 'who' and 'how'. Human resources consist of artists, organizers and the audience.

Artists. If a man is the foundation of any organization, it means that the human factor is important for the success of any organization up to 80 per cent, while all other resources cover 20 percent. In the new millennium, people and their knowledge and skills in the first place make the capital of companies. Serbia has a large capital in artistic resources, artistic performers in music and stage arts. National music school system is still at a very high level and that is where we can compete with most developed countries – the education of artists meets high professional and artistic requirements. The largest number of Serbian artists is organized in professional art associations.

The Ministry of Culture, in accordance with the provisions of Article 2 points 3 and 13 and Article 4 of the Law on the Activities of General Interest in Culture ('Official Gazette of RS', no. 49/92) and the Budget Law of the Republic of Serbia for 2008 ('Official Gazette of RS', no. 123/07), and within its curriculum, provides funds for the work of republic art associations, that is for the realization of their programs in terms of achieving basic objectives for which the associations were founded. A bit more than 1000 music artists, composers and performers are members of professional musical art associations (member-

ship criteria are professionally very strict), although this number is relative and fluctuates from year to year. The Association of Musical Artists of Serbia has 450 members, the Association of Serbian Composers approximately 400 (according to SOKOJ Agency records, while 241 composers protect their rights through the Agency), the Association of Orchestral Musicians about 150, and the Association of Ballet Artists of Serbia more than 120. Only when the final lists of representative artistic associations is determined through fields of activity, more specific information regarding membership can be discussed. These figures do not include all those musical artists and authors of various ages who are not listed any records of professional arts associations. This number probably exceeds several thousand, and as unrecorded, this figure is not used in the activities of cultural policy of Serbia.

What is more, a unified database of chamber and symphony orchestras, operas and ballets of Serbia does not exist. Of the great classical music orchestras in Serbia the following are currently functioning:

- Belgrade Philharmonic Orchestra
- RTS Symphony Orchestra (as a part of RTS music production there are the following: a Large National Orchestra, the National Ensemble, Mixed and Children's Choir, the 'Kolibri' Choir and the 'Big Band')
- Symphony Orchestra of the 'Stanislav Binički' Artistic Ensemble of Serbian Army (Belgrade)
- The National Theatre Orchestra of Opera and Ballet in Belgrade
- Nis Symphony Orchestra
- Vojvodina Symphony Orchestra (Novi Sad)
- The Orchestra of Serbian National Theatre (Novi Sad)
- The Symphony Orchestra of Novi Sad Academy of Arts and Belgrade Faculty of Music Arts
- The 'Borislav Pascan' Youth Symphony Orchestra (Belgrade)
- Camerata Serbica (Belgrade)

The number of employed musicians in the orchestras varies. For example, in the Belgrade Philharmonic Orchestra there are 98 of them, while the management, production, technical service and the secretariat employ 20 people, including the director, art director and conductor. This number of orchestral musicians meets the needs of a large symphony orchestra repertoire from Baroque to contemporary music, but it is unattainable in other orchestras because of the financial support provided to BF (Belgrade Philharmonics), as a cultural institution of national importance, by the Republic and the city. Chamber orchestras perform mainly in Belgrade (the 'Dusan Skovran' Orchestra, 'St. George String Orchestra', 'Ljubica Maric Orchestra'...) and are often assembled to meet the need of a particular project. Often the same musicians perform in these ensembles, whose dissatisfaction is often initiated by the unfavourable situation in the art music

and extremely low wages in this area. The same remarks apply to the musicians in major orchestras.

Organizers. In contrast to the high level of artistic musical supply, the level of transmission, organizers, managers in art, who should organize musical life in Serbia at the same level and send local artists abroad at the relevant artistic and organizational level, is not satisfactory. The result of negligence towards the artists was the draining of mainly young people abroad, where they were able to more successfully develop and market their potential. To stop the artistic 'brain drain', it is necessary to make an effort to create a better organization in the arts.

At the time of Yugoslavia, before the nineties of the previous century it was the government that financed art at home (Self-managing Interest Communities of Culture, SICs), as well as promoted our art on the international scene. While the tours of our solo singers and ensembles took place according to inter-state agreements, the 'Jugokonzert', a state concert agency realized in practice what had already been signed at the state level - and everything functioned perfectly well. Big markets knew about us, and appreciated our artists and ensembles. By disintegration of the country, entering the transition, and especially losing the stable bilateral ties, after 2000 Serbia faced a lack of organizational structure quality in the arts, which became even more obvious when the state financial support weakened. Real managers in arts do not exist, because in Serbia, as a rule, 60 per cent of the budget is spent on the employees' salaries, 20 per cent on material costs, and only 20 per cent on the programs¹. The directors of cultural institutions are appointed according to party affiliation, so that only now do we begin to appreciate the positive achievements of the past (the SICs, where there was an open competition for the appointment of directors, as well as the systematic adoption of the plans for the development in culture). It was a model of the state cultural policy ('at arms' length'), in which the organizations that put to effect the decisions made at the state level, were delegated by the public administration to do so.

Human resources in culture, need to be constantly educated, trained at new levels of knowledge in music culture, global trends in the organization of the arts (a complex system of marketing, fund-raising, management), as well as the sense of cultural needs, from local to general communities. This should be the task of public administration, the Ministry of Culture and the Secretariat of Culture of the City of Belgrade and other local public administration bodies, in cooperation with NGOs, foundations and all relevant stakeholders of the cultural life of Serbia. It should never be forgotten that music, culture and arts are production, and not consumption.

¹ The research of local cultural policies, ZAPROKUL 2010.

3. Institutions

The organizations in the sphere of culture are in charge of the realization and presentation of music as a public event (opera, ballet, concerts). It can be individual, a part of a music festival, or a music competition. These organizations may have the status of established institutions or may be formed if necessary (for a project). Therefore, the organization of musical events may be institutional and project (festivals, competitions and individual events).

The organization (the host) which sets or enables an event in music and stage arts, may be a state institution, non-governmental organization, corporation, social and / or socio-political organization, or a profit company, run by a manager: private (profit oriented) sector, governmental sector and non-profit (voluntary) sector. In Serbia, since private sector is still underdeveloped to invest in arts, it is mainly the government sector that deals with art events organization. The exception is private 'Madlenianum'.

Institutionally, in the public sector, the Ministry of Culture of Serbia, as the biggest and most important factor, deals with the realization of cultural events, (Belgrade Philharmonics, The National Theatre). In Belgrade, a network of cultural institutions / institutions of importance for the city, whose work, realization of programs and premises maintenance is financed (partially or completely) from the budget, comprises the theatres (except The National Theatre), The 'Jugokonzert' Agency, Youth Club, Children's Cultural Centre, museums, libraries and cultural centres, as well as two public companies in the field of culture (The 'Sava' Centre and The Belgrade Fortress). Music and ballet schools, The Cultural and Educational Community of Serbia, and Musical Youth of Serbia and Belgrade are also institutionally involved in the music activities.

4. The project forms (project and / or event management)

The project forms of presentation such as festivals, competitions and individual events, appear as independent projects of musical and theatrical events within the institutional form, or independently.

Festivals. Today's festivals (theatre, dance, opera, concerts) are attractive in relation to the annual concert-opera seasons because of their limited duration and attractive programs concentrated in one place. Therefore what is extremely important is the profile and identity of the festival, as well as originality (which sometimes goes at the expense of real aesthetic value!) that defines the audience and the very attendance. Ideally, festivals should be included in tourist, economic and cultural policy and the offer of the local communities, at the same time taking care of the artistic needs of the local population, which in our country, with rare exceptions, does not participate in festival activities. Before setting

up a new festival in any field, one should ask *why, for whom and how* it should be established, because any investment in new projects should be a source of dynamism in the local economy (jobs, incentives for further cultural development). A well-designed and profiled festival becomes a *hallmark event* (an event that is identified with the essence and ethos of the village, town or region), a trademark of local cultural offer.

Festivals can be classified according to the location of event (indoors, outdoors), the time of the event (summer, winter, autumn), according to content (opera, ballet, choir, rock or pop concert, chamber, mixed), according to the style (old music, Baroque, Romantic and Modern Music), according to the authors (authors of domestic, foreign, contemporary, old music), theme - theme festivals (dedicated to a particular topic), and so on. A festival does not need to have strict guidelines. It can 'wander' in profiling, following the interests and artistic preferences of their selectors. The newly established festivals tend to suffer from the 'children's diseases' that accompany each new and unfamiliar music event. However, those that are with a long tradition may have the following problems.

- 1) Fatigue from continuous searching for and changing concepts (if there is no strategy at the beginning, and this usually happens). The music critic of the 36th Bemus Festival in 2004 compares a festival with a tired old man, because it 'runs silently and with a starchy attitude, encouraged by a sincere belief in the justification of a fifteen-year-old life, despite the deafening roar of half empty concert halls²'.
- 2) A festival looks like its selector, changing its profile with the change of the selector. This problem should be carefully considered, as there are still festivals in Serbia financed by the public sector, so that private preferences of selectors should not affect the prestigious, expensive and complicated musical events.
- 3) If a music festival is not well profiled or positioned from its inception, the audience inevitably becomes scarce (gets dispersed) during its long duration, though the mere audience is not the only infallible measure of quality; concert audience should be carefully nurtured, from an early age, and must have its own aesthetics. These issues - the public / education / aesthetics - should be paid more attention to, because they represent crucial points for the development and marketing of music and performing arts.

Statistics of cultural events in Serbia³ showed several years ago that the musical-theatrical events of importance, especially festivals with long history and have therefore become traditional, are concentrated in Belgrade, which is

² M. Smiljanić Radić, 'Festivali maraton', *Politika*, October, 12, 2004.

³ The Statistics (The Plus Factor Agency) is provided from Smiljka Isaković's doctoral dissertation: 'Interpolation of management in the field of music and performing arts', The Library of the Faculty of Culture and Media, Belgrade, as the appendix no.1.

their founder. So the city is loaded with events, while the highest artistic achievements cannot be seen in throughout Serbia. Therefore it is necessary to present festival events outside Belgrade. By means of statistical analysis conclusions can be drawn on cultural events, which are still topical. Events are mostly concentrated in May, June and October, the most frequent ones are visual arts, then music and theatre. Unfortunately, only one event the subject of which is cultural heritage was registered. Events are usually located in large cities, although, less frequently, they are located in towns and villages. Most events belong to international type, then to the republic and province.

It is interesting that most events take place in Vojvodina (38.9%), followed by Šumadija and western Serbia (27.35%), then in southern and eastern Serbia (17.71%), Belgrade (13.49%) and in Kosovo and Metohija (2.53%)⁴. The most common founder is the city, than cultural institutions, and finally the Republic. A large number of events have quite a number of related activities, the most often being a catalogue and a monograph. There are no musical events accompanied by the recordings. They are mostly long, traditional events, the existence of which exceeds the limit of five years; then there are the events up to five years old and the youngest ones, of three years (in Serbia out of 157 there are only 8). New festivals have an obvious problem to consolidate on our soil, probably due to financial barriers.

This research is becoming a solid basis for future research, in which audience participation, attendance at events, media coverage, the quality of their production, etc. could be objectively defined. Surprisingly, from 2004 (when there were 157) to 2011 the number of cultural and entertaining events was constantly increasing. Currently there are more than 800, despite an acute economic crisis, the artistic level often being reduced.

5. The audience - participation in culture and development strategy

Any activity in culture and arts does not make any sense without audience. The essence of the impact of music on society is of aesthetic-artistic nature, ephemeral, and generally non-commercial, but it is a very important factor in the society development and the state should recognize it as a fact. Developing habits of the audience must be a planned process which deepens positive associations about the already experienced event. Dispelling the myth of the art of music as an isolated ghetto of the selected elite is the first step in establishing contact with a new audience, because the audience of the past with its habits is slowly disappearing; that is a worldwide trend. The aim of the true cultural strategy is to put as many people from the wider social, economic and demographic range as possible in contact with the art of music. With the organized media activity, dispelling

⁴ Data provided by ZAPROKUL 2011.

the myth of the elite and displaying art as the mainstay of a development of a society is certainly the basis for winning new consumers of musical culture. The audience is not a 'buyer', but a partner, and without restoring the auditorium and audience participation every artistic activity becomes utterly meaningless.

According to a survey on cultural values (research was conducted by the 'Faktor Plus' Agency for research and opinion poll in late 2007, by means of a telephone survey of a sample of 1000 respondents across Serbia)⁵, Serbian citizens do not have the developed needs for musical events of artistic, jazz and other 'elite' music. However, what is striking is the fact that the artistic music was marginalized in the very study, so that in question number 18 referring to the visits to music festivals only 'Guca' and 'Exit' were mentioned. That narrowed the choice of subjects only to a rock or turbo-folk festival, while all great music festivals were left out, such as Bemus, jazz festivals, and so on (the question: 'Do you visit or would you visit ...', the results were: 43.5% - Guca, 16.8% - Exit, 19.2% - neither of the two, 20.5% - both).

A specialized survey that explored cultural needs⁶, and dealt with the attitudes of citizens in terms of music and musical events (*Marketing Research Faktor Plus Agency*, 2005), examined the citizens' interest in music, their satisfaction with the current music events, concerts and festivals attendance, and their choice of the music genre. The survey analysis showed the following results:

1. Domestic audience:

- rare visit to concerts (74 %)
- never on a concert (46 %)
- pop music is mostly listened to (49 %), classical music is least listened to (5%)
- the guitar is a leading instrument, than the piano
- music is mostly listened from CDs, at home (inertness)
- awareness: the following festivals are the most known: Bemus, The Days of Mokranjac, Nomus and Nimus; Etnofest and The 'Mermer i zvuci' are little known of, The Guitar Art, Organ and Flute festivals are almost unknown!
- the presence at festivals is not bad (54 %)
- not exactly satisfied with the quality (yes; partially yes 59 %; dissatisfied 41 %)

Conclusion:

- 1) Inert audience (listens to music at home)
- 2) Uninformed audience (Belgrade festivals are unknown, as well as The 'Mermer i zvuci' after forty years of existence)

⁵ S. Isaković, *Menadžment muzičke umetnosti*, Megatrend univerzitet, 2010, p. 228.

⁶ The poll is taken from Smiljka Isaković's doctoral dissertation: 'Interpolation of management in the field of music and performing arts', The Library of the Faculty of Culture and Media, Belgrade. A total of 100 adult citizens were interviewed in Belgrade, by the field survey using a structured questionnaire on a random sample.

- 3) General quality of the offer does not satisfy almost half of the respondents
- 4) Good marketing does wonders (Bemus, pop music)

2. Cross analysis

Gender – female:

- attend concerts more;
- listen to music more;
- prefer the piano, than the guitar, etc. (men prefer the violin);
- know less on: the Bemus and Nomus Festivals, and The Days of Mokranjac;
- know more on: the Nimus Festival, The 'Mermer i zvuci' Festival, the Organ Festival and The Flute Festival...;
- attend festivals less;
- are more critical on the quality.

Conclusion:

- 1) Female population is more informed on festivals regardless of advertising.
- 2) Men are affected only by headlines (Bemus...).
- 3) Women are too occupied – despite having the information, they do not attend cultural events.
- 4) Women filter information on culture more.
- 5) Women are more romantic.

3. Age

Attendance is the weakest before 20 and after 50 years of age. The young:

- do not attend concerts;
- listen only to pop and ethno music;
- listen to the music only at home;
- have heard only of The Bemus Festival and The Days of Mokranjac;
- have not heard of other festivals!;
- do not attend the events (76,5 %);
- have divided opinions on quality.

Conclusion:

- 1) There is a total unawareness on general culture.
- 2) The imposed information (pop, ethno).
- 3) Disinterest in the events in Belgrade.
- 4) Disinterest in attending concerts.
- 5) Inertness regarding the issues of culture and arts.

4. Education

Secondary school:

- 1) Rare attendance (83,7 %) or none (16,3 %).
- 2) do not listen to the classical music, only pop and ethno.
- 3) listen to the music only on the recordings.
- 4) have never heard of 'The Mermer i zvuci' Festival
- 5) have only heard of The Bemus Festival and The Days of Mokranjac.
- 6) do not attend festivals.
- 7) are critical of the quality (!).

College:

- 1) often attend concerts.
- 2) are the only ones who mention classical music for listening.
- 3) like the violin.
- 4) listen to the classical music on the radio.
- 5) are well informed about the festivals, are the only ones to mention The 'Mermer i zvuci' Festival, The Guitar art Festival, and also The Ethno fest.
- 6) attendance of festivals higher than with any other group.

University:

- 1) the highest attendance of concerts.
- 2) are more informed about The Organ Festival than college educated people.

Quality evaluation: college educated people are most critical, than come those with secondary school education, while those with university education are the least critical.

Conclusion:

- 1) People with secondary school education are excluded from cultural events.
- 2) University educated people choose particular concerts, while college educated people choose events (festivals).
- 3) College educated people have the set criteria and demand quality.
- 4) University educated people are more tolerant.

5. Status

- 1) The employed listen to folk music most.
- 2) The employed prefer the violin.
- 3) The unemployed attend concerts more.
- 4) The unemployed attend more concerts than the employed.
- 5) The unemployed like the piano most, than the guitar.
- 6) The unemployed listen to pop music.
- 7) The unemployed attend festivals more.
- 8) The quality criticism is equal with both categories.

Conclusion:

- 1) The category of the unemployed is of higher quality than of the employed; those people have more free time (more of them responded to the survey, 64 %).

According to their influence on the audience the festivals have shown:

- 1) quality approach to management (The Bemus Festival, The days of Mokranjac, The Nomus and Nimus Festivals),
- 2) good, but insufficient, (The Ethno Fest, The Guitar Art Festival),
- 3) completely insufficient The 'Mermer i zvuci', The Organ Festival, The Flute Festival).

Conclusion:

Since the population surveyed is only from Belgrade, The Days of Mokranjac, and NOMUS and NIMUS festivals have conducted their propaganda more than well (Negotin, Novi Sad, Nis), together with The Ethno Fest (Zlatibor), while the weakest results are right here in Belgrade (The Organ and The Flute Festivals). The unfavourable marketing result of the 'Mermer i zvuci' festival (Arandelovac) is concerning because it is one of the oldest and best-quality cultural events in Serbia.

Directions and priorities in addressing the problem of audience participation are education at all levels. In Europe the RESEO organization (European Network for Opera and Dance Education) has been active for fifteen years, and is dedicated to promoting music and performing arts (opera, ballet) with the aim of animating the public. RESEO is a non-profit non-governmental organization, based in Brussels, which is financed by membership fees, sponsorships, various partnerships (FEDORA - the organization of associations and foundations supporting the opera houses and festivals), particularly educational institutions, as well as by participation in European cultural projects. Educational activities are carried out through talks, seminars, live performances, workshops, opera productions of the young, mostly 'on the field': in schools, hospitals, community centers ... At the moment its members come from over fifty opera and dance companies from twenty European countries. The 'Madlenianum' Opera is the only member from Serbia. RESEO functions through the annual conferences of its members, forums and websites, as well as printed publications that inform the members about news and activities three times a year. During the fifteen years of its existence RESEO initiated: programs aimed at training artists in different fields of art, so that a wider audience could learn about the music and performing arts in the best way; the music and performing arts repertoire for the young and by young performers; research on methods in which opera houses educate young audiences, educational projects and programs for teachers through which children and adolescents in and out of school approach top musical art, but also participate in creation; online database of music and performing works for young people, as well as data exchange between opera and ballet companies and ensembles in Europe.

The most interesting are the programs for school and preschool children (London, Barcelona). In Sweden, special art music programs are included in the school curriculum, while some projects deal with the beneficial influence of classical music in the prenatal period. By following this target group of children up to university, it was concluded that they are more successful in learning, socialization and general results ('The Mozart Effect').

6. The system of financing and general trends

According to the Law on Culture (Art. 74 to 78), culture can be financed from the budget and from other sources. Budget financing of culture is done in three ways:

- Financing of cultural institutions established by the Republic of Serbia, autonomous province or local administration, and whose programs are financed or co-financed from the budget of the founder in the amount determined by the founder on the basis of the strategic plan and the proposed annual working program of the institution. The program is submitted no later than 1 July of the current year for the next year. It contains clearly defined funds needed for program activities financing, but also for current expenditures financing.
- Budget financing of culture and other subjects in the culture, and not just of cultural institutions founded by the Republic of Serbia, autonomous province or local administration. It is related to the financing or co-financing of cultural projects on the basis of competition that the Republic of Serbia, autonomous provinces and local administrations announce annually. In this context the committees are formed to decide on the selection of projects. In exceptional cases Minister of Culture and the competent authorities of the autonomous provinces and local administration may finance important cultural projects apart from the competition, but only up to 25% of the planned budget for that year.
- Co-funding of current expenses and expenditures, which also does not only refer to the cultural institutions established by the Republic of Serbia, autonomous province or local administration, but also to others in culture. The conditions for this are that the interested party should submit a report on the five years' work, as well as the strategic development plan for the next five years; it should be a subject/institution that meets the cultural needs of citizens in a particular territory in a more permanent way; and the amount of funds requested should not exceed the amount of 45% of the total current expenditures and expenses for that year.

As for other (non-budget) forms of funding in culture, the law clearly states that it is the funding from revenues generated by performing activities of cultural institutions or other entities in culture, from fees for services, from sell-

ing products, assignment of copyright, legacies, donations, sponsorship, but also through the establishment and operation of foundations and endowments. Sources of funding, as a basic precondition for the development of activities in music and performing arts, can be of out-market nature (budget, subsidies), of market nature (concert agency) and a mixed type (non-governmental organizations, endowments, foundations, donors, sponsors).

The indirect budget beneficiaries (The National Theatre, Belgrade Philharmonic Orchestra, the 'Jugokonzert' Agency) are responsible for planning and implementation of their programs to direct beneficiaries of the budget (The Ministry of Culture and the Secretariat for Culture of the City of Belgrade). Regular financing involves material costs, employees' salaries, program activities, investments. In some institutions most of the money goes to the employees' salaries, without criteria, i.e. performance, while the program activities get a small amount of money, which is a paradox that should be corrected. Co-financing includes annual competitions for the projects of the Ministry of Culture, corporate support, individual donations, sponsorship, internal revenue (which are usually negligible). Currently there is no legislation to stimulate sponsorship and patronage in the form of fiscal and tax incentives for sponsors and donors.

Serbian Ministry of Culture provides funds from the budget to stimulate art projects and activities in art, and distributes them through annual competitions, which are usually launched in October for the next calendar year. Department of Artistic Creativity, Cultural Industries and Cultural Relations calls for tenders for the annual financing of projects / programs that contribute with their quality to the development and presentation of art and culture. The competitions are related to programs / projects in the following areas: theatre, music, theatre and dance creation, music creation, visual arts and multimedia, film, cultural and artistic amateurism, original folklore and the preservation of nonmaterial cultural heritage, programs supporting the youth culture, scientific research work and education in the arts and culture, literary programs, periodicals in the field of arts and culture, programs in Kosovo and Metohija and southern Serbia (Presevo, Bujanovac and Medvedja) and international cultural cooperation of importance for the Republic of Serbia. The competition also includes art colonies, workshops and residential programs for artists in these fields. Special attention is given to programs / projects that have: national significance, high artistic quality and contribute to the preservation of nonmaterial cultural heritage, promote alternative culture and new artistic forms and expressions, contributing thus to the decentralization of culture and intercultural dialogue. In all areas the priority is given to projects / programs aimed at children and children's creativity, the creativity of the young, as well as the people with special needs. The following have the right to participate in this contest: institutions, art associations and other organizations / entities, as well as individuals from the Republic of Serbia; this excludes the programs / projects of cultural institutions

under Article 2, paragraph 2 of the Law on the Activities of General Interest in Culture, i.e. 'indirect budget beneficiaries' (Belgrade Philharmonic Orchestra and The National Theatre).

From 2003 to 2008 the amount used for financing musical-theatrical arts through competition of the Ministry of Culture varied, as well as individual distribution (Table 1)⁷.

Table 1: Funding of music and performing arts - Ministry of Culture of Serbia

Year	2003	2004	2005	2006	2007	2008
Music	3,771,240	3,690,000	1,490,000	7,717,500	3,820,000	18,718,000
International cooperation	11,754,000	13,000,000	8,450,000	(together)	16,200,000	16,710,000
Dance	860,000	960,000	1,000,000	2,350,000	2,020,000	2,750,000
International cooperation			(together)	(together)	(together)	3,260,000
Young talents	-	-	200,000	772,000	Together with intern.	410,000
Total	16,385,240	17,650,000	11,140,000	10,839,500	22,040,000	41,648,000

Bemus (Belgrade Music Festival) has always had a privileged position. In 2003 it obtained 8,000,000 dinars (68% of the annual international cooperation in music), in 2004 it received 6 million (nearly half of international cooperation), and in 2005 that amount was 5,000,000 (60% of international cooperation). In 2006 it was not included in the distribution of the Ministry of Culture competition, in 2007 it received 8 million (50% of the annual international cooperation), while in 2008 again it did not appear in the contest because that year the Republic and the City of Belgrade signed an agreement on joint financing of the festivals of special importance to Belgrade, including the Bemus. The 'Jugokonzert' Agency, as the only state institution that organizes music and performing arts, although financed by the budget, participated in the competitions of the Ministry of Culture too:

- 2003 – 8,000,000 (Bemus), 600,000 (International Review of Composers)
- 2004 – 6,000,000 (Bemus), 300,000 (International Review of Composers)
- 2005 – 5,000,000 (Bemus), 1,500,000 (Musical links, the exchange with Sweden)
- 2006 – 500,000 (*Mozart, Lustre, Lustik*, international cooperation), 100,000 (solo arias of great opera composers)
- 2007 – 8,000,000 (Bemus), 500,000 (Collegium Musicum in Sweden), 200,000 (Isidora Žebeljan's night), 300,000 (Konstantin Babić's night)

⁷ The data provided by the Ministry of Culture.

- 2008 – 1,000,000 (The Cello Fest). Since then BEMUS has not been funded through open competition for projects⁸. As for making decisions on the annual competition of artistic achievements for the City of Belgrade, the competition results are not on the website of the City Council, and decisions are communicated in writing, which is not sufficiently transparent.

The Ministry of Culture, as noted above, within its curriculum, provides funds for the work of republic art associations, i.e. the implementation of their programs in terms of the realization of basic objectives for which the associations were founded. Republic Art Associations, at the request of the Ministry, supply information needed to determine the amount of funds necessary for the implementation of these programs. This excludes the Association of Folk Music Artists, which has informed the Ministry that the funds for its work will be provided from its own resources. Art Associations, which so far had only received funds through projects (concerts, awards), were finally included into the system of funding from the budget in 2008, although their status is still unresolved. It remains to be seen whether these will be non-governmental organizations, professional associations of citizens, or something similar to professional unions. Pursuant to Article 2, points 3 and 13, and Article 4 of the Law on Activities of General Interest in Culture ('Official Gazette of RS', no. 49/92) and the Law on Budget of the Republic of Serbia for 2008 ('Official Gazette of RS', no. 123/07), Minister of Culture decided to grant the funds in the amount shown in tables 2 and 2a to the republic art associations for the performance of regular activities for the period from January 1st 2008 to December 31st 2008.

Table 2: *Financing of artistic associations for 2008 – The Ministry of Culture (in dinars)*

The Association of Musical Artists of Serbia	487,995.00	487,995.00	487,995.00	487,995.00	Total 1,951,980.00
The Association of Orchestral Artists of Serbia	172,685.00	172,685.00	172,685.00	172,685.00	Total 690,740.00
The Association of Ballet Dancers of Serbia	487,995.00	487,995.00	487,995.00	487,995.00	Total 1,951,980.00
The Association of Serbian Composers	259,000.00	259,000.00	259,000.00	259,000.00	Total 1,036,000.00

⁸ Data provided by the Ministry of Culture.

The funds for the implementation of this decision are paid quarterly, every three months. The Department of Material and Financial Affairs of the Ministry of Culture controls the implementation of this decision. The distribution of funds for 2009, 2010 and 2011 is given in the following table:

Table 2a – Table 2 continued

UMUS	1,760,000
UOUS	630,000
UBUS	1,760,000
UKS	1,250,000/950,000

The Serbian Government Regulation on financing of the associations adopted in early 2012 should allow transparency in the allocation of funds from the budget and control of their spending. This supplements the Law on Associations passed in 2009 which equated all types of associations. What is new is that the participation of the associations of at least 51% of the total project value was omitted, and the criteria for the selection of programs to be funded are improved. As for the control of spending of the funds approved, besides the legal obligation to make available to the public the report on its activities and the extent and manner of acquisition of funds at least once a year, according to the Decree the associations will be under obligation to submit the report on the implementation of the program quarterly, but also after the program realization. The Regulation is important because most of the artists' associations, which starting from 2012 were given the status of representation, are financed by the state. However, due to the new political circumstances and the lack of cultural development strategy, it does not allocate enough funds for the civilian sector, to which many several decades old art associations belong (The Association of Musical Artists of Serbia, the Association of Fine Artists of Serbia, etc.).

The adoption of the new Law on Copyright and Related Rights in 2009 represents another attempt at financial security of artists. Starting from the fact that in practice the copyright, copyright holders' rights, as well as the related rights are collectively exercised, whose objects of protection are mass-exploited in every society (as is the case, for example, with musical works, phonograms and the recorded interpretations on them), the fees must represent a compromise between the private interests of the holders of these rights and the interests of society that exploits the objects of protection. In this sense, each implementation of the law must balance the competing economic interests and ensure a balance between private and public interests, so that the rights holders, under conditions of collective management of these rights, are properly compensated. As it usually happens in Serbia, the attempt at protecting the composers, compositions and performers also degenerated into its opposite. In the process of protecting intellectual property the organizations that currently 'protect' artists (SOKOJ, OFPS, PI) have required to

tax all the music used in any space, so that not only media could be taxed but also restaurants, taxi drivers, hairdressers, and even all the owners of mobile phones, because they contain the recorded music as well. Thereby experience shows that, as before, only a small part of so enormous revenue collected would find its way to the original authors, and the largest part would remain on the accounts of the 'protective' organizations, which do not use the money transparently. After a great struggle heavily covered by the media, in early February 2012, Serbian Government adopted draft amendments to the Copyright Law which abolishes the payment of 'musical dinar' for craftsmen-entrepreneurs using the radio, transistor or other device for listening to music in their workshops (barbers, shoemakers, car mechanics, beauty salons, etc.), as well as for PC and multifunction devices importers and manufacturers because these devices are not primarily used for playing music. The levy will be reduced three times for the others. Meanwhile the participants of the entire production process, the artists, authors and performers still watch the whole procedure from aside because they were completely marginalized both in the process of the law writing, and in its implementation.

7. Instead of conclusion: International cooperation, networks and partnerships (inter-sectoral cooperation)

What the world calls 'cultural diplomacy in the service of the interests of a country' is left to chance and mostly sporadic initiatives in Serbia. International cooperation in music occurs most often in the organization of the public sector (The Ministry of Foreign Affairs, The Ministry of Culture, regional and local administration), but without any coordination. This does not include individual performances of our artists abroad, which are numerous, but also without real records that would enable us to say that they affect the image of the world about us. Performances of foreign musicians here are also left to chance and private criteria, generally without the partnership reciprocity. It is necessary to establish a base of representatives of Serbia in the world, and all three sectors: public, private and civil must establish the database, with clearly defined highest artistic criteria.

It still cannot be talked about the network and networking in music, because the civil and private sectors still do not have the power to make a partnership with the public sector in forming the music network in Serbia. Barriers to inter-sectoral cooperation may be the fear of commercialization and loss of identity (public sector), slowness and sluggishness of the public sector administration in the implementation, and lack of transparency and serious preparation (private and civil sectors). The barriers are also an adverse effect of policies on the selection of personnel, poor information, lack of trained personnel, insufficient awareness of the need for cooperation, as well as lack of procedures for this cooperation⁹.

⁹ Justat Centar, 2007.

There are opportunities and they must be exploited as soon as possible, because no where in the world is the public sector able to financially support the cultural development of the country as a whole, especially after the economic crisis of 2009. The real opportunities lie in training and exchange of personnel and better mutual information, knowledge sharing, but also in economic stimulating actions, such as the legislative framework that regulates tax incentives. The public sector must be prepared to share responsibility with the private and civil sector in a transparent partnership. It is in such a partnership that the private sector, donors and sponsors see the improvement of the image, but also a spiritual investment in the country. Individuals or companies decide on sponsorship for various reasons: to improve their identity through the impact on target groups, to be involved in the realization of good ideas that can be successful in the future, or to engage in projects in the field of art that they are personally interested in. Unfortunately, apart from Madeleine Zepter, an individual sponsor who annually invests approximately two million euros in the 'Madlenianum' Musical Theatre (opera, ballet, concerts), the companies engaged in investing in music are rare, and then only the most successful ones and the most present ones in the media are sponsored (The Belgrade Philharmonic Orchestra, and the singer Miroslav Ilic who has been supported for years by 'Dunav Insurance' Company). In the world financial and corporate reputation is gained through investment in music and arts (for example, live opera broadcasts for the whole world from the Metropolitan Opera in New York have been sponsored by private corporations and individual donors for decades). In a regulated environment sponsorship of the music arts would take place both as socially responsible behaviour as well as a profitable investment, and that is something what should be developed in Serbia. Successful partnership of public, private and civil sectors is the key to a safe and prosperous development of culture, music and other arts in Serbia.

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ASSOCIATE PROFESSOR MÁRIA TAJTÁKOVÁ, PHD*

College of Management, City University of Seattle, Bratislava, Slovakia

PROFESSOR ŠTEFAN ŽÁK, PHD

Faculty of Commerce, University of Economics in Bratislava, Slovakia

PROFESSOR PETER FILO, PHD

Faculty of Commerce, University of Economics in Bratislava, Slovakia

SHIFTS IN AUDIENCE DEVELOPMENT STRATEGIES IN THE TIMES OF ECONOMIC CRISIS

Summary

During the recent global economic crisis in the years 2007 – 2009 most of the managers of cultural organizations were facing the problem of lowering both public and corporate expenditures on culture. Given the supply-driven demand for culture and the arts¹ (Evrard, 1999) the restrictive policy in recessionary periods can negatively influence also the audience development programs of cultural organizations. Namely, the cutting of marketing budgets of arts organizations may lead to diminished incentives towards arts participation and consequently result into a reduced attendance at cultural events. Furthermore, in view of the deferrable nature of the need of culture,² it could be expected that people postpone or even abandon their arts participation due to lacking resources in economically problematic periods. On the other hand, culture is regarded as a kind of an escapist therapy during economic downturns.³ People seek cultural activities in order to immerse themselves in a different world and forget about their economic problems. The aim of the paper is to examine these different phenomena related to arts participation in recessionary periods in view of audience development strategies. We present the findings of our original research conducted in the field of cultural consumption in Slovakia comparing the pre-recession arts participation (2006-2007) and the participation during the economic crisis (2009) on the sample of semi-panel respondents.

Key words: arts, economic crisis, audience development, strategy

JEL classification: M31, D12

* E-mail: tajtakova@gmail.com

¹ Y. Evrard, “Les spécificités des activités culturelles”, *LES ECHOS*, 18 juin 1999, p. 1-3.

² M. Tajtáková, et al., “The Impact of Crisis on the Sustainability of Cultural Consumption: The Case of Slovak Republic”, The 7th International Conference on Environmental, Cultural, Economic and Social Sustainability, University of Waikato, New Zeland, January 5-7, 2011; http://s11.cgpublisher.com/proposals/54/index_html

³ R. B. Keegan, “Hollywood to Recession: Bring It!” *Time*, March 21, 2008; <http://www.time.com/time/arts/article/0,8599,1724889,00.html>, 2. 5. 2011.

1. Introduction

The managers of arts organizations increasingly recognize the importance of audience development strategies for the arts. Audience development can be defined as a pro-active process of cultivation and growth of long-term relationships through engaging, educating and motivating diverse communities to participate in a creative entertaining experience.⁴ The audience development strategies imply either encouraging current visitors to more frequent attendance and/or enhancing an audience diversification by targeting new market segments. Within the audience development framework arts managers assess different factors influencing the participation in the arts. Two principal influences are known to have a positive effect on the arts consumption – education (education in general and artistic education in particular)⁵ and personal experiences with the arts.⁶ Both these factors are endogenous. However, within audience development programs managers should take into account also exogenous variables, among which economic conditions with a special focus on the economic recession and its influence on the individual arts participation should be highlighted.

The aim of this paper is to examine the impact of the global economic crisis on the arts participation and its implications for audience development strategies. In the first part we provide a conceptual framework of audience development tools and models. In the second part we present the results of our original research exploring the arts participation in Slovakia before the global economic crisis and during the recession period and discuss them in view of audience development strategies.

⁴ D. Walker-Kuhne, “Building Community-Based Audiences for the Arts. Part 1 and 2”, 2001; <http://www.artsmarketing.org>, 2. 5. 2005.

⁵ P. J. DiMaggio, M. Seem, P. Brown, *Audience Studies of the Performing Arts and Museums: A Critical Review*, National Endowment for the Arts, Washington, 1978; F. Colbert et al., *Marketing Culture and the Arts*, Morin, Montreal, 1994; P. Kotler, J. Scheff, *Standing Room Only: Strategies for Marketing the Performing Arts*, Harvard Business School Press, Boston, 1997; E. Hill, C. O’Sullivan, T. O’Sullivan, *Creative Arts Marketing*, Butterworth-Heinemann, 1997.

⁶ C. M. Gray, “Hope for the Future? Early Exposure to the Arts and Adult Visits to Art Museum”, *Journal of Cultural Economics*, Vol. 22, No. 2-3, 1998, pp. 87-98; L. Lévy-Garboua, C. Montmarquette, “Demand”, in: Towse, R. (ed.), *A Handbook of Cultural Economics*, Edward Elgar, 2003, pp. 201-213.

2. Conceptual framework

Most authors describe audience development as an essential function of marketing management in the arts.⁷ Colbert⁸ defines arts marketing as the art of reaching those market segments that are likely to be interested whilst adjusting the commercial variables – price, place, promotion – to the cultural product. A wide range of marketing tools is available to practitioners in order to achieve audience development objectives. However, the audience development strategies go beyond the marketing effort and encompass also educational activities⁹, relationship-building skills¹⁰ and social objectives.¹¹ Tajtáková¹² suggests five areas to be considered and employed within audience development framework: marketing, education, relationship-building, programming and social projects (picture 1).

⁷ K. Diggle, *Arts Marketing*, Rhinegold Publishing, London, 1994; F. Colbert, F. et al., *ibid.*; P. Kotler, J. Scheff, *ibid.*; E. Hill, C. O'Sullivan, T. O'Sullivan, *ibid.*; M. Stokmans, "MAO-model of Audience Development: Some Theoretical Elaborations and Practical Consequences", International Conference of Arts and Cultural Management – A.I.M.A.C., Montréal, Canada, 2005.

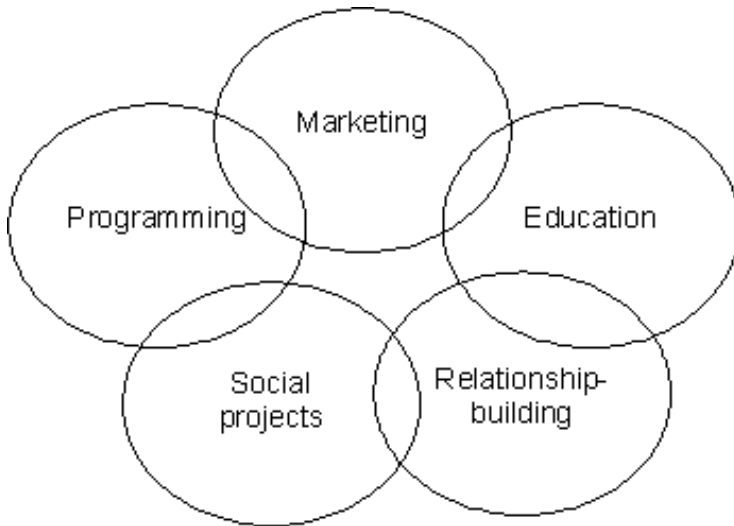
⁸ F. Colbert et al., *Marketing Culture and the Arts*, Morin, Montreal, 1994.

⁹ K. Diggle, *Guide to Arts Marketing: The Principles and Practice of Marketing as They Apply to the Arts*, Rhinegold Publishing, London, 1984; B. G. Morison, J. G. Dagleish, *Waiting in the Wings: A Larger Audience for the Arts and How to Develop It*, American Council for the Arts, New York, 1993; P. Kotler, J. Scheff, *ibid.*; R. Rogers, *Audience Development, Collaboration between Education and Marketing*, Arts Council of England, London, 1998; B. J. Soren, "The Learning Cultural Organization of the Millennium: Performance Measures and Audience Response", *International Journal of Arts Management*, 2 (2), 2000, pp. 40-49.

¹⁰ B. G. Morison, J. G. Dagleish, *Waiting in the Wings: A Larger Audience for the Arts and How to Develop It*, American Council for the Arts, New York, 1993; E. Hill, C. O'Sullivan, T. O'Sullivan, *Creative Arts Marketing*, Butterworth-Heinemann, 1997; D. Walker-Kuhne, "Building Community-Based Audiences for the Arts. Part 1 and 2", 2001; <http://www.artsmarketing.org>, 2. 5. 2005.

¹¹ A. G. Voss, G. R Voss, "Exploring the Impact of Organizational Values and Strategic Orientation in Performance in Not-for-Profit Professional Theatre", *International Journal of Arts Management*, 3 (3), 2000, pp. 62-76; D. Walker-Kuhne, *ibid.*; D. Hayes, A. Slater, "Rethinking the missionary position – the quest for sustainable audience development strategies", *Managing Leisure*, 7, 2002, pp. 1-17.

¹² M. Tajtáková, *Stratégia rozvíjania publika v interpretačných umeniach (Audience Development Strategies in the Performing Arts)*, EKONOM, Bratislava, 2007.

Picture 1: Audience development tools

Source: M. Tajtáková, *Stratégie rozvíjania publika v interpretačných umeniach*, EKONÓM, Bratislava, 2007, p. 60.

In particular, the education is important for stimulating an interest in the arts – namely the high arts. Mokwa et al.¹³ define the aim of educational activities in marketing the arts as giving consumers the tools and codes they need to evaluate the specific features of an artistic product. Therefore, the expansion of audiences for the arts requires the development of a level of understanding, appreciation, and enjoyment sufficient to arouse a desire to attend arts events.¹⁴ Nevertheless, educational projects may comprise either marketing and/or social objectives. A distinction could be made by a target group, which is being educated. Recently, the importance of culture as a tool for achieving wider social inclusion of diverse groups started to be emphasized. For instance, Voss and Voss¹⁵ argue that non-for-profit theatres have a responsibility to provide community access to their performances, remove economic and cultural barriers to attendance, and educate audiences in theatre arts. As a result, audience development strategies of many arts organizations are focused on those on the margins of society such as the physically and mentally challenged, minority ethnic

¹³ M. P. Mokwa, W. M. Dawson, E. A. Prieve, *Marketing the Arts*, Praeger Publishers, New York, 1980.

¹⁴ P. Kotler, J. Scheff, *Standing Room Only: Strategies for Marketing the Performing Arts*, Harvard Business School Press, Boston, 1997.

¹⁵ A. G. Voss, G. R Voss, “Exploring the Impact of Organizational Values and Strategic Orientation in Performance in Not-for-Profit Professional Theatre”, *International Journal of Arts Management*, 3 (3), 2000, pp. 62-76.

groups, the unemployed and teenagers.¹⁶ Walker-Kuhne¹⁷ argues that the effort to achieve a social inclusion has become a moral imperative of current audience development projects.

Hand in hand with increasing the access of socially disadvantaged groups to the arts, a need for sustainable audience development has been pointed out by several authors. They emphasize that endeavours to reach non-traditional audience groups cannot substitute the development of traditional attendees, including an arts organization's existing audience,¹⁸ and that when targeting selected market segments, an arts organization has to be aware of the potential effects of these strategies on non-target segments.¹⁹ This approach highlights the importance of relationship marketing as a new relevant model for marketing the arts,²⁰ together with the implementation of different methods of reaching new audiences. The main challenge of the overall system of audience development, as explained by Hayes and Slater,²¹ is to acquire new audiences whilst retaining and developing the loyalty patterns of existing audiences through the implementation of selective strategies with short, medium and long-term potential.

Several audience development models have been created in order to analyze audience or non-audience members based on their likelihood to become more frequent arts participants. The models such as A.D.A.M²² and SELL²³ branch out to segments non-attending individuals into those who are likely to become participants 'soft targets' and those who are not 'hard targets'. Other models – such as The Performing Arts Adoption Process²⁴ and RAND model²⁵ – focus rather on the subsequent individual process of becoming an audience member passing through distinct stages. On the other hand, MAO model²⁶ provides a matrix

¹⁶ D. Hayes, A. Slater, "Rethinking the missionary position – the quest for sustainable audience development strategies", *Managing Leisure*, 7, 2002, pp. 1-17.

¹⁷ D. Walker-Kuhne, "Building Community-Based Audiences for the Arts. Part 1 and 2", 2001; <http://www.artsmarketing.org>, 2. 5. 2005.

¹⁸ D. Hayes, A. Slater, *ibid.*

¹⁹ J. Wiggins, "Motivation, Ability and Opportunity to Participate: A Reconceptualization of the RAND Model of Audience Development", *International Journal of Arts Management*, Vol. 7, No. 1/2004, pp. 22-33.

²⁰ E. Hill, C. O'Sullivan, T. O'Sullivan, *Creative Arts Marketing*, Butterworth-Heinemann, 1997.

²¹ D. Hayes, A. Slater, *ibid.*

²² K. Diggle, *ibid.*

²³ B. G. Morison, J. G. Dagleish, *ibid.*

²⁴ A. R. Andreasen, *Expanding the Audience for the Performing Arts*, National Endowment for the Arts, Report #24, 1991.

²⁵ K. F. McCarthy, K. Jinnett, *A New Framework for Building Participation in the Arts*, Santa Monica, RAND Corporation, CA, 2001.

²⁶ J. Wiggins, *ibid.*

segmentation of inclined (soft targets) and disinclined (hard targets) individuals dividing them into eight subgroups based on the specific barriers they face. Finally, the Attendance/interest model²⁷ combines two behavioural criteria (participation vs. non-participation and interest vs. no interest) to identify four segments within the market for cultural activities.

Generally, Hayes and Slater²⁸ describe two styles of audience development: 'mainstream' focusing on existing arts attendees and 'missionary' focusing on traditional non-attendees. They suggest both of them to be pursued by arts organizations in order to achieve sustainable audience development. Nevertheless, as a result of growing emphasis on arts as a social tool in the community context²⁹ many arts organizations seem to prioritise audience diversification by reaching non-attending groups and increasing access to the arts. However, the recent global economic crisis brought forward a new perspective on many societal issues, including the audience development. It is assumed that audience development strategies in recessionary periods should focus primarily on diminishing barriers to arts participation perceived by both existing and potential audiences.

In the further text we report the findings of our research conducted in the field of cultural consumption in Slovakia comparing two situations: a pre-recession cultural consumption and cultural consumption during the economic crisis.

3. Methodology

Two surveys were conducted on the sample of 734 respondents (a semi-panel) in two stages. The first survey was carried out in spring 2007, with the aim to identify the typology of cultural consumption in Slovakia. The second one was carried out in winter 2010 with the aim to explore the affects of the global economic crisis on cultural consumption in Slovakia. Both surveys were mapping mainly a past consumption referring to the period of past 12 months. It means the survey in 2007 covered the period from spring 2006 to spring 2007, and the survey in 2010 covered the year 2009. In the further text we refer to these surveys using the years in which they were conducted, i.e. the first survey (2007) and the second survey (2010).

The same standardized questionnaire was used in both surveys. However, in 2010 two more questions were added. Respondents were asked about changes in their cultural consumption levels and the corresponding reasons during the

²⁷ M. Tajtáková, *Stratégie rozvíjania publika v interpretačných umeniach (Audience Development Strategies in the Performing Arts)*, EKONÓM, Bratislava, 2007, p. 88.

²⁸ D. Hayes, A. Slater, *ibid.*

²⁹ A. G. Voss, G. R. Voss, *ibid.*; C. A. Carter, et al., "Advocacy to Agency: The Broward Center for the Performing Arts: Emerging Model for Systems Management", International Conference of Arts and Cultural Management – A.I.M.A.C., Montréal, Canada, 2005.

past 12 months (the recession period). In total 1468 questionnaires were gathered in both surveys. The sample consisted of 734 respondents in each year. Females represented 55 % and males 45 % of the sample. The sample was divided into eight age groups comprising respondents from under 18 to over 76 years. Different educational levels as well as different professional activities were included in the sample. The research was carried out in all eight geographical regions of Slovakia encompassing both respondents from urban and rural areas.

4. Findings

4.1. Arts participation patterns

The most frequent arts participation pattern (Graph 1) identified consistently by both surveys was the statement ‘I attend cultural events from time to time’. This was claimed by 66 % of respondents in 2007 and 72 % in 2010. However, both sporadic and regular attendance was slightly higher in the recession period (together 88 %) in comparison to the pre-crisis period (together 80 %). Accordingly, in 2007 the survey identified 13 % of non-attendees in contrast to only 6 % of non-attendees in 2010.

Graph 1: *How would you characterize your attitude towards culture? (%)*



Source: authors

4.2. Motivation and barriers to arts participation

Tables 1 and 2 summarise motivation and barriers concerning the participation in culture and the arts in both examined periods. Respondents were asked

to evaluate the importance (using 5-point Likert scale³⁰) of twelve different motivation factors and six different barriers. The given motives encompassed emotional, intellectual and social stimuli which corresponded to the usual reasons for arts participation identified by culture attendees in published consumer surveys³¹. Similarly, the usual barriers perceived by non-attendees were investigated. The chosen barriers were consistent with the MAO model³², describing lacking motivation, ability or opportunity of non-attending respondents.

Table 1: *Reasons for attending cultural events*

Order	Year 2007		Year 2010	
	Motives	Mean	Motives	Mean
1.	Entertainment	3.75	Entertainment	4.21
2.	Relaxation	3.61	Relaxation	4.08
3.	To meet with friends	3.34	To meet with friends	3.65
4.	To go out	3.07	To feel emotion	3.54
5.	Meaningful leisure time spending	3.04	To go out	3.48
6.	To feel emotion	2.99	Educational development	3.38
7.	Educational development	2.95	Meaningful leisure time spending	3.37
8.	General interest in culture	2.92	General interest in culture	3.22
9.	Social interaction	2.47	Social interaction	2.52
10.	Accompany a partner	2.30	Accompany a partner	2.47
11.	To dress up	1.91	To dress up	1.83
12.	To improve one's image	1.60	To improve one's image	1.50

Source: authors

The first three motives for attending cultural events remained unchanged in both analyzed periods. Respondents prioritized a leisure attitude towards cultural consumption highlighting an entertainment and relaxation together with a social dimension associated with meeting with friends. However, there were some changes in the ranking of motivation factors between the fourth and the

³⁰ The 5-point Likert scale included these options: Very important (5), rather important (4), neither important nor unimportant (3), rather unimportant (2), very unimportant (1).

³¹ See for instance Boudier-Pailler, D. 1999, 'A Model for Measuring the Goals of Theatre Attendance', *International Journal of Arts Management*, Vol. 1, No. 2, Winter 1999, s. 5-15 or Cuadrado, M. and A. Mollà. 2000, 'Grouping Performing Arts Consumers According to Attendance Goals', *International Journal of Arts Management*, Vol.2, No. 3, Spring 2000, pp. 54-60.

³² J. Wiggins, "Motivation, Ability and Opportunity to Participate: A Reconceptualization of the RAND Model of Audience Development", *International Journal of Arts Management*, Vol. 7, No. 1/2004, pp. 22-33.

seventh positions. The most evident one was a shift in the emotional stimulus which moved from the sixth place in 2007 to the fourth one in 2010. Interestingly, respondents tended to attribute more extreme values to the importance of different motivation factors in 2010 (ranging from 1.50 to 4.21) in comparison to 2007 (ranging from 1.60 to 3.75).

The most important barrier (Table 2) to cultural consumption perceived by non-attendees was the lack of time in both years. However, the ranking of other reasons for not attending cultural events was quite contrasting between the years 2007 and 2010. In particular, the lack of money and the lack of information about culture moved to higher positions in 2010 in comparison to 2007. Similarly to the motivation ranking, the respondents used more extreme values in the evaluation of barriers in 2010 (ranging from 1.96 to 3.41) than in 2007 (ranging from 2.40 to 3.01).

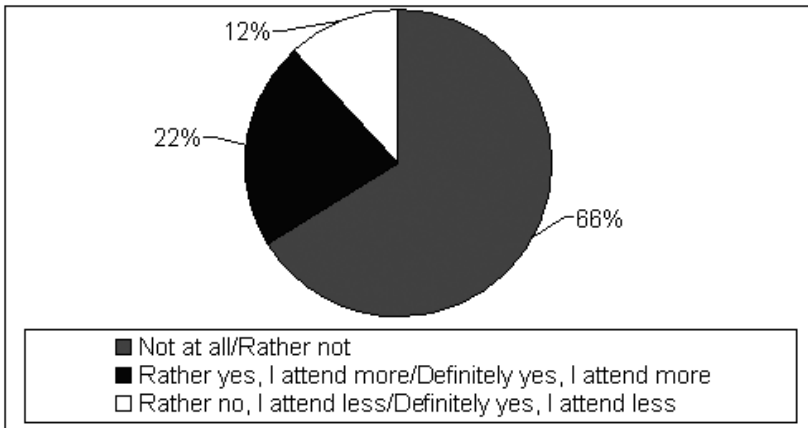
Table 2: Reasons for NOT attending cultural events

Order	Year 2007		Year 2010	
	Barriers	Mean	Barriers	Mean
1.	Lack of time	3.01	Lack of time	3.41
2.	Lack of interest in culture	2.96	Lack of money	2.76
3.	Lack of money	2.86	Lack of information about culture	2.22
4.	Lack of information about culture	2.76	Lack of interest in culture	2.16
5.	Limited opportunities in surroundings	2.74	Limited opportunities in surroundings	2.15
6.	Nobody to go with	2.40	Nobody to go with	1.96

Source: authors

4.3. Changes in attendance at cultural events during the recession period

The survey in 2010 (Graph 2) identified 66 % of respondents whose attendance at cultural events remained unchanged during the recession period. Moreover, 22 % of the sample claimed that their arts participation was even higher. Together, this makes 88 % of respondents with an equal or a higher cultural attendance in the times of recession. Only 12 % of people reported a lower cultural attendance during the year of crisis. These respondents were further investigated.

Graph 2: *Did your attendance at cultural events change during last 12 months? (%)*

Source: authors

4.4. Reasons for a lower attendance during the economic crisis

Only 12 % of the sample in 2010 claimed that their attendance at cultural events was lower in the year of crisis. These respondents were asked to identify their reasons for the lower cultural participation (Graph 3). The reason number one stated by 43 % of less-attending respondents was an overload in job. The economics reason connected with a sparing consumer behaviour caused by the crisis was placed on the second position (28 %). The family reasons (13 %) and prioritizing other activities before culture (11 %) occupied the third and the fourth place. The other reasons were found irrelevant.

Graph 3: *If you attended less, what was the reason?(%)*

Source: authors

4.5. Discussion

In this paper we assumed that the audience development strategies in recessionary periods should focus primarily on diminishing barriers to arts participation perceived by both existing and potential audiences. There are several models of audience development focused on the analysis of barriers to arts participation. Namely, the RAND model³³ and MAO model³⁴. McCarthy and Jinnett's³⁵ RAND model of audience development is a process-based model that comprises four distinct stages of becoming an arts participant. The process begins with the background stage where general attitudes towards the arts participation are assessed. It progresses to the first stage in which a consumer forms a predisposition towards arts participation under the influence of perceptual factors (such as personal beliefs about arts attendance, perceptions of the arts by his or her reference groups etc.). It is in the first stage where perceptual barriers to arts participation may be in play. Once completed the attitudes-formation an individual moves to the second stage, where he or she considers practical factors (such as price, date and location of the event). In this stage practical barriers to arts participation may appear. Finally, in the third stage a consumer evaluates his or her own arts experience and adjusts attitudes towards arts participation based on experiential factors. RAND model of audience development provides a method for not only describing how an individual progresses to the point of becoming an audience member but also helps to understand the factors that influence consumer behaviour in different stages of this process. However, Wiggins³⁶ points out to several limitations of this model resulting from the restriction of perceptual and practical factors to the separate stages without considering their interactions and a joint influence on personal decision regarding arts participation, and further, from the inability to predict the impact of different targeting strategies on non-target segments.

The MAO (Motivation/Ability/Opportunity) model of audience development³⁷ aims to overcome these limitations by analysing various interactions of practical and perceptual barriers that influence individuals in audience development process. The model assumes that participants as well as non-participants experience three types of barriers, which determine their likelihood of participation: lacking motivation, lacking ability and lacking opportunity to participate,

³³ K. F. McCarthy, K. Jinnett, *A New Framework for Building Participation in the Arts*, Santa Monica, RAND Corporation, CA, 2001.

³⁴ J. Wiggins, "Motivation, Ability and Opportunity to Participate: A Reconceptualization of the RAND Model of Audience Development", *International Journal of Arts Management*, Vol. 7, No. 1/2004, pp. 22-33.

³⁵ K. F. McCarthy, K. Jinnett, *ibid.*

³⁶ J. Wiggins, *ibid.*

³⁷ J. Wiggins, *ibid.*

or some combination of these. Motivation is defined as a desire to attend arts events, ability as the absence of individual barriers to attendance (such as unaffordable ticket prices or subjective psychological reasons) and opportunity as the absence of situational barriers to attendance (such as difficulty travelling to the venue). Combining the three criteria eight different market segments have been identified and labelled by Wiggins³⁸ (2004) as: 'patron of the arts', 'patron next door', 'wannabe patron', 'wannabe patron next door', 'football fan', 'neglected neighbour', 'weary traveller' and 'stranger'. The improvement of the MAO model is that it divides inclined and disinclined individuals from the RAND model into more precise segments based on the combination of specific barriers they face. According to Stokmans³⁹ the MAO model can be used to select the most interesting segments, since the segment can differ in terms of size and, as well as the feasibility of the cultural organization to decrease the barriers experienced successfully, given its budgetary restrictions and time perspective. However, Wiggins⁴⁰ considers as a key advantage of the MAO model the fact that it enables organizations to see how their strategy will affect the rest of the market.

In view of the economic crisis we suggest to focus first of all on the analysis of barriers related to economic factors and the 'belts-tightening' behaviour of consumers. Thus, the practical barriers of RAND model and lacking ability from MAO model should be considered.

5. Conclusions

The results of our research did not confirm a negative correlation between arts participation and the economic crisis. In contrast, 88 % of respondents attended cultural events equally or more during the recession period vs. the pre-crisis period. Moreover, 22 % of them claimed that their arts participation was even higher in the times of recession. The motivation of culture attendees in the times of recession emphasized more emotional aspects of cultural consumption, what may support the theory of culture as an escapist activity during economic downturns. The barriers of non-attendees placed the lack of money and the lack of information about culture in higher positions in 2010 in comparison to 2007. This reflects limited resources and also reduced marketing incentives in times of recession. The most important reason for not attending culture during the crisis

³⁸ J. Wiggins, *ibid.*

³⁹ M. Stokmans, "MAO-model of Audience Development: Some Theoretical Elaborations and Practical Consequences", International Conference of Arts and Cultural Management – A.I.M.A.C., Montréal, Canada, 2005.

⁴⁰ J. Wiggins, "Motivation, Ability and Opportunity to Participate: A Reconceptualization of the RAND Model of Audience Development", *International Journal of Arts Management*, Vol. 7, No. 1/2004, pp. 22-33.

was an overload in job (43 %). The economic reasons connected with the recession were explicitly identified only by 26 % of respondents.

To conclude, the findings of our research support the general belief that people tend to seek entertainment and cultural activities as an escapist therapy during economic downturns. However, should we still consider a shift in audience development programs even if the arts attendance has not been negatively influenced by the economic crisis? It is believed that we do. Given that the audience development strategies encompass a continuous effort to build and retain audiences, the arts organizations should constantly monitor all factors with a possible impact on their consumers. Although the overall arts participation did not change during the economic crisis, the research identified certain changes in perceptions and attitudes of consumers. First, a group of consumers having faced practical barriers (RAND model) or individual barriers - lacking ability (MAO model) disabling them to attend arts events during the crisis was found. The barriers were related mostly to overload in the job, lacking money or lacking information. All these reasons may be directly or indirectly connected with the economic crisis. Further, the research discovered a move within motivation factors. While the perception of culture and the arts as leisure activities remained unchanged the emotional aspects of arts consumption became more important during the crisis. Moreover, both in case of barriers and motivation factors people had a tendency to attribute more extreme values to different categories what may also reflect the increased emotionality of consumers.

There is no doubt that these observations are important for audience development endeavors. Thus, it is suggested that arts organization slightly modify the communication message they want to deliver to their audiences during economic downturns. We suggest this message to be based on emotional communication appeals emphasizing the arts participation as an immersion to the world of stories and fantasies. Further, the relaxing effect of the arts as opposite to the increased work deployment in job should be highlighted. Finally, changes in pricing policy should be considered ensuring a more differentiated price for different market segments and providing price offers with the aim not to lose economically disadvantaged consumers during the crisis.

However, some limitations of our research have to be pointed out too. Although we mapped both pre-crisis and during-crisis consumer behavior and attitudes in the field of arts participation, the research was limited to a particular geographical area – the Slovak republic. Therefore, a further research from different countries is needed in order to support our findings.

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ASSOCIATE PROFESSOR MARTA BAKUCZ, PHD*
Faculty of Business and Economics, University of Pécs, Hungary

SUSTAINABLE CITY TOURISM OR HIGHER QOL FOR LOCAL RESIDENTS? – An ex post analysis of the Pécs 2010 European Capital of Culture (ECoC) project –

Summary

Since the change of regime there has been no Hungarian city which has experienced such a complex event as that in Pécs in 2010 – planned to drive and renew political and cultural life and to unite local social forces. Although the Pécs 2010 year is now over, it will remain a major topic for investigation, analysis and research for a long time to come, as reports and studies by experts of many varieties are published continuously. However, the sustainability of successful cultural events and the burden of the associated financial investment remain issues for the future.

Key words: *quality of life, tourism development, mega-events*

JEL classification: O18, L83

1. Introduction

Reconstructed public areas and parks in various districts, the Kodály Centre, the Great Exhibition Site, a renovated Museum Street and the Zsolnay Cultural District, not to mention memorable cultural events; these were the product of the title of European Capital of Culture for Pécs - financed from 28 billion forints of external support and an 'own contribution' of 6 billion forints. A Deputy Mayor referred to the ECoC 2010 year with its 400+ events as 'a successful and exceptionally dynamic year, rich in outstanding events'.¹

How successful these events were is a stale question, and this study tries to show evaluations of the ECoC year from two very different perspectives. The first is that of the business sector of the city which certainly had high hopes of

* E-mail: bakucz@tkk.pte.hu

¹ Bama.hu (2011): *Mögöttünk a kultúrfővárosi év, de mi jön ezután?* –<http://www.bama.hu/baranya/kultura/mogottunk-a-kulturfovarosi-ev-de-mi-jon-ezutan-352280>, downloaded: January 3rd, 2011.

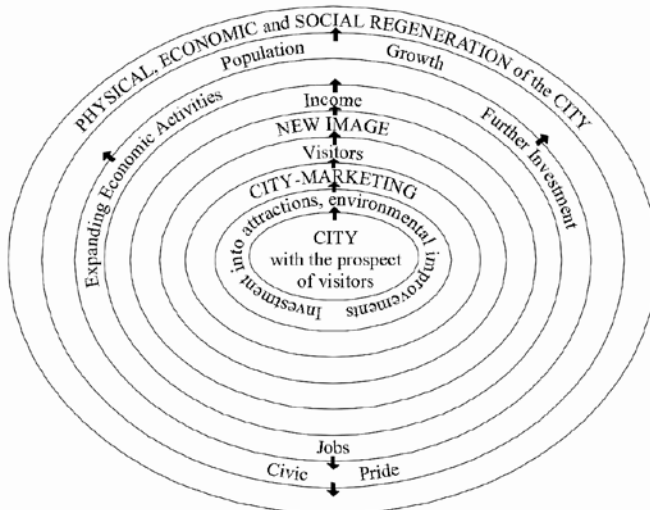
financial benefit from the year. Their expectations for the future were also significant. The second perspective is that of the residents who saw (relatively) huge sums of money spent – allegedly, on their behalf. Was this worthwhile? Will the financial burden be seen as a good investment to improve the city economically and as a place to live – that is, the Quality of Life (QoL)? The concepts are both of great importance and, of course, potentially closely linked.

The traditional concept of tourism envisaged beautiful scenery – the countryside, mountains or the sea – clean, healthy and invigorating, a place to recuperate. Of course a little appropriate entertainment was included – depending on the tastes and pockets of the travellers. If we ignore the earlier 18th century phenomenon of the Grand Tour when young gentlemen both cultivated and moneyed would slowly move around the cities of what we might term “classical Europe”, urban areas did not feature in itineraries to a serious extent until quite recently. It was probably in the early ‘80s that the potential benefits of tourism development acquired some recognition at government, industry and research levels - and in the later ‘80s and ‘90s that its capacity to play an important role in urban regeneration was more fully appreciated: CITY TOURISM.

The total impact, of course, depends upon several factors – the scale of the industry in the given location, the absolute number of visitors attracted, the income generated in the wider area, the number of jobs created and the physical transformation of the locality. These factors, together with professional marketing efforts, create the positive image of the city – the desired impact. There follows the growing recognition and appreciation by local residents of the ‘QoL factor’

The diagram below offers a graphic representation of the overall process.

Diagram 1: *Tourism and City Regeneration*



Source: The author's own diagram on the basis of Law, 1990.

Even in the medium-term, of course, tourism should generate jobs, profit, tax revenues and the like – and also vital, private investment. In the earlier stages of a planned development programme, however, it is very likely that the public sector (and the public purse) will have to play a major role. The core question, therefore, must be: how realistic are the claims for tourism as a true catalyst for urban regeneration – especially in the cities of Eastern Europe as they face the challenges of globalisation and regional transition? How realistic is tourism as a major factor in the rebirth of a city – in its transformation from an old Socialist industrial centre to an attractive, even beautiful, city where people are happy or proud to live?²

Many of these cities were industrialised in earlier years and totally lack any tradition of tourism. To answer this question, therefore, tourism should be examined from the wider perspective of urban regeneration. It is well-known that some Hungarian cities such as Pécs, a South Transdanubian city with, as its advertising slogans repeatedly tell us, both a Mediterranean climate and a Mediterranean atmosphere, have suffered serious economic decline in recent years. They can no longer rely on older, traditional industries (for example, coal- and uranium-mining in Pécs) and seem to have to struggle to show any return from their inherited regional leadership.

The earlier socialist regime - as elsewhere in Central-East European countries - also forced heavy, prestigious, strategic industries on other fringe towns and cities in some of the most beautiful parts of Hungary – hopelessly uneconomical in today's open market and now requiring huge investment to repair the accumulated damage.

A city such as Pécs, therefore, must reposition itself totally in the urban market-place and sell a product (that is, itself) with a Unique Selling Proposition attractive to both companies and people. In general, cities wishing to be, or to remain, competitive must attract appropriate activities - science parks & offices; consumption activities - tourism, leisure and cultural enterprises, a process which equates to CITY-MARKETING.

However, market demands change – sometimes rapidly – and a serious approach to assessment and planning is needed to develop an image – which must be well-founded – for the longer term.

The 1990 work of Williams and Shaw which develops their concept of the four main themes to be used in favour of tourism-based economic strategies shows their positive potential:

- The *flexibility* of the tourism product makes it especially suitable to local economic policies.

² M. Bakucz, “Evropska prestonica kulture na periferiji” (potpuni zapisnik sa konferencije), in: *Regions in Focus? 2nd – 5th of April, 2007, Lisbon, Portugal* – Regional Studies Association, Seaford, United Kingdom, 2007; www.regional-studies-assoc.ac.uk/events/020407papers.asp

- The *low rates* of capital formation per job in tourism make it particularly suitable to employment-driven economic policies and, at the same time, a low-cost strategy. This is also connected to a further argument concerning the potential for small firm growth in tourism, and therefore its relevance to Small and Medium Sized Enterprise (SME) based policies.
- The *speed* at which even relatively large-scale tourism developments can be implemented as a result of favourable demand and production conditions has to be highlighted.
- Tourism is favoured as an instrument of economic policy because of its potential as a *catalyst* for wider economic changes. Tourism-based initiatives can transform derelict physical landscapes, lead to improved infrastructure (particularly in the area of transport) and foster better service provision for the local community, possibly leading to a higher confidence level both among the local residents and the whole area, which itself might attract new investment in the locality.

There is, however, a negative side to tourism-based development which has to be considered for any balanced perspective to be achieved and, therefore, the following counter-arguments should be outlined in relation to the four specific themes mentioned above:

- Tourism development is inherently uneven and differentiates between regions and localities.
- While it is conducive to small business formation, the quality of such firms may be questionable.
- As it permits rapid economic growth, it may also be subject to equally rapid processes of decline. There is, therefore, a need to pay greater attention to product cycles, uncertain demand and competition conditions in the tourism industry.
- Tourism may generate wider social and economic costs, not least of which are social conflicts between locals and immigrants (both temporary visitors and residents) and house price inflation.

There is no precise formula by which we can predict whether the advantages will out-weigh the disadvantages in any particular community. The conditions and possible consequences of any specific tourism development project have to be analysed in each case.

At the beginning of the 21st century and following serious scientific research into the economic and other significance of tourism, we need to be able to recognise the many different forms of tourism, each with distinctive regional implications and not necessarily conforming to any simplistic periphery-centre or centre-periphery model. The following table is my attempt to summarise some of the salient regional features of the forms of city tourism:

Table 1: *Typology of the regional implications of city tourism developments*

Type of tourism	Type of regions					
	Locational Bias			Selective Regions		
	Core	Periphery	Capital	Urban	Rural	Coastal
International Cultural	+		+			
Industrial Heritage		+		+	?	
International Conference and Exhibitions	+		+			
Conference	+	+	+	+		+
Exhibition	+	+	+	+		?
Business General	+			+		
“EVENTS”	+	+	+	+	+	+

Source: Selected in part from Williams and Shaw, 1990, p.6

As we can see, two of the most polarised forms of urban tourism – international cultural tourism and international conference tourism – are mainly capital city activities. In contrast, “events” tourism can be located in many types of region. These may be supplementary tourist attractions such as the Arts and Gastronomic Weeks in Pécs or the Open-air Theatre Festival in Szeged, a major tourist attraction. These can be traditional events or entirely new creations. However, the European Capital of Culture (ECoC) project gives free rein to a city to set out the widest of stalls in its efforts to market itself.

An initial survey was made of students at our University (mostly full-time residents and members of local families). This was done during the first 2011 semester and the results are presented in this study. A larger survey is currently underway of non-student residents of the city, using the same questionnaire. Not only is this timing convenient for us, but the time lapse since the end of the ECoC year allows a more balanced perspective to emerge. The value of our preliminary conclusion in respect of the latter may be queried, but the results drawn from the two sample groups are remarkably similar.

The main body of the paper describes the planning and preparatory process by professionals under the authority of local and central government. This is followed by data and post-event views from two important economic sectors of the city – hotels and restaurants. A third section introduces and describes our ongoing surveys among residents, focusing on their QoL and any changes they may have experienced. Our conclusions close the study.

2. Theoretical background to the research

Quality of Life (QoL) is a compound package of objective factors defining human existence and their subjective reflection. This relatively broad definition includes terms such as 'way of life', 'living conditions', 'standard of living', 'lifestyle' etc. The subjective pillar includes satisfaction, hope, happiness and priorities, whilst the objective includes personal income, health, schooling and public safety. Internationally, the terms objective well-being (OWB) and subjective well-being (SWB) are often used - which are the two basic pillars of QoL.

Tourism, in which an individual is involved either by making a journey or as a part of the social environment of a particular destination, affects his QoL.³ MICE (Meetings, Incentives, Conferences and Exhibitions) and leisure tourism have several factors which are activated whilst satisfying human needs.⁴ The QoL related to tourism appears via the subjective, although we cannot ignore the objective, which influences it. With local residents, this may appear in their utilisation of leisure facilities, their 'consumption' of 'tourism spaces', in the earnings linked to the tourism industry; from the tourists' point of view it is essentially shown in the activities which they feel motivated to indulge in during their holiday.

The 'tourism space' can be considered as a psychological resource from which both the tourists visiting a particular destination and the local residents can benefit. In an ideal case, the construction of the 'tourism space' - together with its qualitative elements - will help to improve the QoL of both tourists and local residents. Naturally, investments produce change - from both perspectives - and it is obvious that both parties need to be satisfied that the changes which appear are to their liking. Our on-going research is targeting an analysis of these changes in respect of local residents and their view of their QoL as influenced by the Pécs 2010 ECoC year.⁵

2.1. *Hungarian Tourism plc (Magyar Turizmus Zrt)* *and the international selling of Pécs*

At a public meeting in November, 2010, the Director of the South Transdanubian Regional Marketing Directorate of Hungarian Tourism claimed that her organisation had worked with very modest financial and human resources for the success of 'Pécs - European City of Culture'. Since 2008, she, together with 2 managers and 1 assistant in the Pécs Regional office, had handled the international promotion of Pécs with an annual budget of 30m forints (little more

³ A. Coskun, D. Rahtz, J. Sirgy (eds.), *Advances in quality of life: theory and research*, Kluwer Academy Publisher, Dordrecht, 2003.

⁴ A. Maslow, *A lét pszichológiája felé*, Ursus Libris, Budapest, 2003.

⁵ G. Michalkó, *A boldogító utazás: a turizmus és az életminőség kapcsolatának magyarországi vonatkozásai*, MTA Földrajztudományi Kutatóintézet, Budapest, 2010.

than €100,000). This is a modest sum, but, via their international network, they had gained significant coverage in each of the 3 years. The national entity has 22 offices abroad, although one problem was a lack of offices in ex-Yugoslavia, where they would have been productive.

Their work focused on two main areas: incoming tourism and the general public. It is, in fact, significant that 97% of foreign tourists traditionally arrive in Hungary as independent travellers and only 3% via travel agencies or in groups. 80-90% of visitors to Pécs and the region come from Germany and Austria, but Hungary's other neighbouring countries are also major sending regions. As Hungarian Tourism has no offices in the Former Yugoslavia, accessing Slovenia, Croatia and Serbia proved difficult, and, since Pécs defined itself as capital of a Southern cultural region, it could not afford to be absent from those areas [Hegyí, 2010a].

2.2. Campaign – Reaching the professionals

To reach tourism professionals via above-the-line (ATL) methods was fairly simple, since incoming partners tasked with organising group travel to Pécs could be reached via the large tour-operators. For example, Hungarian Tourism plc signed a contract with the largest travel organiser in Germany, Austria and Switzerland (Der Tour) for €44,000, as a result of which Pécs featured in 1.7m travel brochures in Germany alone from early 2010. However, ECoC programmes were published relatively late and so many could not be included in major brochures which appear s many months before the event. More flexible, smaller offices with cultural tourism as their main profile (below-the-line or BTL methods) were required, and forty were contacted.

2.3. Campaign – Reaching the general public

The general public was reached through media coverage, and over 200 publications were invited to Pécs, the full costs of these visits covered by Hungarian Tourism plc. Interestingly, several hundred positive articles appeared in foreign magazines, whilst the domestic equivalents highlighted only negative aspects and the failure of the ECoC year was forecast. A 10m forint investment produced publicity worth several hundred million forints in prestigious foreign magazines – *Le Figaro*, *Stern*, *Frankfurter Allgemeine Zeitung* etc – and positive contact was maintained.

A special campaign was launched in the relatively new countries of Slovenia, Croatia and Serbia. They presented primarily native-language brochures on Pécs at larger events and tourism exhibitions where they could access target groups. Since Pécs has several youth hostels and hosts an established high-level interna-

tional youth festival, they also visited universities with the promotional staff of ICWIP – International Culture Week in Pécs [Hegyí, 2010b].

3. Results

In reality, no growth in arrivals was recorded between January and April, numbers significantly increasing only from May. The number of foreign guests then increased most, and in some months the number of German and Austrian visitors (and guest nights) soared by several hundred percent. Commercial accommodation income rose by 40-50%.

Campaigns directed southwards were also successful. Numbers from Slovenia rose by 338% (albeit from a low base). More arrived from Croatia, but the relative proximity of several major Croatian centres meant that these remained day-visitors [Hegyí, 2010b].

TÉDÉEM PÉCS (TDM Tourism Non-profit Co.) in November reported on visitor numbers during 2010. The continuous decline evident from 2002 was reversed in 2010. Between January and September 95,000 visitors arrived at commercial accommodation, a 21% increase over the previous year according to Hungary's Central Statistical Office (CSO). Visitor-nights rose to 185,000, a 22% increase. The significant 63% increase in the number of foreign visitors produced a 65% increase in corresponding visitor-nights. September was the busiest when 63% more visitors spent 68% more nights at commercial accommodation, domestic visitors rising by 53% and foreign visitors by 86%. The high number of the latter originated in increases in German (+75%) and Austrian visitors. Increases were also seen in Italian, British, American, Dutch, Czech, Croatian, Serbian and Slovenian arrivals. A total of 84,000 visitors visited the Tourinform office in Pécs, 70% more than in the previous year, and visits to tourist attractions also showed a very significant advance. The main question, of course, is whether this positive trend can be preserved for the long term.

3.1. *The current scene*

A good opportunity is seen in the future EU membership of Croatia, since Pécs will have a working international airport only some 100 km away in Osijek (although this is ironic following the failure of the Pécs airport) and a reliable transfer service to Pécs is projected. In 2010 the city depended on Budapest and its airport (200 km away). Guests mostly arrived there in the evening or overnight and Hungarian Tourism plc tailored Budapest+Pécs four- and three-star packages. These give guests two nights in Budapest and two in Pécs. Cheap car rental and motorway passes are available and these packages will remain.

As borders disappear, the prospect of similar cooperation with Osijek becomes more realistic.

Also retained is the Infopoint network in Budapest (opened 2010). Information about Pécs for visitors is needed since the number of organised tours is very low. The touristic image of the city is largely determined by local service providers, but it is vital that incoming tourists receive guidance and information freely and so the development of communication and language skills of service providers such as bus drivers and policemen was started in 2008.

Seasonality is an ongoing problem since the city is much weaker in terms of programmes at the turn of the year, although this could be balanced by wellness, gastronomic and wine tourism. The season may, however, be prolonged by the Kodály (Concert) Centre, and programmes are already prepared for a 'World Stars in Pécs' series. The 'Kodály Marathon' was organised with the object of tradition-creating, and, for autumn 2011, conferences are booked for 7-800 and 1,000 people. A further concept for the Centre is that each season will show a different face: spring will highlight the concert hall; in summer open-air programmes will appear; in autumn, minorities and the Heritage Festival will feature; in the winter regional programmes and business tourism will dominate.

3.2. The impact of the Pécs 2010 programme on the hotel industry

The Pécs Director of the Danubius Group evaluated the performance of Pécs hotels: 'hoteliers are fully aware that guests do not choose a particular hotel, but, on the basis of the products offered, the destination and programmes. Only then do they decide which hotel they would like. For hoteliers, 2010 was an extremely good year... It would be good to maintain this in the long term'.⁶

3.3. The Pécs hotel industry in 2009-2010

Data is available from the CSO which gives a good picture of the hotel industry in the city at this juncture, and we show a table constructed by the author giving visitor numbers and occupancy rates for 2009 and 2010 (Table 1). The basic, critical figures are that there are 657 hotel rooms in Pécs, 120 of which appeared in 2010.

⁶ A. Danka, Pécs Director of Danubius Hotels Group – Presentation at the Pécs City Council public hearing – 2010, November 25.

Table 2: *Occupancy rates and visitor turnover in commercial accommodation places in Pécs 2009/2010*

	Room-capacity utilisation (%)		Number of domestic guests in commercial accommodation (persons)		Foreign guests at commercial accommodation (persons)		Average length of stay of guests (nights)	
	2009	2010	2009	2010	2009	2010	2009	2010
January	21.3	19.3	5311	3850	911	800	1.9	1.8
February	24.3	22.7	5076	4457	692	799	1.7	1.8
March	25.3	25.2	6990	6226	1288	1880	1.7	1.9
April	31.3	28.1	8020	6798	1435	2348	2	1.9
May	34.4	38.5	8940	10139	2030	4413	1.8	1.7
June	39.6	42.4	9032	10977	2060	3104	1.9	2
July	36.2	38.6	6317	8126	2446	3602	2.3	2.4
August	36.7	40.5	6494	8847	3050	5250	2.1	2
September	32.9	43.5	5712	8744	2681	4978	1.8	1.9
October	34.5	44.3	7599	9683	1796	4435	1.8	1.9
November	24.1		5325		958		1.7	
December	16.2		3725		775		1.7	
10 months	31.01	34.31	69491	77847	18389	31609	1.94	1.93
Total	29.9		78541		20122		1.9	

Source: Hungarian Statistical Office, author's own construction

Between January and October, the number of guests in commercial accommodation increased 24.5 5% compared with 2009 - with a 71.89 % increase in

relation to foreign guests. Room capacity utilisation showed a 3.3 % increase during the first 10 months of 2010 compared with 2009 - positive, but still below the national average. The hotel industry achieved 2006 results, which is very modest in international terms. Hotels generally do not operate below 60% utilisation - posing a serious problem.

The Danubius Group's 2 major hotels in Pécs (Pátria and Palatinus) showed a 47% increase from January to October, whilst total income, including catering and other revenue, rose by 40%. November and December were significantly better than the same months in earlier years.

Hotel Laterum is also satisfied with its 2010 performance with a 32% increase in guest numbers. A significant and positive result is that their average length of stay increased from 1.5 to 2.5 days. The Sopianae Boutique Hotel also had a successful year, boasting a 10% increase in capacity utilisation. Hotel Corso has no reference year yet since it opened only during 2010 but the owners would have nurtured greater hopes for the EcoC year.

It is useful to examine the composition of guests, as strong segments must be preserved and weak ones strengthened. During the previous year, business tourism was a strong segment demonstrating most growth – 158% in the conference segment, for instance. It remains in question, however, whether this was only due to meetings, debates and conferences related to the ECoC. It is true that several international and national conferences were organised in 2010, but these figures will be hard to exceed or even to maintain in the coming years.

3.4. Vision for 2011 and beyond – the 'post-event' years

The 2004 Palmer Report prepared for the EU had made a thorough study of the history of the ECoC project since its inception and were able to indicate the probability of a marked decline in traffic in the years immediately following the event, although there are exceptions in that, in a few cities, visitor numbers continued to increase. The ultimate example may be Glasgow (ECoC 1990) whose post-event performance has excited both admiration and envy.

The Danubius Group believe that all the conditions exist for making 2011 a successful year for Pécs, but obviously this depends on several factors. Methods of reservation have changed. On-line booking and the growth of the 'last-minute' sector means that little is known at the halfway point. It is expected to be better than 2008 or 2009 but not as good as 2010.⁷

⁷ A. Danka, Pécs Director of Danubius Hotels Group – Presentation at the Pécs City Council public hearing – 2010, November 25.

3.5. *The impact of the Pécs 2010 Programme on the hospitality industry of Pécs*

Tamás Háber, a Pécs restaurateur and President of the Industry's National Association, has the most negative picture of the results of Pécs in 2010, although it must be added that the sector is struggling with enormous problems nationally and slashing expectations for the ECoC year.

3.6. *General problems in the catering sector*

During the last 20 years the number of catering businesses has almost quadrupled, leading to a 40% reduction in per unit turnover. The taxes imposed on the Hungarian industry are extremely high – double the EU average. The absence of professional management also poses serious problems. Despite the fact that catering provides 42% of the revenues of the domestic tourism sector, there is a lack of adequate management at national level.

The regulation of the food industry was imposed on the catering sector, even though the two are clearly incompatible. Restaurateurs, for example, must pay taxes to the state and to the local authority under 35 different headings. In the words of Háber, 24 different taxes and 11 public charges are imposed on the sector's businesses, and the operation of individual units can only be profitable by exploiting special exemptions and 'manoeuvring', with the result that the Hungarian catering industry is becoming a part of the grey economy.

3.7. *Catering in Pécs in 2010*

Tamás Háber conducted his own survey on the results of the ECoC year in which he questioned 10 businesses operating in the old, historic inner city. Of these, 3 reported an increase in income above 100% in the period between May and October. In order to achieve such results, however, large-scale investment was needed and did not generate an adequate return. The other 7 declared that the year had not produced extra income, or, if it had, everything had been swallowed up by extra investment. It was unanimously felt that, whilst tourist turnover had increased, turnover from local residents had declined. The past 12-13 years had been characterised by a growing trend for residents to go out of town to eat – a loss which exceeded any revenue from tourists. This was not so in 2010, since the year did show an improvement in turnover from tourists and some local residents reappeared.

The problems which were most frequently mentioned by respondents were:

- Public procurement procedures deprived Pécs entrepreneurs of opportunities to win business for ECoC events, and so the taxes paid from their operation did not benefit the Pécs budget.

- The ECoC did not adequately exploit Hungarian gastronomic culture as a product. According to the profession, organisers regarded gastronomic services as secondary. Local gastronomy has a weak profile, and so the multi-ethnic composition of Pécs remained under-exploited.
- The publicity focused primarily on events, neglecting the services providing their background. In this way, festival events 'stole' guests from the restaurants.
- The opening day of the ECoC was badly scheduled, according to some. Although the city was full, immediately following the programmes it emptied, and no extra turnover arose.
- The ideas of local gastronomic businesses were omitted from planning programmes.⁸

3.8. *The future operation of cultural institutions*

Péter Hoppál, Director of the City's Cultural Committee declared at the end of the ECoC year: "The name of Pécs has been engraved in bold letters on the cultural map of Europe in 2010. This is shown by tens of thousands of Hungarian and more than one thousand foreign press releases on ECoC events in Pécs. Thanks to the motorway, we no longer have problems of access, and our cultural infrastructure has been totally renewed. Approximately five thousand square meters of new cultural space have been created."⁹

This inevitably involves many future tasks. In reality, the future operations of the Zsolnay Cultural District and the Kodály Centre are not clear. The information contained in the prepared impact studies is no longer relevant, and, moreover, the county has withdrawn from financing several cultural institutions. Another dilemma for the city is the fate of the former culture bases integrated into the Zsolnay Cultural District or the Kodály Centre. The inner city will be a cultural desert with the departure of the Bóbita Puppet Theatre, the House of the Arts, the Music Park and the Youth Centre, and the fate of the buildings (with questionable utility value) is not yet known. One possibility may be to pass the empty halls to amateur artistic groups as workshops, rehearsal or production venues – but their financial viability is a bleak prospect.

Unfortunately, the city's budget does not permit the further financing of culture, but Pécs will receive a ft 140m (€500,000) subsidy for organising programmes to adapt the new institutional network of the city to the actual post-ECoC demand. Negotiating state finance for the Kodály Centre is also in hand. The local authority argued that it was a crucial investment meeting cross-border needs and functions, but to hope for the ft 400m required annually seems unrealistic.

⁸ T. Hon Hábér, President of National Catering Industry Board – Presentation at the Pécs City Council public hearing – 2010, November 25.

⁹ N. Dunántúli, *Milyen az új pécsi kultúrtérkép?*, December 27th, 2010.

4. Preliminary survey results

Our survey looking for reported change in the QoL of residents as a result of the Pécs 2010 ECoC project consists of 22 multiple-choice questions. The first ‘test-period’ of the survey included our own students and was processed in May 2011. Of the 129 respondents, 75% are from Pécs, and the remainder from the region, but all can be considered residents since they spend most of their time – at least 9 months of the year - there. This is complete, but our study of the main body of residents is only underway (starting in June 2011 and closing at the end of August) and in this we are using the most popular, local on-line newspaper and the local authority website. Here, however, we offer the ‘final’ data from the student survey and the early, though limited data received so far from residents (47, which suggests that the interest and affinity level to the particular topic is declining!). If 2 figures are shown, the first relates to the student group and the second to the residents.

Inevitably, all those surveyed had heard about the Pécs ECoC Programme. The proportion of respondents who had experienced positively that the city had become a European Capital of Culture was very similar in both groups. 81.4% / 85.11% agreed with this. Most respondents (53.1% / 63.83%) agreed that the ECoC had improved their QoL (Table 2).

A majority in both groups felt uneasy about the major construction work (59.6% / 53.19%) (Table 2). Although most use, or intend to use, these new facilities (Parks and other Public Areas, Knowledge Centre, Kodály Concert Centre, Zsolnay Cultural Quarter) to a relatively large extent and evaluate them quite highly, most respondents to the on-going survey evaluated the Kodály Concert Centre most highly (38% giving ‘5’ in their evaluation list), whilst the student group found the ‘Knowledge Centre’ the most valuable (40.3% giving the maximum score, whilst the adult respondents were less enthusiastic with 32% giving only a medium rating). However, it must be said that the University’s Central Library and the Libraries of two Faculties of the University are located in this new facility and so many students are obliged to use it – even though its location is not convenient. The ‘Renovated Parks and Other Public Areas’ sector (seen or used almost daily by local residents) was considered successful by a high proportion of both groups. 52.7% and 40% gave ‘4’, and 25.6% and 32% gave a ‘5’ to this quite complex package of renovation and ‘clean-up’ works in the public areas of the city (Table 3-4).

Table 3: Results of Survey Q2-Q6-Q13-1910

Correlation level of responses	Students (%)	Residents (%)
Experienced ECoC positively Q2	81.40	85.11
Felt uneasy about the major constructions Q6	59.6	53.19
Cultural infrastructure changed a lot Q17a	55.81	36.8
The number of programmes sustainably increased Q17b	38.75	21.31
The number of visitor nights sustainably increased in the city and its region Q17c	1.15	8.2
Public transport not improved Q13	86.82	87.23
Public safety not improved Q14	85.2	74.47
Job demand not increased Q15	79	85.11
ECoC project useful for Q16Pécs	95	78.72
The project brought change in your life Q18	37.5	53.19
The biggest achievements in leisure activities Q19	81	67.6

Source: The author's own calculation

Table 4: Results for Survey Q7

(Rank the ECoC investments on the basis of your own preferences)

Preference ranking		Students (%)	Preference ranking		Residents (%)
1.	Knowledge Centre	56.6	1.	Renewal of parks and public areas	64
2.	Renewal of parks and public areas	50.3	2.	Knowledge Centre	34
3.	Kodály Concert Centre	70.5	3.	Kodály Concert Centre	32
4.	Zsolnay Cultural Quarter	84.5	4.	Zsolnay Cultural Quarter	43

Source: The author's own calculation

¹⁰ Q2: Have you experienced positively that your city won the ECoC title? Q6: Has your everyday life been disturbed by the construction of the ECoC big projects? Q13 Has the city transport improved related to the ECoC year? Q14 Has the public safety improved related to the ECoC year? Q15: Have you experienced an increased demand of jobs in your professional area as a result of the ECoC year? Q16: Was the ECoC year useful for Pécs? Q17: Which opportunities are sustainable for the city after the ECoC year? (a. Cultural infrastructure changed a lot, b. the number of programmes sustainably increased, c. the number of visitor nights sustainably increased in the city and its region) Q18: Has the Pécs 2010 project brought change in your life? Q19: In which area of your life has the ECoC year brought any change?

Table 5: Results for Survey Q8 (Evaluate the success of the ECoC investments on the basis of your own opinion)

Correlation level of responses	Q 8 Student (%)/ Success Score(1-5)	Q 8 Residents (%)/ Success Score(1-5)
Knowledge Centre	40.3 / 5	32 / 3
Kodály Concert Centre	19.4 / 5	38 / 5
Renewal of parks and public areas	25.6 / 5 52.7 / 4	32 / 5 40 / 4

Source: The author's own calculation

To questions as to whether public transport and public safety had improved in respect of the project year, and increased job demand had been experienced in their employment area – questions relating most closely to the QoL issue - respondents reacted quite critically. To all these questions most residents (a: 86.82% / 87.23%; b: 85.2% / 74.47%; c: 79% / 85.11%) answered negatively. Apart from these, most respondents (95% of students and 78.72% of normal residents) think that the ECoC project year was useful for Pécs. To the question of what sustainable opportunities are still valid after the ECoC year, most chose: 'The city supply in terms of cultural infrastructure has changed a lot'. (55.81% / 36.8%) as first, and 'The number of programmes of international importance has sustainably increased as a result of the last project year (38.75% / 21.31%) as second. The lowest score was achieved by: 'A sustainable increase in terms of visitor nights has been achieved in the city and its region'(1.15% / 8.2%), which shows the judgement of the residents and the real rate of importance of the sustainable performance of the tourism industry in the city.

An interesting split between student and resident opinion can be detected in answers to the question of whether the Pécs 2010 ECoC project had brought any changes into their life. 37.5% of students said 'yes' whilst 53.19% of the on-going survey respondents (residents) agreed. By contrast, 62.5% of students disagreed, whilst 46.81% of the adult respondents said 'no'. However, most respondents (81% / 67.6%) agree that the biggest achievement can be seen in terms of the new facilities and opportunities for leisure activities in the city.

5. Conclusion

In terms of marketing the city, the European Capital of Culture project displayed a full range of Strengths, Weaknesses, Opportunities and Threats. The winning of the title itself, incentive marketing practices taken from other big cities, appearances in the international press, participation in tourism exhibitions,

some devoted stakeholders in tourism and marketing activities, development concepts, city-marketing strategy in-progress, and the successful utilisation of the Destination Management Organisation application published at national level at the right time – all of these factors created a sound base and effectively contributed to the success of the Pécs 2010 ECoC project. Some problems such as the lack of printed, English language information about excursion opportunities in the area, the missing ‘unique image’, inefficient city marketing, the inefficient transmission of the value of culture, the lack of communication between city and business, weak PR activity in respect of residents, the lack of a full survey of culture consumers’ needs, the lack of balance of the demand and supply sides - all of these resulted in an ambiguous evaluation of the project year and in forcing the stakeholders to consider what the real objective was. Was it outstanding results in the tourism industry - hopefully sustainable in the long term, or a sustainable improvement in the QoL for local residents? Our (still on-going) survey was targeted at investigating the impact of Pécs 2010 on residents.

All the opportunities created by the ECoC project: its image-building effect, highlighted concentration on programmes and visitors even after the big event year, participation in international and EU projects, the exploration of national applications for funds in the region, and the promotion of the city to become an investment target area with the help of the connection-building opportunities offered by the ECoC title, can help the city to overcome the looming threats. These persist, rooted in the continuously weakening financial situation, in deteriorating marketing communication after the project year resulting in declining visitor-nights, in weak support for the developments resulting from a lack of comprehensive information towards local residents, and the residual effect of the earlier, negative, press campaign

To summarise, we would repeat that Pécs had lost its position in the tourism market since 2005, when it was ranked among the best 10 in Hungary in terms of visitor nights (www.itthon.hu). This negative trend was halted by the ECoC project, but it is evident that the accommodation developments and improvement in accessibility are not enough to transform visitor numbers and to strengthen the cultural industry as a pillar of sustainable development. On the basis of the 2010 result, we should ask whether the ECoC developments can ensure a revitalisation of cultural tourism, or whether we should follow international and domestic trends, with different city-product concepts being adopted to improve our competitiveness. For Pécs, culture is a distinctive strength, but the city has no special features which would merit a leading position. The domestic reputation of the city is good; it is considered a nice city with a Mediterranean atmosphere, but it failed to create a ‘special’ image. Apart from the main tourism senders Pécs is not known abroad, or, if known, still geographically not well located.

At the beginning of 2011 the local authority accepted the slogan ‘Pécs - the city of culture’, and this is now the central element of the city brand. The slogan,

however, is a step backwards from “Pécs - the European Capital of Culture”. The latter should be used even after the project year – precisely as other cities do. Further, although Pécs clearly adopted culture as its base, being dependent on one single product is highly risky. All Hungarian cities which regard themselves as cultural define their own distinctive segment – as Pécs should do.

In terms of soft location factors Pécs has a great capacity to create a marketable product from culture, appealing to a wide field, and to develop its own related ‘trademark’. During its 2,000-year history, Pécs has been well-known for its industry for, at most, a century, whilst at all other times its fame has depended on the beauty of its landscape and of its townscape, on the climate and on its cultural and intellectual life. A new colour could be added to the image of the ‘beautiful city’ with a culture industry development programme of which the ECoC title would be a most important component.

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MILENA GNJATOVIĆ, GRADUATE STUDENT AND GRADUATE ASSISTANT*

Faculty of Philosophy, University of Arts in Belgrade

ANA GNJATOVIĆ, ASSISTANT PROFESSOR

Faculty of Arts, Priština - Zvečan University of Priština

FESTIVALS AS CARRIERS OF CULTURE IN SERBIA - PROBLEMS AND LIMITATIONS -**

Summary

In this paper we analyze the activities of festivals as more and more popular and present cultural events in Serbia. Along with factors that influenced the expansion of festival events, we also analyze those factors which provoked the weakening of activities of local institutions of culture and fall in regular seasonal cultural supply. We present the disadvantages and pitfalls of two prevailing methods of financing and their implications on cultural programs – on one side there is project financing on which festivals depend mostly, and on the other side are the activities of institutions which depend entirely on government budget. At the end, we analyze how present situation in culture affects the tastes and cultural needs of citizens.

Key words: *festivals, institutions of culture, cultural production, financing in culture, cultural resources, cultural needs, audience research, project management*

JEL classification: Z11, H76

Festivals are “significant forms of cultural diffusion, since the creation at those festivals is valued” by choice and often rewards, “by which an insight into the artistic scope of a particular environment in certain period is achieved.”¹ With its festive character and constant adapting to contemporary social and market trends, festivals are increasingly popular and visited, and combine different forms of art, entertainment, sports, crafts and fashion under one umbrella. In this paper the term *festivals* will refer to various art gatherings, presentations and events of competitive or exhibition character.

* E-mail: gnjatovic.milena@gmail.com

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¹ M. Dragičević Šešić, B. Stojković, *Kultura: menadžment, animacija, marketing* (5th edition), Beograd, CLIO, 2007.

The reasons why cultural organizations increasingly opt for the implementation of their programs through events of the festival character are numerous, ranging from economic, which manifest themselves as a potential of events to attract money of foundations and sponsors by their image or offer and - through numerous sold tickets - audience. In addition, festivals open space for regional and international cooperation, overcoming the limitations of the medium and genre, contemporary and interdisciplinary forms of production and presentation, and have a great media potential.

In the past, festivals celebrated various events through art, rituals and celebrations. They were seen as special gatherings in which all the people were invited to participate and have a unique experience. The roots of modern festivals stemmed from the first European carnivals. The majority of cultures in their heritage had carnival events such as festivals, port and market celebrations and folk plays. The word *carnival* is derived from the Latin word *carnivale* or “the rise of flesh,” and refers to the period of celebration of the body, leaving physical self-control where debauchery, hedonism and sexuality were expressed through music, dance, masks and celebration. Carnivals in the Middle Ages represented massive celebrations, often religious in character, during which social life was disturbed, and carnival participants mocked the bureaucracy. While Amantidis claimed that carnivals were “creative space for different expressions and reflections of everyday life” and had their own level of social reality, many critics, however, considered carnivals too revolutionary for representing processes of opposing class, gender, racial division and inequalities in which the lower classes freely expressed their frustration. By the mid-nineteenth century in Great Britain and other European countries, carnival fairs were considered obsolete in comparison to carnivals in Latin America and the Caribbean, which abounded in dynamic cultural events, expressions of racial identity and striving for regional harmony. Interestingly enough, if we look at this historical development, today festivals are not considered significant only for the celebration and preservation of one’s culture and tradition, but its tendency toward mass production and reference to tradition. Also, they facilitate the development of modern social environment.²

Festivals and carnivals, from their inception, were the activities of the people, masses and therefore represented the form of mass culture in which participants did not need to be educated, literate or members of a higher economic or social class. In contrast to these events, the culture of sparse elite developed in courts, reserved only for the chosen ones, those who would understand. The concept of the elite culture occurred in the nineteenth century, and this idea occupied a special place with Habermas, just referring to different types of representative events organized at courts. According to Habermas, if culture is real,

² C. Arcodia, M. Whitford, “Festival Attendance and the Development of Social Capital”, *Journal of Convention & Event Tourism*, 8:2, 2006, pp. 1-18, downloaded: http://dx.doi.org/10.1300/J452v08n02_01, February 2012.

it is always elite. Namely, it is intended only for the elite, educated, spiritualized minority. The concept of the elite culture was correlated with the expansion of universities, civil society and liberal capitalism. While capitalism is based on the idea of the market as an organizing principle in itself (which was no longer managed by the king or the court) and the idea of strengthening the individual, liberal civil society has expanded by industrialization and urbanization. By these very phenomena, the notion of the elite culture was brought to the paradox - the culture was popularized due to the emergence of the press and new media, faster and easier communication and information transfer. Thus, festivals, typical for irrepressible masses in the past, today cannot be classified into any of the former categories, but slowly become a kind of social construct.

The expansion of festival events in Serbia began after the Second World War, and the most important and most prominent theater festivals (Bitef, Sterijino pozorje), film (Fest) classical music (Bemus, Mermer i zvuci), folklore and folk art (Dragacevski sabor) were established from the middle 1950s to the early 1970s. A new wave of expansion began in the late 1990s and the largest number of different cultural and artistic events has been established since 2000, from the change of political system and the growth and strengthening of the nonprofit sector. In the Agenda of events available on the website of the Institute for the Study of Cultural Development, there is data about 845 cultural events in Serbia. More than a half, 454 of them, were established from 2000 to 2011. By comparison, in the preceding twelve-year period, from 1988 to 1999, almost three times less events were launched, the total of 162.³ Events in the Agenda can be searched by titles, organizers, geographical indications (city, municipality, district), the month of performance and type (literary, fine art, applied, film, theater, musical-theatrical, musical, mixed, religious, folklore). Their importance and reputation are different, the size of the audience ranges from just over a hundred to over one hundred thousand, their founders are public institutions, nonprofit and private organizations. Some festivals, especially those directed to popular genres of art, are commercial, and they generate a profit to their founders, but there is a large number of them where works of the elite culture and complex art forms are presented and which do not make a profit and often offer completely free events.

When one observes regular events organized by various cultural institutions in Serbia (theater and concert season, exhibition of galleries and museums, programs of multi-purpose centers), there is a negative trend - in the amount of funds allocated for the financing of these activities - and, consequently, in their number, quality, variety and number of visitors. From extensive research by Zaprokulov "Cultural resources of districts of Serbia", it is recognized that municipal budgets for culture are reduced nominally and per capita annually, the offer of cultural events is very limited and dissatisfaction with the overall activities and the situation in culture are expanded among the audience and workers

³ [Http://www.zaprokul.org.rs/AgendaManifestacija/Search.aspx](http://www.zaprokul.org.rs/AgendaManifestacija/Search.aspx), February 2012.

in cultural institutions.⁴ While the “Exit” in Novi Sad has recorded attendance of more than 150,000 people in the past several years, the most visited multipurpose center in Serbia is the Cultural Center in Krusevac, whose programs (mostly cinema) are visited by the average of 148,333 people annually.⁵ The next institution according to the number of visits is the Cultural Center of Smederevo with 108,262 visitors, almost the same number of visitors who watch films at the Fest annually. Multipurpose centers as complex cultural institutions where different types of programs take place, in addition to libraries, are the most widespread cultural institutions in Serbia. The largest number was set up at the time when previously mentioned major festivals were established in the 1960s and 1970s. Today, almost every town in the country has at least one such center. However, data on the work of these institutions is discomfoting. The number of programs per center ranges from 966 (the Cultural Center of Kruševac) to only three (Rekovac, Senta) per year.

In the overall picture of culture in Serbia, one can see radiant activities of festivals on the one hand, and a drastic incapacitation of regular cultural events on the other. The increase of the number and success of festivals is certainly not accidental and it is the result of the current socio-cultural conditions and market demand. Sponsors, companies and public figures have direct benefits from events they invest in, which link their image with positive values of the very events and which, often sensationally and spectacularly, promote more successfully than regular marketing activities. The economic potential of festivals is manifested through their influence on the development of tourism, trade, various service industries, positive image of cities and the overall regional development. It can be understood that sponsors are willing to invest rather in these events than in the problematic mainstream cultural production of institutions which the public rarely visits, which unfortunately means that, in the case of cultural institutions with seasonal programs, as a rule, the cooperation of public and private sectors is absent. The audience is easier to spare time and money to visit an event that happens rarely or only once a year in their environment, followed by a tempting advertisement, a good image and very probably, a package of tickets for all programs at the promotional price. Local cultural institutions lack resources to invest in advertising and the concept and activities of public relations in many cases are quite unknown to their employees.

Festivals with the highest attendance and profit from tickets, that is, events already established and clearly positioned on the cultural map, have the greatest

⁴ A. Lazarević et al., *Kulturni resursi okruga Srbije, Upporedni pregled*, Zaprokul, Beograd, 2010, downloaded from <http://www.zaprokul.org.rs/Media/Document/90cfdc809a0e4943bb8b730f4d479e0f.pdf>, February 2012. The research results relating to the period 2007-2009 and provide the most complete currently available insight into the local culture in Serbia.

⁵ Exepting the Center for Culture, Sport and Tourism of Lucani “Dragačevo”, including the Museum of trumpets, a record number of visitors due to association with the manifestation of the Trumpet Festival in Guca.

support from sponsors. So that any event could occur and attract its audience, achieve credibility, create its own image and identity and interest sponsors in the initial period, it is necessary to rely on the support of public funds. This is usually done through project design and justification of reasons to a particular ministry or municipality why that particular project should be financed.

Turning the majority of cultural activities and festivals more towards projects and less to management of established businesses is an issue that is directly related both to changes in cultural policy and changes in the *Zeitgeist*. The cultural policy of most countries with market economies insists that cultural institutions must act as the institutions responsible for their business results and few countries are willing to finance the activities of the institutions as a whole, cover all their material expenses including salaries, utilities, etc., but the decision on the amount is made on the basis of the project which the institution submits every year or - as unfortunately it is not the case in Serbia - every four years, which offers the opportunity for the institution to realize long-term projects. However, most municipalities in Serbia do not call for tenders for projects in the fields of culture and majority of cultural institutions do not report their projects to existing republic or other (provincial, regional, international) competitions. Thus, complete cultural activities of local governments rely on insufficient budget financing, and more than 80% of their budgets, on average, is allocated for salaries and material costs of cultural institutions. To make things worse, one fifth of local governments "do not recognize the funds for the programs while making the record of budget allocation."⁶ Cultural manifestations, on the contrary, are often funded through projects. However, long-term financing plan often lacks here: for example, according to the knowledge of Jelena Janković, none of the six major classical music festivals (Bemus, NOMUS, Međunarodna tribina kompozicija, Mermer i zvuci, Belgrade International Cello Fest, Guitar Art) was not reported to the international calls for allocation of funds in culture until 2006, even to those foundations which had their offices in Belgrade at that time,⁷ thus relying only on local, primarily public sources of funding and uncertain annual republic budget for culture.

Until a decade ago, according to the research by Milena Dragicević Šešić, in the cultural domain, as in other activities directed more towards business and financial success, the project was, first of all, turned to the realization of a product (exhibitions, performances, festivals). Today, the orientation to the product is replaced by the orientation to processes and the very content of work.⁸ The formulation of various projects has become a major preoccupation of modern man.

⁶ A. Lazarević et al., op. cit., p. 11.

⁷ J. Janković, *Place of the Classical Music Festivals in a Transitional Society*, Master thesis in Interdisciplinary postgraduate studies of The University of Arts in Belgrade, 2006, pp. 63-64; downloaded: <http://www.efa-aef.eu/en/activities/efrp/>, February 2012.

⁸ M. Dragicević Šešić, B. Stojković, op. cit., pp. 210-216.

Today, whatever anyone wants to achieve on the economic, political or cultural level, firstly he has to make an appropriate form of the project in order to seek official approval and funding from the public authorities. If the project is rejected in its original form, it is modified in order to have a greater chance of being accepted next time. Finally, even if such modified project still does not meet the criteria of the public authorities, there is no alternative but to start writing a completely new project. Thus, all members of society are constantly preoccupied with writing, exposing and missing endless series of projects. People constantly write estimates, calculate budgets, gather commissions and fill in endless tables. A significant number of those who have the discretion of appraisers spend time reading these proposals, estimates and budgets, and yet the majority of written projects remain unrealized. It is sufficient that only one person in the commission states that the project does not promise or that it is difficult to finance it, even that it is simply undesirable, and all the work put into the formulation of the project has become a waste of time.⁹

Thus, workers in cultural institutions spend their time and resources on better verbal explanations of their projects, trying to make the proper formalization of the goals of the project, with the use of a large number of the so-called key words, actually explaining the budget and justifying requested funds. When the project is approved, the amount of funds depends primarily on availability of financial institutions that award it, and only then on the real needs of the program. The result is the organization of cultural and artistic activities on the principle of “as finances allow it.” As usual practice in our country is that decisions on the final funding are made in mid-year for the current year, cultural products, in anticipation of the funds, sometimes lose their actuality and relevance, and market conditions change from the moment of submission of the project until its approval.

Such analysis of the financing of culture in Serbia shows a lack of strategic orientation and long-term plans of cultural doers. While local governments do not have clear criteria for allocation of funds, and sometimes they even do not plan funds used for culture, plans for financing festivals are annual, and relatively easily fall into the trap of short-term project financing. Factors that significantly affect the funding of a project are current social and economic circumstances in which the country survives. Changing, crisis and unpredictable situations, specific to the countries of Southeast Europe, affect all aspects, including the cultural development of the environment. Namely, in turbulent and unstable conditions systematic and transparent cultural policy lacks in general and there is not a balanced system of art institutions in practice, and that is why cultural institutions and NGOs are forced in each artistic sector to expand the scope of

⁹ B. Groys, “The Loneliness of the Project”, *New York Magazine of Contemporary Art and Theory*, 1:1, 2008, pp. 1-6, downloaded: <http://www.ny-magazine.org/PDF/Issue%201.1.%20Boris%20Groys.pdf>, February 2012.

their social, cultural and educational activities (organizing encompassing entertainment events), proving that artistic management in these circumstances is not possible in its pure form, but primarily as a hybrid derivative of cultural management.

Especially important factors of environmental instability arise from the crisis of public policies and public sector, which usually involve the non-profiled administration in culture, the creation of development policies that do not involve the cultural field and its doers, the introduction of the liberal model of cultural policy from which sometimes follows inadequate privatization and poor coordination of the sector and levels. Also, the result of a weak civil society is underdeveloped relationships of three sectors: public, private and civil. This usually involves unequal conditions of existence of all cultural organizations, the lack of mutual dialogue and public scrutiny of cultural policy. At the same time, the development of cultural entrepreneurship and the possibility of survival of civil society are complicated.¹⁰

Interestingly, employees in cultural institutions have serious objections to the expertise and number of staff in culture and they see their own education as a high ranking priority. As there are no established criteria and mechanisms of evaluation in culture, so the work of employees in institutions is not assessed or valorized. An average worker in institutions of culture in Serbia today is female, age 47 or older, with a high school diploma and permanent job in the budget organization.¹¹ Education and motivation of such worker are insufficient to meet today's requirements of the culture market and social circumstances.

Crises of the positions of institutions and their social roles, enhanced by insufficient emphasizing of staff development, by the chain reaction, lead to deprofessionalization or lack of knowledge and neglect of their experience and proven practices, particularly in relation to the demands of world markets and new relationships in culture. Finally, potential audience faces a global range of entertainment on the market, which leads to a crisis of participation and the cultural market, and causes a change of taste and value in the long run. This crisis of interest in cultural works and content, especially those that come from local communities, deepens the crisis of cultural institutions and organizations and the sector as a whole.¹² Family values, school environment, visiting art events or institutions in childhood and amateur dealing with art are cited as the four most important factors in the formation of consumer tastes of (high) art.¹³ The adoption of cultural values takes place, therefore, in childhood. Where the family factor is absent, which happens in our community due to a general change in

¹⁰ M. Dragičević Šešić, S. Dragojević, *Menadžment umetnosti u turbulentnim okolnostima*, Beograd, CLIO, 2005, pp. 13-14.

¹¹ Compare with: A. Lazarević et al., op. cit., pp. 12-17.

¹² M. Dragičević Šešić, S. Dragojević, op.cit., pp. 13-14.

¹³ F. Kolber, *Marketing u kulturi i umetnosti*, Beograd, CLIO, 2010, pp. 72-73.

taste and value, the necessity of cooperation between cultural and educational sectors is even more noticeable. The lack of quality cultural events designed for children leaves the deepest mark in the modest offer of cultural programs in cultural institutions. Teachers do not have programs to take school children and children and teenagers do not have opportunities to engage in the work of art, drama or music sections.

The work of cultural institutions, cultural programs, manifestations, festivals and similar events should be based on researched and presumed interests and needs of citizens. The research and knowledge of cultural needs are fundamental tasks of managers in culture, primarily in order to be able to plan cultural activities and programs and cultural development as well – to encourage the development of new cultural needs or widen a circle of people who will have rich and diverse cultural aspirations. First of all, cultural needs are those by which a man realizes his being and which are different from others at the top of the Maslow pyramid. These are the needs by which a man develops his character so that he acts, produces, creates new material and spiritual values, enjoys the present and interacts with the environment. If any of these needs does not develop into a true man's need and interest, but at one time stagnates or vanishes, this means that a person did not acquire cultural habits on time, within the period of development. That is why it is essential that special attention should be paid to creating conditions for the development of cultural needs and cultural practices in early childhood.¹⁴ In the case when cultural institutions as holders of the development fail, the formation of the cultural needs of the majority is based on a questionable offer of media, primarily television (whose cultural profile this paper will not deal with) and, again, sporadic visits to festivals.

When we look at current cultural and artistic festivals in Serbia, the first question that arises is whether the audience goes to the festival and very often only to the opening ceremony because of the desire to satisfy their cultural needs and genuine interest in the content offered by the event, or they are drawn by good advertising and promotions organized by sponsors or any idea about the presence, or being noticed at a prestigious city gathering? Does man develop cultural needs by attending festival events and to what extent? What percentage of visitors will come back to artistic products presented on this occasion and deepen their knowledge and preferences?

Most festivals do not deal with the research of their audience and do not take clear steps towards their development, mainly having only data on the number of visitors and empirical assumptions about their profile and social status.¹⁵ According to Digl, without market research and planned marketing and promotional activities, it is impossible to attract new available, potential audience in sufficient numbers without organized effort to change negative attitudes

¹⁴ M. Dragičević Šešić, B. Stojković, op. cit., pp. 20-30.

¹⁵ Compare with: J. Janković, op. cit., pp. 51-61.

and investments in addressing the widest possible segments of the population. Festivals cannot achieve a long-term goal of transforming unavailable audience (not interested in the event and with negative attitudes and antipathy toward it) into the potential one.¹⁶

If we talk about the potential audience, their needs, tastes and interest in cultural and festival events, we must first define these terms. In the most general sense, the term audience relates to recipients of message or readers, viewers, listeners, regardless of the nature of the medium through which the communication process and content of messages take place. However, with the development of media communication, the very phenomenon to which the term public relations relates is constantly changing and requires constant redefinition and new theoretical and empirical research approaches. The audience, as a social phenomenon, was institutionalized two thousand years ago, in ancient times, with its own customs, rules and expectations in terms of place, time and content of action. The ancient audience occupied the auditorium in amphitheatres, the place from which it could directly observe the drama and it was in constant interaction with live performers, and so formed the potential collective, which shared common background and experience. So, the key difference between the ancient and modern audience is in their characteristics that are determined by spatial and temporal components.

The formation of mass audience, as mentioned in the introduction, occurred parallel with the advent of printing, since the book provided effective communication at a distance as well as the privacy of experience. With the advent of printing, there was the phenomenon of *dispersed* readership - groups of individuals that perceive and read the same text. Further development of the media and the emergence of the film allowed the interaction of the audience, while radio and television, according to observations by Zorica Tomić,¹⁷ enabled the creation of today's mass audience which is characterized by *anonymity, dependence and passivity*. This audience is guided by the collective opinion, their taste is defined according to the established model, and their development and critical thinking are exceptions.

In sociological research, the taste of people is operationalized through verbal expressions of marks for specific works of art or preferences of certain artistic genres and, on the other hand, through the behavior or cultural activities such as visiting certain cultural events (concerts, theaters, museums, etc.), watching films and reading books.

Cultural capital, according to Bourdieu, is a currency based on taste. It includes knowledge of high art and culture, a high level of sophistication and knowledge and positive evaluation of general knowledge and familiarity. Bourdieu identifies three areas of taste, which roughly correspond to educational levels and social classes: the legitimate taste - preferences for works of art of high culture (propor-

¹⁶ K. Digi, *Marketing umetnosti*, Beograd, CLIO, 1998, pp. 221-227.

¹⁷ Z. Tomić, *Komunikologija*, Beograd, Čigoja štampa, 2001, p. 130.

tional to the level of education, most abundant in fractions of the richest class in the educational capital), the mediocre taste - preferences for less significant works of art and the best works of popular art (more present in the middle class than in the working class) and the popular taste - preferences for works of legitimate art that have lost their prestige through the process of popularization and the works of popular art that have no artistic pretensions (most common in the working class).¹⁸ Somewhat broader typology of culture tastes was suggested by Herbert Gans, considering, besides the class membership, other socio-demographic factors: age, race, ethnicity and place of residence.¹⁹ As basic differences between status groups Paterson emphasized the scope of leisure activities and diversity of cultural choice and defined the members of the cultural elite as omnivores, who showed their exclusivity by wider range of leisure activities and knowledge of all art forms, from high to low and popular culture.²⁰

The paper analyzes the state of the culture in Serbia, without Belgrade. Even if we ignore the general adverse financial conditions or low income of citizens, on the basis of available data it is not difficult to come to the conclusion that the achievement of Bourdieu legitimate taste or status of Paterson's omnivorous in Serbia today is possible only if an individual acquires one of the factors stated by Gans – geographical or place of residence. With the exception of the capital and several other major cities, the offer of regular, seasonal cultural programs in Serbia amounts to rare productions which, without a strategic plan and the necessary cooperation with other sectors, with relatively scarce resources are organized by relatively professional and unmotivated staff, who struggle every day with financial problems, inadequate space and indifferent audience. Festivals, as diffuse and sporadic events, which in their essential conception do not mean and do not allow the regularity of events annually or are committed to long-term cultural and educational objectives, lack predispositions for the development of cultural needs and formation of tastes of their visitors. Additionally, due to the current situation in culture, and bearing in mind that the formation and profile of the majority of festivals coincide with the process of deterioration of cultural values and tastes, most of the events that take place in smaller towns turn to the presentation and promotion of culture that has its audience in these areas, mostly folklore and national heritage and the products of popular culture. Without a clear cultural policy, strategic plans of local governments to strengthen cultural institutions and established elements of their implementation, it is difficult

¹⁸ P. Bourdieu, *Distinction: A Social Critique of the Judgment of Taste*, Routledge and Kegan Paul, London, 1984.

¹⁹ H. J. Gans, *Popular Culture and High Culture. An Analysis and Evaluation of Taste* (revised and updated edition), Basic Books, New York, 1999.

²⁰ R. A. Peterson, "Problems in Comparative Research: The Example of Omnivoresness", *Poetics*, no. 33, 2005, pp. 257-282.

to find a way out of this vicious circle, eliminate the habits of today, change the situation in culture and take a different path.

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PROFESSOR YUN TAI, PHD*

Department of Sociology, Emory University, Atlanta, Georgia, USA

THE EFFICACY OF AUDIENCE BUILDING AMONG NONPROFIT CULTURAL ORGANIZATIONS: THE IMPACT OF MARKETING STRATEGIES AND ORGANIZATIONAL ATTRIBUTES

Summary

Given the importance of individuals' participation in the sustainability of nonprofit cultural organizations, I look at how those organizations attract audiences to partake of their services. By analyzing the data drawn from approximately 500 nonprofit cultural organizations in the U.S., I find that both internal factors (i.e., age, size, presenting performing arts, specialist vs. generalist) and external factors (i.e., location in a city with a rich cultural tradition) combine with marketing strategies to shape the efficacy of audience building. The results provide some perspective on how such organizations negotiate both their aesthetic and economic concerns.

Key words: audiences, non-profit cultural organizations, marketing

JEL classification: M31, D12

1. Introduction

Marketing strategies are essential not only for the revenue accumulation of commercial companies but also for the client-building efforts of nonprofit institutions. That is, both general types of organizations are concerned with securing enough resources to survive, if not thrive. Thus, to distinguish clearly between commercial and nonprofit organizations may be more complicated than it seems. Nevertheless, notable differences do exist between both types of organizations. For example, in the U.S., organizations are designated as nonprofit when they are granted tax-exempt status in exchange for the beneficial services they provide the broader community (e.g., healthcare, education, religion). When granted this designation, a nonprofit is not allowed to distribute any profits to shareholders,

* E-mail: ytai2@emory.edu

if they gain any profits, but must reinvest those surplus earnings in the organization itself.¹ Historically, US nonprofit have received their earnings from consumers who use their services, as well as from external funding by government agencies and private foundations and donations from individuals and corporations.² Therefore, even though nonprofit organizations do not aim for accumulating profits, it is still important for them to garner enough clients in order to survive – especially as a healthy client base not only provides an important source of income, it can also legitimate and attract income from such sources as government funding and corporate donations.

A notable difference is also found within nonprofit organizations in the United States. Compared to nonprofit organizations in other fields (e.g., health-care, education), nonprofit organizations in the cultural sector (e.g., the arts) are distinctive because they rely more on personal donations and less on government grants.³ Given this, it is especially important for these particular nonprofits to attract individuals to partake of their services, activities, or events – thereby boosting income derived from ticket sales and individual donations. Thus, an important question is how nonprofit cultural organizations market their “product.” That is, how do they attract a large enough audience to consume their cultural products in order to fulfill their organizational goal of preserving and propagating the arts? We can approach this inquiry by looking carefully at three questions. Two of them are descriptive in nature: (1) What have nonprofit cultural organizations done with respect to marketing – what are their actual strategies, both in sheer number and in type? (2) What kind of audience changes they have achieved – both in terms of overall numbers and particular audience segments? The remaining question is explanatory and draws upon previous scholarship; hence, it is the focus of this study: (3) How do the number and type of marketing strategies combine with organizational attributes to shape audience building in positive fashion? My essential statement as follows: nonprofit cultural organizations with particular characteristics (e.g., large size) and that pursue particular marketing strategies (e.g., those focused on the artistic mission) are more likely to see an increase in overall numbers and in particular audience segments (e.g., lower-income participants). However, none of these strategies or attributes has

¹ P. DiMaggio, “Nonprofit Organizations and the Intersectoral Division of Labor in the Arts”, in: *The Nonprofit Sector: A Research Handbook*, 2nd edition, ed. by W. W. Powell, R. Steinberg, Yale University Press, New Haven, CT, 2006, pp. 432-461; Sh. Potter, T. Dowd, “Executive Turnover and the Legal Environment: The Case of California Hospitals, 1960–1995”, *Sociological Forum* 18, 2003, pp. 442-464.

² P. DiMaggio, “Can Culture Survive the Marketplace?” in: *Nonprofit Enterprises in the Arts: Studies in Mission and Constraint*, ed. by Paul J. DiMaggio, Oxford University Press, New York, 1986, pp. 67-92.

³ P. DiMaggio, “Nonprofit Organizations and the Intersectoral Division of Labor in the Arts”, in: *The Nonprofit Sector: A Research Handbook*, 2nd edition, ed. by W. W. Powell, R. Steinberg, Yale University Press, New Haven, CT, 2006, pp. 432-461.

consistent and strong effects across all audience segments – thereby showing the limits of efficacy with regards to audience building in the early 21st century. Before turning to the analysis itself, I first lay out some explanatory factors in the following section.

2. Nonprofit Cultural Organizations in Action

There is a literature that addresses the operation of nonprofit cultural organizations. The studies comprising it often investigate these organizations by examining and explaining the range of products they offer – such as the diversity of their repertoires (symphony orchestras, opera houses, theatrical companies) or exhibitions (museums). Their explanations emphasize, among other things, the competing missions at the core of these organizations, their internal characteristics (e.g., age, size) and their external environment (e.g., the cities in which they are located), and the distinction between performance arts organizations versus others. I draw upon such studies to examine and explain parallel outcomes among nonprofit cultural organizations – the range and efficacies of their marketing strategies. Thus, I describe below what this literature finds, so as to situate my own focus on the marketing of nonprofit cultural organizations.

3. The Competing Missions of Nonprofit Cultural Organizations

Certain case studies of individual organizations clearly demonstrate an important point: nonprofit cultural organizations are distinct from other organizations because of the two missions they are expected to balance. On the one hand, differing from for-profit organizations in media that deal with music and the like, nonprofit cultural organizations are more or less responsible for preserving and enhancing the diversity of the arts and culture – hoping to ensure that the public can, and will, participate in cultural events and / or activities. On the other hand, somewhat resembling commercial media organizations, nonprofit cultural organizations are also expected to cover a certain portion of their operational costs. Thus, nonprofit cultural organizations are expected to provide events or activities with aesthetic value but also to sustain themselves so as to survive.

Given that these two missions are sometimes contradictory, it can be difficult for nonprofit cultural organizations to achieve them both. In her case study of the Atlanta Symphony Orchestra (ASO), Mary Ann Glynn⁴ details the uneasy

⁴ M. A. Glynn, “When Cymbals Become Symbols: Conflict over Professional Identity within a Symphony Orchestra”, *Organization Science* 11, 2000, pp. 285-298; M. A. Glynn, “Chord and discord: Organizational crisis, institutional shifts, and the musical canon of the symphony”, *Poetics* 30, 2002, pp. 63-85.

existence within the orchestra of these two missions. Indeed, she emphasizes the “hybrid identity” of the ASO (as well as of arts organizations in general) that involves “the aesthetic elements that craft cultural products and the economic elements that characterize their production”.⁵ Furthermore, she demonstrates how these competing missions map onto certain parts of the orchestra – with musicians being the carriers of the artistic mission and the board and management upholding the utilitarian mission.⁶ Not surprisingly, the tension that exists between the two missions – and their respective proponents – can sometimes erupt in outright conflict, as evidenced by the ASO musicians’ strike of 1996. The inner tension between the artistic and utilitarian missions also places pressures on the music director or conductor of the symphony orchestra. The role of music director is especially “controversial” in times of organizational contestation (e.g., a strike) and of economic crisis – such as the decreasing attendance, aging audiences, and reduced opportunities for touring and recording that now face the ASO and other US orchestras.⁷

The tension between these missions has implications for the range of music the ASO offers – especially when strikes and economic difficulties tilt the balance toward the utilitarian mission. Thus, the ASO (and other orchestras) has started to adopt more popular interpretations of the musical canon⁸ – mixing “high” art forms from the classics with the “low” art forms drawing from popular culture,⁹ which results in the yielding of the artistic identity to the utilitarian identity.¹⁰ In a study of music critics’ reviews of ASO concerts found in the local newspaper during in the 1995-96 and 1997-98 seasons,¹¹ investigate how the critics’ discourse and judgments of performances are shaped by shifts in the orchestra’s missions, whereby the utilitarian mission begins to edge out the artistic mission. They find the changes do exist after the ASO musicians’ strike; the percentage of the reviews containing aesthetic references decreased from 91% in the pre-strike season (1995-96) to 53% in the post-strike season (1997-98), while the percentage of reviews containing economic references increased from 30% to 57%. In other words, the pressure of constrained resources, as the strike reveals,

⁵ M. A. Glynn, “Maestro or Manager? Examining the Role of the Music Director in a Symphony Orchestra”, in: *The Business of Culture: Strategic Perspectives on Entertainment and Media*, ed. by J. Lampel, J. Shamsie, T. K. Lant, Mahwah, Lawrence Erlbaum, NJ, 2006, p. 66.

⁶ M. A. Glynn, op. cit., 2000, pp. 285-298; M. A. Glynn, op. cit., 2002, pp. 63-85.

⁷ Glynn, op. cit., 2006.

⁸ Glynn, op. cit., 2002.

⁹ See also: T. J. Dowd, K. Liddle, K. Lupo, A. Borden, “Organizing the Musical Canon: The Repertoires of Major US Symphony Orchestras, 1842 to 1969”, *Poetics* 30, 2002, pp. 35-61.

¹⁰ Glynn, op. cit., 2006.

¹¹ M. A. Glynn, M. Lounsbury, “From the Critics’ Corner: Logic Blending, Discursive Change and Authenticity in a Cultural Production System”, *Journal of Management Studies* 42, 2005, pp. 1031-1055.

does push the critics to be more inclined toward utilitarian rather than artistic aspects of the orchestra.

Similar to Glynn's concept of hybrid identity among symphony orchestras, Stefan Toepler¹² emphasizes the balancing of aesthetic and utilitarian missions among art museums. By way of his case study of the Metropolitan Museum of Art – which spans 1960 to 2002 – Toepler tracks the trend of commercialization in nonprofit sector. He finds that commercialization first emerged in 1970s, with reduced endowment funds due to the broader economic crisis, and it kept rising in the 1980s and early 1990s in the face of dwindling government support and heightened for-profit competition. The nonprofit sectors thus were forced to build up alternative financial sources. Toepler is concerned that, when nonprofit sectors' involvement in private good production is increased, there are increased chances of financial considerations overriding artistic considerations. In the case of museums, the pursuit of popular exhibitions became an outright strategy in 1980s and 1990s, rather than a lucky happenstance as in 1970s, because “profitable” popular exhibitions were able to support unprofitable but “highly important” (i.e., scholarly) art works. Like that of Glynn's (2000, 2002, 2006), Toepler's research also indicates the tension between aesthetic and utilitarian missions – showing that this tension is not limited to orchestras but also occurs for museums.

4. Internal and External Aspects of Nonprofit Cultural Organizations

Given the difficulty of balancing the two competing missions, it is important to understand how different nonprofit cultural organizations deal with them, and as a result, how conventional or how adventuresome they are in their programming. There are several studies that take as their focus – not a single organization – but an entire group of nonprofit cultural organizations in a particular setting. Many organizational studies have generally explored how the age, size and specialization of organizations shape how adventuresome they are,¹³ so too do these studies of nonprofit cultural organizations – thereby heeding how factors internal to these organizations (e.g., size) shape their operations. Of course, as much organizational scholarship reminds us,¹⁴ organizations are also shaped by factors beyond their boundaries. Thus, these studies of nonprofit cultural organizations acknowledge that these organizations do not operate in isolation but are embed-

¹² S. Toepler, “Caveat Venditor? Museum Merchandising, Nonprofit Commercialization, and the Case of the Metropolitan Museum in New York”, *Voluntas* 17, 2006, pp. 99-113.

¹³ Videti: T. J. Dowd, “Concentration and Diversity Revisited: Production Logics and the U.S. Mainstream Recording Market, 1940-1990”, *Social Forces* 82, 2004, pp. 1411-1455
Dowd, 2004; W. G. Roy, T. J. Dowd, “What is Sociological about Music?”, *Annual Review of Sociology* 36, 2010, pp. 183-203.

¹⁴ Videti: C. Johnson, T. J. Dowd, C. L. Ridgeway, “Legitimacy as a Social Process”, *Annual Review of Sociology* 32, 2006, pp. 53-78.

ded in a larger social context. Among other things, these studies emphasize the importance of being in cities with rich traditions of artistic activity.

A landmark study in this tradition is offered by Paul DiMaggio and Kirsten Stenberg,¹⁵ who examine what internal and external factors shape the programming of U.S. resident theaters, particularly the extent to which they are each innovative. Regarding internal factors, their study reveals a less than clear-cut impact of both age and size. DiMaggio and Stenberg hypothesize that highly “institutionalized” theatres are more conformist than less institutionalized theatres. In the American resident stage, four properties are related to institutionalization: the size of a theater company, its age, its level of bureaucratization, and the extent to which the theatre adheres to the norms of the field. On the one hand, some suggest that theatres need a strong economic base, solid management, and a subscription audience to make it possible for them to pursue their artistic goals. Seen in this light, institutionalization is essential for their economic success as well as for their artistic achievement. That is, older and larger theaters have the capacity and resources to offer innovative programming. On the other hand, some argue that age is associated with conservatism, size with stultification, earned income with enslavement to philistine audience tastes, and managerial growth and differentiation with the displacement of artistic by financial goals. In this critical view, profits are placed above artistry by professional managers; risk-taking is financially harmful because of the dependence on subscription; and burdensome commitments – to administrators, to subscribers and customers, and to large and expansive equipment – that result from a large budget will lower the possibility of innovation. In addition, the authors also point out large seating capacities as a potential element that is positively related to conformity, because theatres with larger seating capacity have more expensive financial commitments to meet than those smaller ones have. Regarding these internal factors, DiMaggio and Stenberg find small effects – with organizational age having no negative impact on programming innovation, while small theater companies (measured in terms of budget or seating) tend to be more innovative. Among external factors, they find a strong effect: theaters located in New York City are more innovative than others. They attribute this to its considerable infrastructure for theatrical production and consumption – one that stems from its role as a center of the American stage. Some of the results – particularly that regarding the negative impact of size on innovation – indicate the tension between innovation and the concern with the box office – that is, the tension between artistic and utilitarian missions.

¹⁵ P. DiMaggio, K. Stenberg, “Why Do Some Theatres Innovate more than Others? An Empirical Analysis”, *Poetics* 14, 1985, pp. 107-122.

Lamar J. Pierce's study¹⁶ of American opera companies' programmatic risk-taking displays the impact of one internal factor (organizational size in terms of budget) and various external factors (e.g., different funding sources) on adventuresome programming – illuminating further the tension between artistic and utilitarian missions. By analyzing the programming data for all of the Opera America's members from 1989 to 1994, Pierce notes that lower-risk operas are the more frequently produced, such as works of Mozart, Verdi, and Puccini, while higher-risk ones are less popular and involve higher costs works, e.g., Britten, Argento, and Wagner. In terms of organizational size, he finds an inverse relationship between it and conventionality; thus, opera companies with larger budgets tend not to be averse to risky programming. This runs counter to DiMaggio and Stenberg's (1985) finding for large theatrical companies and their programming conformity. Regarding external factors, Pierce does not examine the impact of location in a particular city (as DiMaggio and Stenberg do for New York City). Instead, he finds that federal funding, such as that from the National Endowment for the Arts (NEA), does reduce the financial pressure on opera companies and thus enables them to produce unconventional, high-risk operas. However, local government funding promotes conventional, lower-risk operas. In short, Pierce's work shows that the influence of external financial support on programming selection is knotty – with organizational size having an independent and positive impact on experimentation. Reduced financial pressure does not necessarily lead to either innovative or conventional programming; rather, it depends on what kind of funding resource the organization received. In addition, he also finds that private donation does not tend to encourage conventional programs, while conservatism does lead to lower-risk productions; opera companies in cities with liberal, higher education and income population are more likely to produce more innovative works.

One analysis beyond the U.S. reveals some similar results on the conventionality of arts, focusing on both internal factors (e.g., organizational size) and external factors (e.g., funding source and location). John O'Hagan and Adriana Neligan¹⁷ examine repertoire conventionality in the nonprofit English theatre sector – doing so via a dataset that includes 40 grant-aided English theatres in three theatre seasons (1996/97, 1997/98, and 1998/99), during which the 40 theatres received grants from the Arts Council of England (ACE)/Regional Arts Boards (RAB) and the local authorities. The conventionality index is constructed by using the production lists of the 40 theatres in the three seasons from the ACE's playlists. The most important finding of this study is that the increase of

¹⁶ J. L. Pierce, "Programmatic Risk-Taking by American Opera Companies", *Journal of Cultural Economics* 24, 2000, pp. 45-63.

¹⁷ J. O'Hagan, A. Neligan, "State Subsidies and Repertoire Conventionality in the Non-Profit English Theatre Sector: An Econometric Analysis", *Journal of Cultural Economics* 29, 2005, pp. 35-57.

state subsidy decreases the conventionality in repertoire – somewhat resonating with what Pierce (2000) finds for U.S. opera companies. O’Hagan and Neligan also find that theatres with smaller budgets and less seats are more likely to produce innovative works; this is more consistent with the size effect found among U.S. resident theaters¹⁸ and at odds with the size effect found among U.S. opera companies (Pierce, 2000). In addition, the authors indicate that higher income in a community and location in London both decrease conventionality – with the latter being similar to DiMaggio and Stenberg’s (1985) finding that theatres in New York City are more likely to be innovative. Thus, both studies point out the impact of external factors on cultural organizations by showing these organizations tend to be more innovative when they are located in places rich in cultural goods (e.g., New York and London).

One final study brings together the impact of internal and external factors on the programming of nonprofit cultural organizations, while also complicating the picture by emphasizing the programming strategies of these organizations (e.g., specialization). In a study that addresses innovation by heeding the performance of living composers, Timothy Dowd and Kevin Kelly¹⁹ use data provided by the League of American Orchestras, which contains 7570 performances by 313 orchestras during the 2005-06 season, to analyze the extent to which the three categories of factors influence the presence of living composers in U.S. orchestral repertoires. The three categories are: (1) internal factors, including the age and size of given orchestra, as well as its productivity, (2) external factors, such as location in the New York City metropolitan area, and (3) its programming strategies, including specialization in a limited range of composers. They find that about 89% of performances in 2005-06 are of dead composers rather than living ones – showing small levels of innovation in this particular sense. How to explain when this innovation does occur? First, in terms of internal factors, all large orchestras present performances from living composers; however, the extent to which they do so is limited. For smaller orchestras, some of them do not present any living composer’s work, whereas some have repertoires that are completely made up of music composed by living ones. In addition, productivity significantly influences the programming choices of orchestras; as both large and small orchestras offer more performances during the season, they tend to present fewer works by living composers. One internal factor – the age of orchestras, be they large or small orchestras – has no impact upon the extent to which they feature living composers. Second, in terms of external factors, most variables do not significantly influence the percentage of performance that orchestras devote to living composers, except the NYC variable. In particular, large orchestras in the New York City metro-

¹⁸ P. DiMaggio, K. Stenberg, *ibid.*

¹⁹ T. J. Dowd, K. J. Kelly, “Composing a Career: The Situation of Living Composers in the Repertoires of U.S. Orchestras, 2005-06”, in: *Careers in Creative Industries*, ed. by Christopher Mathieu, Routledge, London, 2011, pp. 210-233.

politan area feature more living composers' works than do all other orchestras. Third, in terms of programming strategy, repertoire specialization among large orchestras tends to reduce the performance of living composers, whereas specialization among small orchestras promotes this particular innovation.

This final study, then, suggest that the inconsistent findings in terms of organizational size on programming found among the previous studies may be explained by whether or not nonprofit cultural organizations are specialists (or, by contrast, generalists) in terms of operational strategies. Meanwhile, as three of the studies discussed above show, the impact of location in a leading city of artistic production (e.g. New York, London) contributes to innovation among orchestras, opera companies and theater companies. Such internal and external factors help us make sense of the way in which nonprofit cultural organizations negotiate the tensions between artistic and utilitarian missions.

Given the data that I have at my disposal (see below), I am not able to delve into the intricacies of funding arrangements (e.g., federal versus local funding) or the intricacies of community characteristics (e.g., cities with highly educated populations). However, I am able to investigate how three internal factors – organizational age, organizational size, and programming strategies (i.e., specialization versus generalization) – and one external factor – location in a city known for its artistic heritage and vitality – when examining the types and efficacies of marketing strategies found among a group of nonprofit cultural organizations.

5. Varieties of Nonprofit Cultural Organizations: Performance versus Exhibition

Not all nonprofit cultural organizations are alike; as a result, organizations with different characteristics deal differently with the tensions between artistic and utilitarian missions. Vera Zolberg²⁰ compares the innovation patterns of two structures of artistic media – performance versus display – by using the examples of museums and symphony orchestras. The performance of music depends on time and it is ephemeral while the display of visual art depends on space and it is concrete. These distinct characteristics for performance and display extend to costs, expectations of growth and patronage sources of cultural organizations. On the one hand, the performance of a symphony orchestra requires a group of trained musicians with prearranged and rehearsed occasions but one that only occurs during a particular period of time as well as in a hall with limited seats. Hence, performed music is unlikely to capture audience numbers beyond current capacity of the concert venue. On the other hand, a museum is able to display numerous works with various styles, topics, and tastes simultaneously. Hence, it

²⁰ V. Zolberg, "Display Art and Performed Music: Selective Innovation and the Structure of Artistic Media", *Sociological Quarterly* 21, 1980, pp. 219-231.

is possible that a variety of visitors can make their own choices regarding which display they want to see, as well as how long they will remain in particular display rooms – often without infringing upon the access of other audiences. As a result of more constraints on time and space for performing arts, the numbers and variety of performing works are more limited than for displayed visual works, and the public access is much less for live performance than for visual display. According to Zolberg, increased costs that occur when more people go to the cultural and arts events is relatively little for display organizations such as museums but larger for performance organizations, as the deficits for the latter will be increased beyond the amount that the contributors are willing or able to cover if the numbers of performances are greatly increased. This suggests some constraints to innovation and adventuresome that the studies in the previous section do not address, as all focus on performance arts organizations.

In contrast, Victoria Alexander's²¹ research shows how display organizations manage the two distinct missions of nonprofit cultural organizations. Alexander examines the impact of funding on the display of art by using longitudinal data from 1960 to 1986 – which includes quantitative analysis of 15 American art museums with more than 4,000 exhibitions and qualitative analysis of 30 museums. When considering the impact of types of funding on the format of exhibitions, Alexander reveals that corporate and government entities largely sponsor traveling exhibitions and blockbuster exhibitions – both of which are considered as more popular exhibitions – while individuals and foundations sponsor more on patron's own collection. When considering the content of art exhibitions, government entities tend to sponsor scholarly types (modern, European, medieval-19th century, but not classical), and living artists types (postmodern and contemporary), but they tend to not sponsor commercial art, mixed styles, child-and-community-oriented art, and craft, costume, decorative, and folk art as an accessible type of art. Also, individual donors prefer both scholarly art (modern and classical) and accessible art (American old master, craft and costume). Finally, Alexander divides her data into two time periods (1960-72 and 1974-86) so as to investigate the changes in the format, content, and style of exhibitions after a notable increase in institutional funding. She finds that in the latter period, with increased institutional funding, both popular (blockbuster exhibition, traveling exhibition), accessible (theme exhibition), and scholarly (art-historical exhibition) formats increase, while patron collections decrease. For content, classical art, postmodern and contemporary art, photography, and other styles increase, while local artists' art and child or community oriented art decreased. However, the change of content is less significant than the change of formats, which indicates that the existence of museum curators' autonomy – as they work in various ways to balance the demands of external funders with their own aesthetic concerns.

²¹ V. D. Alexander, "Pictures at an Exhibition: Conflicting Pressures u Museums and the Display of Art", *American Journal of Sociology* 101, 1996, pp. 797-839.

While replication of Alexander's approach is beyond the scope of my study, it nonetheless shows the merit of distinguishing between types of nonprofit cultural organizations. Given the data available (see below) I will do so by comparing performance organizations to others when accessing marketing strategies and their attendant efficacies.

6. Moving Beyond Programming: The Importance of Marketing

While all of the studies discussed above deal with the programming of nonprofit arts organizations – using such programmatic elements as innovation and risk to get at the tensions between artistic and utilitarian missions – Laura Scholz²² reminds us that the marketing efforts of such organizations are also important to consider, as they offer another way by which these organizations seek to balance aesthetic and economic concerns. Scholz demonstrates how the American Symphony Orchestra League (ASOL) and its members grappled with audience building in difficult times. Given negative publicity about symphony orchestras' financial instabilities in the late 1900s and about their lack of diversity in terms of the composition of their audience and musicians – and given the absence of public policy on how to deal with these problems – the League endeavored to diagnose and treat these problems and, thus, to build future audiences for orchestral music. The League found that the main causes of the fiscal crisis were increasing production costs and decreasing public grants, as well as the wane of private donations. The league thus suggested that symphony orchestras need to revitalize their roles in American society, where demographic and economic changes were happening. Therefore, League statements about the need to enhance diversity grew commonplace – such as the following: "...the new American orchestra is built on the diversity and vibrancy of the racial and cultural groups that comprise American society ad a whole, and each orchestra's community is particular" (Scholz, 2002: 141).²³ These statements would be matched by efforts on the part of various orchestras that belong to the League, as Scholz documents. For example, the Saint Louis Symphony launched partnerships with 25 African American churches, the Long Beach Symphony aggressively promoted educational opportunities in neighboring populations of various ethnic groups, and the Atlanta Symphony Orchestra courted the participation of African American students in its Young People's concert series.

Whereas Scholz hints at the variety of marketing strategies found among US orchestras, I draw on a unique survey to document the types and extent of mar-

²² L. Scholz, "Across the Private Policymaking Process: The Case of the American Symphony Orchestra League and Americanizing the American Orchestra", *Journal of Arts Management, Law & Society* 31, 2001, pp. 137-148.

²³ L. Scholz, op. cit., p. 141.

keting strategies among all types of nonprofit cultural organizations. As recent economic difficulties have made such strategies increasingly relevant for symphony orchestras,²⁴ I suggest that this is the case for all types of arts organizations. Hence, I first provide a rare documentation of these strategies before offering a statistical analysis that demonstrates how internal and external attributes of these nonprofits shapes the efficacies of their marketing strategies.

7. Data

This paper relies on an unusual dataset – a U.S. survey that captures the marketing strategies of nonprofit cultural organizations operating in five metropolitan areas. The Survey of Arts and Cultural Organizations was conducted in 2000 by the Urban Institute, and it was part of a series of surveys evaluating the Lila Wallace–Reader’s Digest Fund’s Community Partnerships for Cultural Participation (CPCP) Initiative.²⁵ Surveys were sent by mail to government or nonprofit art and cultural organizations in five geographic areas: the Kansas City metropolitan area; Humboldt County, California; Silicon Valley, California; Southeastern Michigan; and Boston, Massachusetts. Five hundred and fifty-three valid cases are in this dataset, representing a response rate of 33.4%. While that response rate may seem rather low, it is not that low when compared to other organizational surveys.²⁶

In the early findings report for the CPCP Initiative, we can see the reasons for the funder’s interest in this survey and, hence, its general purpose. The Lila Wallace–Reader’s Digest Fund (the Fund) has embarked on a broad-scale effort to extend arts and culture to more people in the United States. Currently, the Fund is pursuing a three-pronged strategy to enhance participation – working through leading cultural institutions, stimulating community-based initiatives, and using media and technology. The Community Partnerships for Cultural Participation (CPCP) Initiative is a component of the Fund’s community based strategy. It is supporting nine community foundations, which are, in turn, helping art, culture, and other organizations in their communities to broaden, deepen, and diversify participation...Through the CPCP Initiative, the Fund also hopes to spotlight the importance of arts and culture to community life, and strategies to enhance residents’ participation in these activities.²⁷

²⁴ L. Scholz, *ibidem*.

²⁵ This survey is available at the Cultural Policy and the Arts National Data Archive via the following link: <http://www.cpanda.org/stage/studies/a00219?view=summary>.

²⁶ See: F. Dobbin, J. R. Sutton, J. W. Meyer, R. Scott, “Equal Opportunity and the Construction of Internal Labor Markets”, *American Journal of Sociology*, 99, 1993, p. 409-410.

²⁷ The Urban Institute 2000: 1.

Given the funder’s interest and the survey’s purpose, the questions asked reveal information about the range of marketing strategies that these nonprofit organizations pursue in terms of building their audience. The questions also allow these organizations to gauge how successful they have been in such audience building – both in terms of general numbers and particular audience segments. I thus present descriptive information on the marketing strategies and their efficacies – doing so before I examining the simultaneous impact of such strategies, along with internal and external organizational factors – on these efficacies.

8. Results

8.1. The Extent and Range of Marketing Strategies in Five Metropolitan Areas

The survey gathered information of 14 distinct marketing strategies. In particular, the survey provided the following question: “Please indicate whether you made use of any of the following strategies to encourage more active participations.” Respondents then checked which of the fourteen strategies their respective organization employed. Eight of these strategies were listed in the original questionnaire (those that I label “A” through “H” in Table 1), while six were added to the code-book itself (strategies “I” through “N” in Table 1). Table 1 summarizes the general response patterns. Two things are worth noting there: the most commonly used strategies are advertising/marketing in new areas or media, co-sponsoring events with other organizations, and presenting new/different offerings, while the least common strategies are other audience service, scholarship, and transportation.

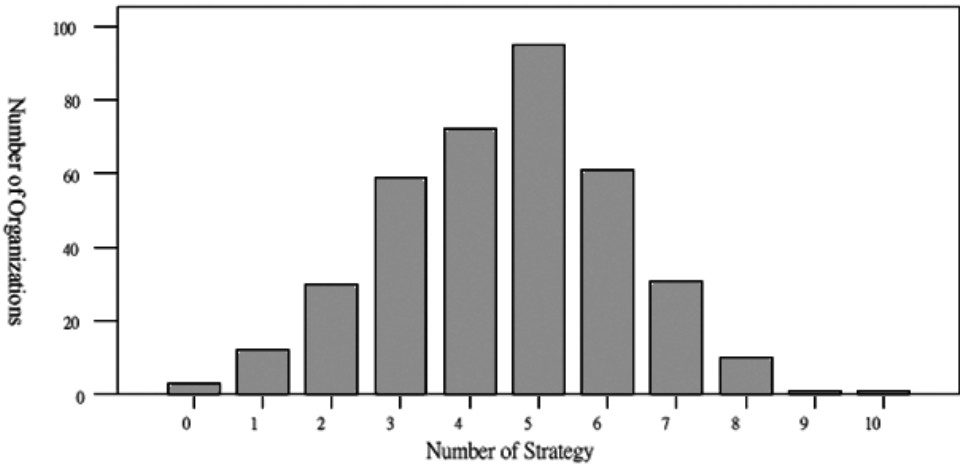
Table 1: *The Use of Fourteen Marketing Strategies by Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas*

Strategy	I=yes N(%)	0=no N(%)	Total N
A. Advertising/marketing in new areas or media	352(79.3)	92(20.7)	444
B. Presenting new/different offerings	381(68.9)	70(12.7)	451
C. Co-sponsoring events with other organizations	333(75.2)	110(24.8)	443
D. Audience service	76(18.2)	341(81.8)	417
E. Research/Planning	199(46.5)	229(53.5)	428
F. Arts instruction/education	250(57.7)	183(42.3)	433
G. Presenting work in new venues/places	270(61.4)	170(38.6)	440
H. Other	20(4.1)	466(95.5)	486
I. Free tickets	37(7.6)	450(92.4)	487
J. Low-priced tickets	80(16.4)	407(83.6)	487
K. Transportation	16(3.3)	471(96.7)	487
L. Audience service	29(6.0)	458(94.0)	487
M. Other Audience service	1(0.2)	486(99.8)	487
N. Scholarship	9(1.8)	479(98.2)	488

Source: Survey of Arts and Cultural Organizations (2000)

Of course, Table 1 does not address an important point: the extent to which given nonprofits cultural organizations make use of multiple strategies. Figure 1 summarizes the number of strategies used by each of the nonprofit cultural organizations. Note that three organizations employ no strategies, while only one employs the maximum of 10 strategies. Meanwhile, the average number of strategies is 4.5 among these organizations operating in five metropolitan areas.

Figure 1: *The Number of Marketing Strategies Used by Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas*



Source: Survey of Arts and Cultural Organizations (2000)

Given that the survey provides a quite large number of strategies, I use factor analysis to see if there are some underlying common dimensions among them. Rather than use all fourteen strategies listed in Table 1, for the factor analysis, I only focus on the first seven (Strategies A through G) because the other seven are so rarely used by the organizations in the survey. Table 2 contains the rotated factor loadings – the correlations between the various strategies and a given factor – with those loadings in bold font being the ones particularly high loadings. The factor analysis reveals three distinct factors – that is, marketing strategies that form somewhat of a coherent grouping the surveyed organizations. The first factor I label as “Reach and Teach” because the marketing strategies that load highly on it deal with arts education (Strategy F), research and planning (Strategy E) and the presentation of new and different offerings (Strategy B). Note that this grouping seems to tap the artistic missions of these organizations – particularly in terms of education and programmatic innovation. I label the second factor “Beyond Borders” because the marketing strategies that load highly are ones oriented to efforts that extend beyond a given organization – advertising in new

settings and cooperating with other organizations. The final factor is marked by one strategy that loads highly: audience service. Both the second and third factors appear to target the utilitarian mission of these organizations, as they deal with increasing exposure and audiences more than content.

Table 2: Factor Analysis of Marketing Strategies Employed by Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas

Marketing Strategies:	Rotated Component Matrix		
	Factor #1: <i>Reach and Teach Strategies</i>	Factor #2: <i>Beyond Borders Strategies</i>	Factor #3: <i>Audience Service Strategy</i>
(A) Advertising / marketing in new areas or media	-.169	.698	.231
(B) Presenting new / different offerings	.573	.147	-.119
(C) Co-sponsoring events with other organizations	.153	.668	-.118
(D) Audience service	.036	.003	.938
(E) Research / planning	.680	-.012	-.020
(F) Arts instruction / education	.699	.119	.271
(G) Presenting work in new venues / places	.295	.574	-.042

Source: Survey of Arts and Cultural Organizations (2000)

8.2. The Changing Audience in Five Metropolitan Areas

As others note, the environment for nonprofit cultural organizations has grown difficult in recent years – particularly in light of funding cuts and gray-ing audiences.²⁸ As a result, it is useful to see how the organizations in the survey view the state of their audience. These organizations were prompted to offer their view with the following question: “Please indicate whether there has been an increase, no change, or decrease over the past year in the following aspects of

²⁸ T. J. Dowd, K. J. Kelly, “Composing a Career: The Situation of Living Composers in the Repertoires of U.S. Orchestras, 2005-06”, in: *Careers in Creative Industries*, ed. by Christopher Mathieu, Routledge, London, 2011, pp. 210-233; M. A. Glynn, “When Cymbals Become Symbols: Conflict over Professional Identity within a Symphony Orchestra”, *Organization Science* 11, 2000, pp. 285-298; M. A. Glynn, “Chord and discord: Organizational crisis, institutional shifts, and the musical canon of the symphony”, *Poetics* 30, 2002, pp. 63-85; L. Scholz, “Across the Private Policymaking Process: The Case of the American Symphony Orchestra League and Americanizing the American Orchestra”, *Journal of Arts Management, Law & Society* 31, 2001, pp. 137-148.

participants in your organization's programs or activities." Table 3 summarizes the response across all the organizations that answered this question.

Table 3: *The Growth in Audiences and Audience Segments among Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas*

Audience / Audience Segment:	Increase During Past Year	No Increase During Past Year	Total
	<i>N</i> (%)	<i>N</i> (%)	<i>N</i>
Overall numbers	365(67.7)	174(32.3)	539
Racial/ethnic composition	213(41.4)	301(58.6)	514
Community residents	146(29.4)	351(70.6)	497
Young people or families	212(41.6)	298(58.4)	510
Lower-income persons	128(25.8)	369(74.2)	497

Source: Survey of Arts and Cultural Organizations (2000)

The descriptive results show that a large portion of organizations indicate that they have seen an increase in the overall number of audiences – with nearly 68% having this view. Furthermore, a good portion of organizations have also seen increase in various audience segments, such as among people of color, and young people (see Table 3). However, this table also shows the challenges that face nonprofit cultural organizations because more have *not* experienced growth among key audience segments than have. Thus, an important question becomes what predicts which organizations do well in audience building in terms of overall numbers, as well as various audience segments? That question thus addresses the issue of efficacy.

8.3. *The Efficacy of Audience Building in Five Metropolitan Areas*

8.3.1. Methods and measures

I approach efficacy by examining what factors matter for five types of audience building detailed in Table 3 – whether or not, over the past year, there have been an increase in (1) the overall number of audience members, (2) the racial / ethnic diversity of audience members, (3) the number of audience members who are from the surrounding community, (4) the number of audience members who represent both the young and families, and (5) the number of audience members drawn from those with lower-incomes. Given that each of these types represents a dichotomous outcome (an increase vs. no increase), I rely on logistic regression. This statistical technique allows me to compare the simultaneous impact of various predictors on the likelihood of a given outcome (e.g., the odds that there has been an increase in lower-income audience members); in doing so, it also allows

me to gauge which of these predictors play a significant role in shaping an outcome and which do not.

One set of predictors that I use are drawn from the marketing strategies described above – particularly those emerging from the factor analysis in Table 2. I use Factors 1 and 2 to create weighted scales that tap these broad types of marketing strategies. For Factor 3, I only use strategy D (audience service) because it loaded particularly high. The scales are calculated as below:

Reach and Teach Scale = $.573*(Use\ of\ Strategy\ B) + .680*(Use\ of\ Strategy\ E) + .699*(Use\ of\ Strategy\ F)$

Beyond Borders Scale = $.698*(Use\ of\ Strategy\ A) + .668*(Use\ of\ Strategy\ C) + .574*(Use\ of\ Strategy\ G)$

Audience Service = $(Use\ of\ Strategy\ D)$.

These predictors allow me to see whether or not those nonprofits with a marketing focus on the artistic mission (“Reach and Teach”) and / or the utilitarian mission (“Beyond Borders” and “Audience Service”) are also those that are likely to enjoy an increase in audience size and audience segments. Of course, it may not be the substance of the marketing strategies that matter as much as it is the sheer amount. As a result, I also see how the number of marketing strategies shapes the odds of success in audience building. These numbers are the one detailed in Figure 1.

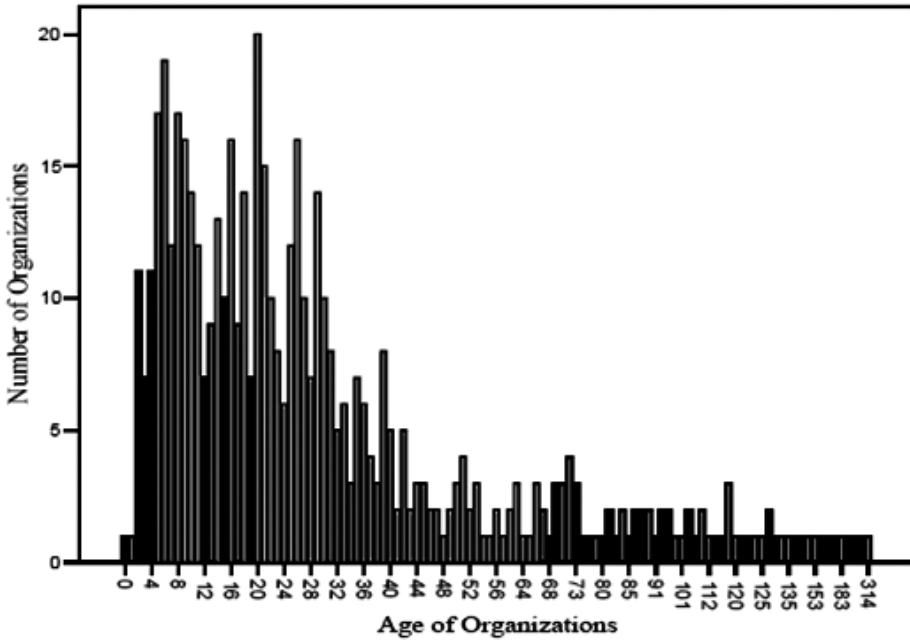
If case studies of nonprofit cultural organizations direct our attention to such things as artistic and utilitarian missions,²⁹ then studies of groups of such organizations draws our attention to internal and external attributes that vary across those organizations³⁰ – another set of predictors that may also shape the efficacy of audience building. Regarding factors internal to a given nonprofit cultural organization, I investigate the following four.

(1) *Age of organization*. When discussing the extent of “institutionalization” among nonprofit cultural organizations, DiMaggio and Stenberg suggest that organizational age may play a role in how they operate and the choices that they make; perhaps it also matters for audience building. The survey posed the following question to respondents: “In what year was your organization founded?” This allowed me to calculate the year of each organization by subtracting its founding year from the year of the survey (2000). Figure 2 shows the age distribution for all the organizations participating in the survey. A good number of them are younger than 40 years (77%) – with the average age being some 34 years of age. The youngest organizations are younger than one year old, and the oldest is an astounding 314 years.

²⁹ E.g., M. A. Glynn, “When Cymbals Become Symbols: Conflict over Professional Identity within a Symphony Orchestra”, *Organization Science* 11, 2000, pp. 285-298.

³⁰ E.g., P. DiMaggio, K. Stenberg, “Why Do Some Theatres Innovate more than Others? An Empirical Analysis”, *Poetics* 14, 1985, pp. 107-122.

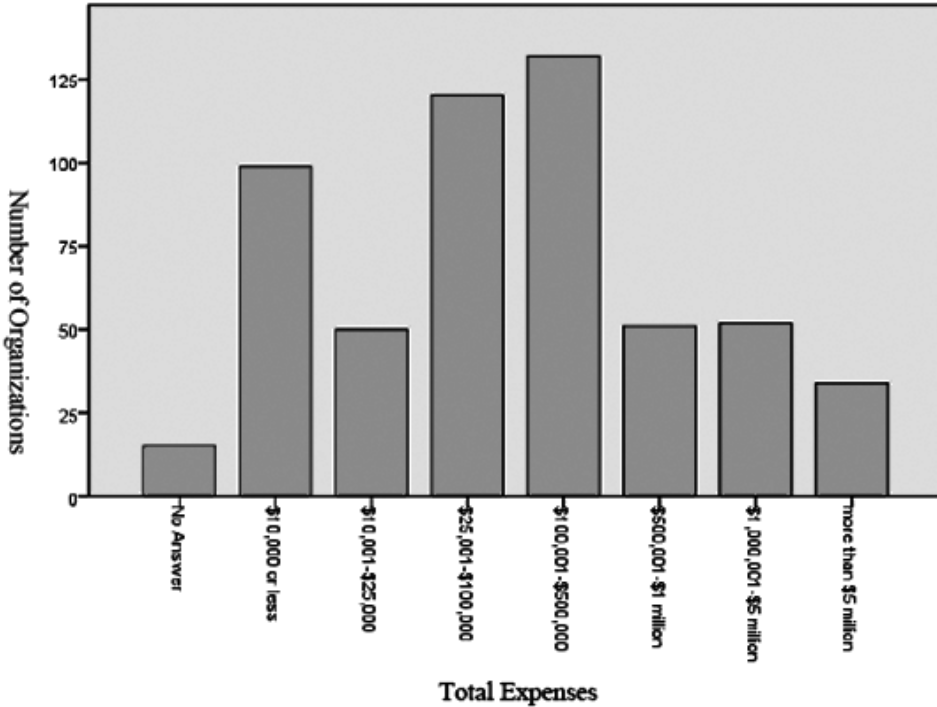
Figure 2: *The Age Distribution of Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas*



Source: Survey of Arts and Cultural Organizations (2000)

(2) *Size of organization.* Like Dowd and Kelly (2011), I gauge size by looking at budget-related aspects of the organization – seeing if it has ramifications for audience building. The survey asked the following question: “What were your total expenses for the most recent fiscal year?” The eight responses possible are depicted in Figure 3. Influenced by Urban Institute (2000), I recoded nonprofit cultural agencies into two sizes: those that are “small” (with annual expenses under \$500,000) and those that are “large” with annual expenses of \$500,000 or more. This resulted in 401 large organizations, 137 small ones – and 15 that did not answer the question and, hence, are not included in the analysis.

Figure 3: The Total Expenses for Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas

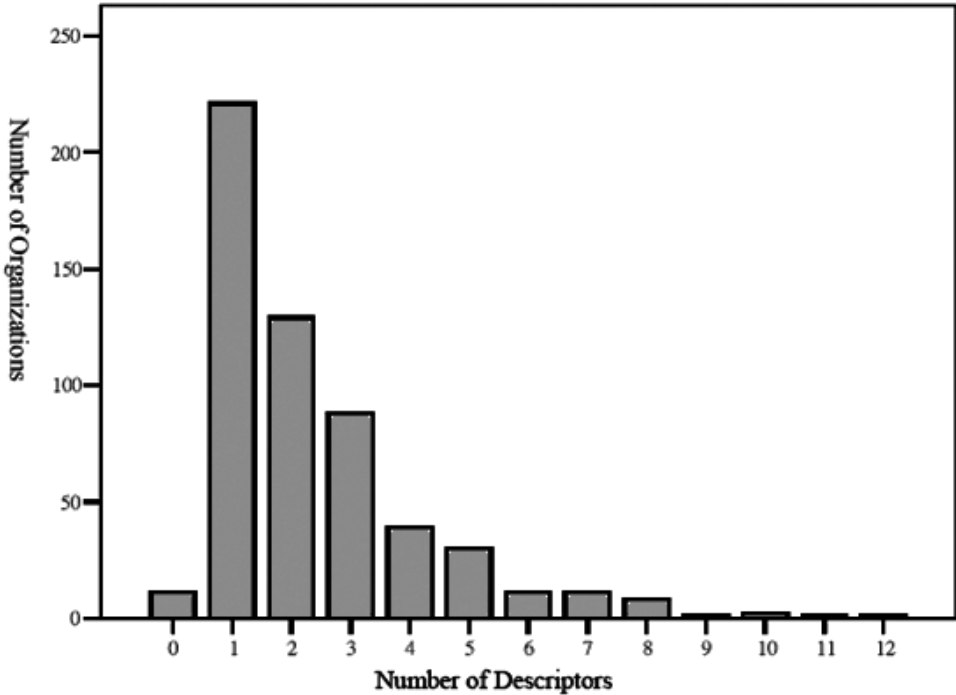


Source: Survey of Arts and Cultural Organizations (2000)

(3) *Specialization.* Dowd and Kelly (2011) find that arts organizations that are specialists tend to diverge from others in terms of programming choices. I see if such specialization likewise shapes the ability to build audiences. The survey gets at this by asking, “Which of the following descriptors [which total 19 in number] apply to your organization? Check all that apply.”³¹ Figure 4 shows the distribution of descriptors in terms of numbers. 221 of the organizations in the survey only claim one descriptor. The average number of descriptors claimed is 2.4 with the maximum number of descriptors claimed by one organization in the survey. For purposes of analysis, I code organizations as “specialist” if they only do one thing (versus doing multiple things).

³¹ The 19 descriptors are (1) arts council / agency; (2) humanities council / agency; (3) library; (4) performance / exhibition space; (5) historical organization / site; (6) service organization; (7) “friends of” / support; (8) performing group; (9) art museum; (10) other museum; (11) presenting organization; (12) fair / festival; (13) arts incubator; (14) publisher; (15) media; (16) arts center; (17) school / teaching facility; (18) part of larger institution; and (19) other.

Figure 4: *The Total Number of Descriptors Claimed by Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas*



Source: Survey of Arts and Cultural Organizations (2000)

(4) *Performance organization.* Zolberg³² notes that performance organizations face constraints in audiences that other arts organizations do not face – thus, I see if such constraints extend to audience building. The survey queries organizations about, “What types of arts and cultural activities does your organization present? Check all that apply.” They are coded as “performance organizations” if they check one of the following: music; dance; theater; opera / music theater; performance / spoken word; and story telling / oral history. Such activities require a live presentation and cannot be merely displayed³³. 429 of the organizations in the survey are devoted to performance.

Regarding factors external to the organization, the survey allows me only to investigate the location of an organization in a city rich with cultural and artistic

³² L. Zolberg, “Display Art and Performed Music: Selective Innovation and the Structure of Artistic Media”, *Sociological Quarterly* 21, 1980, pp. 219-231.

³³ The “non-performance” choices are painting / drawing; photography; sculpture; design arts; crafts; architecture; media arts; new media; literature / poetry; other; educational workshops; history; cultural presentations; and exhibits.

heritage.³⁴ I see if such a location has implications for audience building. Given the five metropolitan areas addressed in this survey, I heed those located in Boston versus those located in other areas. This makes sense because DiMaggio (1982) describes Boston as the location where nonprofit arts organizations first emerged and, in turn, enabled the “arts” (i.e., high culture) to take root in the United States. 171 of the organizations in the survey are located in the Boston metropolitan area.

8.3.2. Descriptive statistics and correlations

Table 4 provides an overview of all the predictors to be used in the logistic regression. The correlations are particularly notable, as they reveal that most of the predictors are not highly correlated. There are a few exceptions, however. First, age and size are modestly correlated at .38, which means older organizations tend to be larger. This is consistent with DiMaggio and Stenberg’s (1985) finding in the study on theater companies, in terms of “institutionalization” – whereby both age and size are part of it. Second, the number of marketing strategies has relatively high correlations with both the Reach / Teach strategies (.73) and Beyond Borders strategies (.72). This indicates that as organizations pursue many strategies, they tend to tap both artistic and utilitarian missions. Also, the correlation between Reach/Teach and Beyond Borders is relatively low (.24); that is, organizations that pursue one type of mission (e.g., artistic) do not necessarily pursue the other.

Table 4: Means, Standard Deviations and Correlations for Predictors Addressing Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas

	Mean	SD	Pearson correlations								
			(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	
Organizational Age (in Years)	33.48	36.10	1.00								
Organizational Size (0=Small; 1=Large)	0.25	0.44	0.38	1.00							
Specialization (0=No; 1=Yes)	0.41	0.49	-0.05	-0.02	1.00						
Performance Organization (0=No; 1=Yes)	0.78	0.42	-0.03	0.04	0.00	1.00					
Location: Boston (0=No; 1= Yes)	0.31	0.46	0.17	0.05	0.00	0.08	1.00				
Number of Marketing Strategies	4.52	1.70	-0.03	0.14	-0.16	0.12	0.00	1.00			
Reach and Teach Strategies (scale)	1.12	0.62	0.04	0.23	-0.11	0.01	0.03	0.73	1.00		
Beyond Borders Strategies (scale)	1.38	0.57	-0.03	0.05	-0.14	0.05	0.02	0.72	0.24	1.00	
Audience Service Strategy (0=No; 1=Yes)	0.18	0.39	0.01	0.03	-0.06	0.07	-0.04	0.19	0.07	0.06	1

Source: Survey of Arts and Cultural Organizations (2000)

³⁴ See: P. DiMaggio, K. Stenberg, “Why Do Some Theatres Innovate more than Others? An Empirical Analysis”, *Poetics* 14, 1985, pp. 107-122.

8.3.3. Logistic regression analyses

Table 5: *Logistic Regression for Efficacies of Audience Building by Nonprofit Cultural Organizations in Five U.S. Metropolitan Areas*

	Increase in Overall Numbers (Yes)		Increase in Racial/Ethnic Composition (Yes)		Increase in Community Residents (Yes)		Increase in Young People or Family (Yes)		Increase in Lower-Income Persons (Yes)	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Intercept	1.256	1.178	0.378	0.389	0.162	0.167	0.173	0.167	0.114	0.103
Organizational Age	0.990*	0.989*	0.996	0.996	0.998	0.998	0.997	0.997	0.988*	0.987*
Organizational Size	0.928	0.947	1.815*	1.896*	1.385	1.438	1.101	1.194	0.944	1.085
Organizational Specialist	0.643+	0.610+	1.101	1.112	0.725	0.745	0.759	0.749	1.171	1.262
Performance Organization	0.949	1.054	0.729	0.692	1.088	0.986	0.931	0.931	0.806	0.642
Location in Boston	2.082*	2.287**	1.564+	1.534+	1.393	1.364	1.208	1.248	1.782*	1.833*
Reach and Teach Strategies	1.444+	2.339*	1.070	0.818	1.398	0.890	2.183**	2.101*	1.674*	0.670
Beyond Borders Strategies	1.601*	2.625*	1.771**	1.363	1.622*	1.038	1.729*	1.686	1.795*	0.705
Audience Service Strategy	2.757*	3.801**	1.970*	1.778-	1.433	1.218	2.471**	2.615**	1.412	1.118
Number of Marketing Strategies		0.794		1.169		1.305		1.027		1.775**

**p<.01 *p<.05 +p<.1 (2-tailed test)

Source: Survey of Arts and Cultural Organizations (2000)

Table 5 shows the results of logistic regression models that examine the impact of organizational attributes (both internal and external) and marketing strategies (both types and sheer number) on five types of audience building – with the latter referring to general audience size as well as to particular audience segments (e.g., young people and families). Given the nature of logistic regression, the numbers reported in Table 5 are exponentiated coefficients of the regression models – otherwise known as “odds ratios.” Odds ratios greater than 1 indicate a positive relationship between a predictor and the dependent variable (the outcome), while odds ratios less than 1 indicate a negative relationship. In Model 1, for example, the coefficient of 2.082 for “Location in Boston” indicates that Boston nonprofits 2.1 times more likely to have increase in the overall number of audience members than those nonprofits located in the other metropolitan areas. Note that those coefficients marked by symbols (such as **) are significant in terms of their impact on a particular outcome. Also note, that for each of the five outcomes (e.g., Increase in Overall Numbers), I run two different models. I do this because of the high correlation existing between the “Number of Marketing Strategies” with both the “Reach and Teach” and “Beyond Borders” strategies. In order to ensure that such correlation is not distorting the regression

analyses, I first run a model without the number of strategies and then include it a second model. A comparison of the five pairs of regression models (e.g., Model 1 vs. Model 2) reveals that the substantive results for both pairs are mostly similar, with the exception of the types of marketing strategies – so interpret those with caution.

The results in Table 5 thus indicate that, first, when look at the type of marketing strategies these organizations pursue, those emphasizing a Reach / Teach approach – that is, favoring the artistic mission – are more likely to have an increase in overall numbers; though this effect is much stronger when controlling for the sheer number of strategies. Specifically, Reach / Teach positively impact the odds attracting young people and families, and it initially appear to increase the odds of attracting lower-income persons – however, what is really driving that relationship is the total number of strategies. Beyond Borders has a positive impact on over overall increase, and it also matters for all the other outcomes – but not when controlling for the sheer number of strategies. Finally, the audience service strategy is particularly good at boosting overall numbers and young people / families. Second, when look at internal factors, the results show that younger nonprofit cultural organization are more likely to see an increase in overall and lower-income audiences, while bigger organizations only more likely to have an increase in racial diversity. Also, it is less likely for specialist organizations to see an increase in overall numbers, while organizations presenting performing arts show no difference with organizations presenting other art works on every dimension of audience augmentation – which tells an alternative story from what Zolberg (1980) suggests. Finally, for external factors, organizations in Boston are more likely to see an increase in overall number, racial diversity, and lower-income persons than those in other areas.

9. Conclusion

Scholars of the arts note that the U.S. environment has proven difficult as the 1900s gave way to the 2000s – with the problems such as decline in funding and aging audience. Given this, the actual attempts to build the audience by nonprofit arts organizations become an important topic of focus. To get at this, I turn to a survey conducted in 2000 – right amidst these changing and challenging times – one that addresses various types of nonprofit cultural organizations that ranging from museums and theaters to libraries and historical sites. This survey reveals that most of these organizations are involved in efforts to build their audiences in some way – pursuing marketing strategies to that end. Not only do many pursue multiple types of strategies – I also find, via factor analysis, three broad types of marketing strategies – those seeking to reach and teach and those seeking to build beyond borders, as well as service the audience. These

broad types map onto the competing missions that Mary Ann Glynn³⁵ and others have described – strategies that address the artistic mission and those that address the utilitarian mission. Given the low correlations between the strategies, the tension becomes evident – with some favoring the artistic mission and others favoring the utilitarian, and relatively few doing both.

These strategies are not in vain. Despite the hardships facing the arts in the early 21st century, a majority of these organizations see that their overall audiences have increased. However, most have not had as much success in recruiting particular audience segments – with low income and community residents among the hardest to reach. Yet, what of their actual marketing strategies? Here, we see a mixed bag. While Reach and Teach has some positive impact on overall numbers and young people / families, and Beyond Border has some positive impact on overall number – neither one offers a consistent impact. Hence, in seeking to expand notable segments of their audience – neither type of strategy offers a clear path to success. Here again, the tension between artistic and utilitarian missions becomes clear – as favoring either one does not provide a ready remedy to building and diversifying the audience.

Moreover, marketing strategies are not the sole factors that impinge on audience building. On the one hand, older organizations tend to be less adept in two ways – thereby going along with DiMaggio & Stenberg's (1985) finding which suggests that organizations' age may bring conservatism. On the other hand, larger orgs are adept at increasing racial diversity alone, which shows that size does not always lead to conservatism – as Dowd's (2004) finding for media organizations. Meanwhile, specialist organizations are significantly less likely to see an increase in overall numbers – which is not surprising given their linkage to small segments of audiences, as Dowd & Kelly (2011) find that specialist larger orchestras tend to reduce the diversity of repertoire; what is surprising is that specialization has no significant impact on the segments examined in this study. Finally, one external factor matters a fair amount – just as NYC is a hotbed for the theater and orchestral music (DiMaggio & Stenberg, 1985; Dowd & Kelly, 2011),³⁶ and London is for theater,³⁷ so too is Boston for all types

³⁵ M. A. Glynn, "When Cymbals Become Symbols: Conflict over Professional Identity within a Symphony Orchestra", *Organization Science* 11, 2000, pp. 285-298; M. A. Glynn, "Chord and discord: Organizational crisis, institutional shifts, and the musical canon of the symphony", *Poetics* 30, 2002, pp. 63-85.

³⁶ DiMaggio, K. Stenberg, "Why Do Some Theatres Innovate more than Others? An Empirical Analysis", *Poetics* 14, 1985, pp. 107-122; T. J. Dowd, K. J. Kelly, "Composing a Career: The Situation of Living Composers in the Repertoires of U.S. Orchestras, 2005-06", in: *Careers in Creative Industries*, ed. by Christopher Mathieu, Routledge, London, 2011, pp. 210-233.

³⁷ O'Hagan, A. Neligan, "State Subsidies and Repertoire Conventionality in the Non-Profit English Theatre Sector: An Econometric Analysis", *Journal of Cultural Economics* 29, 2005, pp. 35-57.

of nonprofit cultural organizations in terms of audience building. The most consistent effect is found for this particular predictor; however, in some ways that is the most troubling: while Boston is the seedbed for arts organizations in the U.S. (DiMaggio 1982), locating there is not a viable option for organizations located elsewhere.

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ASSISTANT PROFESSOR SRĐAN ŽIKIĆ, PHD*

Graduate School of Management, Zaječar, Megatrend University, Belgrade

ASSISTANT PROFESSOR ANETA MARINOVIĆ, PHD

Graduate School of Public Administration, Megatrend University, Belgrade

ASSISTANT PROFESSOR IGOR TRANDAFILOVIĆ, PHD

Graduate School of Management, Zaječar, Megatrend University, Belgrade

PROMOTION OF CONFLICT MANAGEMENT STRATEGIES IN TERMS OF MODERN BUSINESS

Summary

Contemporary understanding of the conflict represents a belief that conflict is not only a positive force of one group, but it is also absolutely essential for achievement of the efficiency of the group. Given the inevitability of conflict and its functional role in the organization, management has the task to manage these processes effectively and not to eliminate them. The results of the research that included a sample of 100 respondents have shown that collaboration and adjustment are the dominant strategies in managing interpersonal conflicts in the group. Research has shown that over 80% of respondents always or often solve the current issues of in a mutually acceptable way, exchanging accurate information with colleagues in order to solve common problems. Also, most respondents openly try to present facts in order to resolve the problem efficiently. The respondents have shown to have inefficient knowledge of advanced techniques of conflict resolution such as “give and take” method with the aim of achieving a compromise, which is otherwise successfully used in organizations around the world.

Key words: *conflict, conflict management, conflict management strategies*

JEL classification: D74, M14

1. Introduction

A society that we live in is characterized by numerous divisions, discontent, social unrest, as well as mass gathering of workers and citizens. Among these phenomena an important role is played by labour conflicts, which primarily express dissatisfaction of the employees and their struggle to achieve certain require-

* E-mail: srdjan.zikic@fmz.edu.rs

ments. When labour productivity in a company starts to decline, the question arises: "Why does this happen?" The answer lies primarily in the fact that the process of improving the company management system did not occur along with the development of productive forces and social changes that took place.

The modern methods of doing business are characterized in the first place by constant organizational changes. These changes are numerous and diverse, their common characteristics being that they always reflect on the employees and their interrelations. Every organization has a particular corporate culture with the already established social relationships that may be broken by certain changes. In many companies the organizational changes are not accompanied by appropriate programs and measures that would help employees to a larger extent to adjust to new job requirements. Employees are often forced to find their own ways of solving interpersonal problems that arise as a result of fear of losing their jobs and privileges. Deterioration of the general climate and interpersonal relationships greatly contributed to the creation and intensification of different types of conflicts at work.

Such conflicts can be solved by appropriate methods and techniques; they can be maintained and directed to the efficient achievement of both the goals of the organization, and through them, the goals of workers. In order to maintain good relations among people the skills of effective conflict management are essential. However, the lack of constructive resolution of conflicts is an essential and inexhaustible source of disharmony in relationships, thus reducing individual and organizational performance.

If the conflict is not managed properly, it can have unintended consequences such as hostility, violence, destruction of relationships among people, and even the disintegration of the company. When under control, a conflict can have many positive characteristics. It can stimulate creativity, innovation, changes, and may even lead to better relations among people. The absence of conflicts in the organization leads to apathy, stagnation and the inability to adapt to organizational changes.

Resolving conflicts in everyday life poses a significant problem that can be handled in two ways - one can choose to ignore it and therefore continue to live with unresolved problems, or one can discover the source of the conflict and take positive steps toward the change.

Without an analytical and systematic approach to the problem that causes a conflict, plenty of frustration and dissatisfaction of the conflict participants is possible, having in mind that the conflict remains silently active over the years. It is no surprise that some of the organizational analysts keep pointing out that no skill is as important for the effectiveness of an organization as constructive management and resolution of conflicts.

Starting from the facts given above and numerous studies, the aim of this study was to examine which technique of conflict resolution and management is used most often by employees working in our organizations.

2. Definition and interpretation of conflict

If different forms of conflict are taken into account such as, for example, conflicts of nations, ideologies, religions or group conflicts which include conflicts at work, it can be concluded that the conflict is one of the most important topics of research in social sciences. There are several interpretations of the conflict because this phenomenon is manifested in different ways and has different causes and effects. Differences in interpretation of the conflict result from different orientations in an effort to resolve and overcome conflicts. One thing that different approaches agree on is that conflicts are essentially clashes among people. These clashes arise from differences of values and interests of opposing parties, those parties being individuals, groups or entire organizations¹.

Although they seem to have a fundamental social relation and take place between two or more people, conflicts basically have a psychological core. The psychological core of the conflict is made by the frustration of basic needs. This underlining of the psychological dimension of a conflict is particularly important in the process of conflict resolution. Even when the sources are removed and a compromise is reached, the consequences of frustration remain, what also needs to be resolved. What also remains is stress, dissatisfaction and the need to get even, all of these the consequences of the need for hurt self-esteem.

Psychological, sociological and organizational theories of conflict have defined a series of approaches to this problem. There are two basic interpretations of conflict, one of which explains a conflict as a socially positive and the other as a socially negative phenomenon. Pluralist interpretation of conflict is related to the famous philosophical doctrine, pluralism. The starting point of this doctrine is a society organized in a way that enables and encourages the expression of interests of all its parts and members. Conflicts are the means of expression of those various groups' and individuals' interests. They assume the characteristics of desirable and necessary social relations. If the society has multiple power centres and more conflicts among them, it will function better. According to a pluralistic view conflicts are very important and desirable phenomena for the organization, but also for the society as a whole. In this regard companies should establish such relations that will enable its members to express their own needs freely, while they should take responsibility for their own proposals and the functioning of the organization. It is good and desirable that the

¹ N. Adler, *International dimensions of organizational behavior*, Fourth edition, South - Western Thomson Learning, 2002.

members confront each other, engage in dialogues and thus express their views and interests. In that way a variety of interests makes it possible for the company to find the optimal solution.

Contrary to the pluralist interpretation of conflict, there is a view that is based on the understanding of human relationships. This interpretation originates from the well-known research of Elton Mayo and other researchers in the field of human relations, whose results have played an important role in understanding the psychology of work and organization, introducing the dimensions of a personality, satisfaction, motivation, and informal organization. According to this view conflicts are undesirable, because they mean disturbance of normal and healthy relationships among people. They break communication and interaction among group members. In this view conflicts are undesirable, should be avoided at all costs and eliminated the functioning of an organization. According to their starting points and assumptions, the two main interpretations of the conflict are mutually contradictory. It is somewhat difficult to understand that a phenomenon should be explained, and also used, in a diametrical manner. The basic tenets of opposing viewpoints are presented in Table 1².

Table 1: *The basic tenets of the views of the nature of conflict*

The interpersonal relationships researchers' views	The pluralist view
Conflict is generally not desirable and should be avoided and resolved.	Conflict is desirable it should be encouraged; conflict must be directed so as not to get out of control.
Conflict is unavoidable.	Conflict is unavoidable.
The conflict arises from the blockage of communication and lack of understanding, trust and openness among different parties.	The conflict arises from the struggle for the goods which are scarce, whether it is a resource, position, responsibility or power; to a lesser degree it arises from the innate aggressive instincts.
Environment plays a major role in shaping of behaviour. Therefore, any inappropriate behaviour such as aggression and competitiveness, derive from the circumstances in the environment which can be changed.	The role of environment in the emerging of conflicts is overrated; there are many determinants of behaviour which may cause aggressive behaviour.
Man is basically good: trust, cooperation and goodness are the main features of human nature.	Although man is not bad by nature, he is motivated by aggressive, egoistic and competitive instincts.

Source: R. Bojanić, *Psihologija međuljudskih odnosa. Konflikti na radu*, Centar za primenjenu psihologiju, Beograd, 2009, p. 225.

² R. Bojanić, *Psihologija međuljudskih odnosa. Konflikti na radu*, Centar za primenjenu psihologiju, Beograd, 2009.

3. Conflicts in organisations

Conflicts are an important social phenomenon. They have a powerful influence on human behaviour in organizations, which brought them into the focus of scientific interest for many researchers and managers. In one study, managers reported that they spent 20% of their time on studying and resolving conflicts in their organizations, which puts them at the top of managerial attention. Conflicts are a feature of human behaviour, but they also reflect the content of human conscious and unconscious processes. The number and frequency of conflicts rises along with the growth and development of companies, and with the increase of the number of internal interaction and communication. Conflict is a form of interaction in the organization, i.e. a form of struggle among individuals, formal and informal groups, organizational units and teams. It can also be said that the conflict in the organization represents a situation in which one of the opposing parties achieves its goals and interests at the expense of the other.

There are different types of conflict. On the one hand, conflicts can be dysfunctional, i.e. negative because they prevent any further action and lead to new disputes and disruption of communication. On the other hand, conflicts can be functional or productive, and they occur as a result of different attitudes and lead to better solutions to problems. What form the conflicts in organizations will take depends primarily on the ability of managers to manage those conflicts³.

Each conflict in the organisation is characterised by three elements:

- There have to be at least two parties for the conflict;
- The conflicting parties can be individuals or groups;
- The conflicting parties' interests are opposed.

The following make an integral part of every conflict in the organization:

- a conflict situation,
- a conflicting action.

A *conflict situation* in the organization represents a particular condition and climate of the latent danger of the emergence and manifestation of the conflict. A *conflicting action* is a form and manner of the conflict expression. The most common conflict situation causes a conflicting action.

It can be argued that conflicts in the organization are essentially a negative phenomenon because they often have a destructive character. They are a sign that a certain state of equilibrium is violated in the company. Therefore, most authors treat them as a cause of disorganization, as the centrifugal force seeking for destruction and disintegration of the collective. Conflict disorganizes the work of the company, causes nervous tension and affects the psychological well-being of people. The conflicting parties think more about the conflict and less

³ J. Greenberg, R. Baron, *Ponašanje u organizacijama – razumevanje i upravljanje ljudskom stranom*, Biblioteka "Klasici menadžmenta", Beograd, 1998.

about their job. Personal animosity rises with this, good qualities are suppressed, and the bad ones are encouraged with the opposing parties. Mental stress and excitement often cause stress, aggression, depression and so on among employees, which causes numerous psycho-somatic disorders, and even suicidal condition. The consequences of this situation are common sick leaves, paid leaves, as well as loss of working ability and motivation.

Some authors describe this attitude towards the conflict as “traditional” because conflict is treated as an undesirable and harmful phenomenon that should be avoided in every way. In contrast to this, the so-called modern attitude views conflicts as a normal and inevitable phenomenon in the organization which derives from the very fact that people work together and share the same resources available. It is believed that they have numerous positive effects on the organization and employees because they bring a certain dynamics and creativity.

In any case the appearance of a conflict indicates that there has been a violation of a state of balance in the organization, organizational behaviour and human relations of staff. If conflicts are a result of the poor state in an organization, disturbed interpersonal relationships in a group and fighting for authority, position and power, they represent a harmful phenomenon. Such conflicts are referred to as destructive, and greatly hinder the performance of one’s duties and tasks. However, if they lead to change, overcoming and resolving of problems in the organization, they are useful and desirable. Such conflicts are referred to as constructive and positive organizational phenomenon⁴.

Conflict refers to a situation in which individuals or organizational units work against each other instead of working with each other. It is a process that begins when one party perceives that the other is taking or intends to take action that threatens its interests. According to one of the many definitions, organizational conflicts mean disagreement between two or more members of an organization or a group that might arise due to the division of scarce resources and tasks, whereby the conflicting parties have different goals, attitudes and perceptions.

To determine a situation as a conflicting, the following elements need to be present:

- previous conditions for the emergence of conflict: the lack of resources, wrong policy of the organization, poor reward system, the wrong perceptions of the group;
- affective conditions of groups of individuals: stress, tension, hostility, anxiety etc;
- cognitive status of individuals and groups: the belief, conscience, knowledge of a conflicting situation;
- conflict behaviour ranging from passive resistance to aggression.⁵

⁴ M. Jovanović, M. Živković, T. Cvetkovski, “Sukobi i konflikti u organizaciji”, *Organizaciono ponašanje*, Megatrend univerzitet, Beograd, 2003, p. 172-174.

⁵ S. Robbins, *Organizational Behavior*, Englewood Cliffs, Prentice Hall Inc., NJ, 2003.

4. Types of conflicts in organisations

Conflicts can be classified in several ways. From the viewpoint of organizational behaviour and the fact that the participants in the conflict in an organization can be individuals or groups, conflicts can be divided into:

- *organisational*,
- *personal (individual and group)*.

Organizational conflicts arise within the organization and are linked to its components and relations, i.e. for the organizational structure, organizational culture, organization climate, the system of decision-making and remuneration, personnel policies etc. According to the level at which they occur, these conflicts can be divided into: *horizontal* and *vertical*.

Horizontal conflict is manifested as the opposition of interests among individuals at the same organizational level within the company. Conflicts can occur because of lack of harmonization of the development level of different business functions or differential treatment by management.

Vertical conflict is the one that occurs at different organizational and hierarchical levels, i.e. that is formed between the upper and lower levels of the organization. A conflict between managers and employees represents a very important form a vertical conflict for the performance of an organization. The basis of this conflict is the psychological distance, or difference in status and ideology between managers and employees. Autocratic leadership style contributes most to the occurrence of a vertical conflict, whereas a democratic style contributes least to it.

Personal conflicts arise from the very personalities and relationships among employees within the workplace, group or team in the organization. They arise due to personal reasons, which may be reflected in the character of the person, the wrong perception, poor communication, and the like. These conflicts are focused on the personality and interpersonal relationships within the organization. This group is said to include conflicts caused by the struggle between personalities, members of the same or different groups and teams which are in the first place in a kind of interaction. This group of conflicts includes:

- intrapersonal conflicts,
- interpersonal conflicts and
- role conflicts.

Intrapersonal conflicts are caused by the conflict of motives, goals and possibilities of their realization. They are related to psychological being and its internal processes in which emotions, experiences and perceptions are shaped. They are manifested in the form of psychological effects such as apathy, anxiety,

depression, frustration, but also as physical consequences, among which are the most prominent are fatigue, aggression, alienation...

Interpersonal conflicts are those among individuals who interact within the same or different groups. These conflicts are one of the most common and most typical kinds of conflicts in the organization. It can be argued that all other kinds of conflicts can in a way be reduced to interpersonal conflicts. The participants in these types of conflicts are two or more individuals, and the causes can be personal hostility, violation of personal interests or differences of opinions, attitudes, perceptions, and the like.

Role conflicts are the kind of personal conflicts that arise when individuals in an organization have two or more mutually conflicting roles. They can also occur when an individual is unable to meet expectations regarding the function, position or job, because his personal resources (knowledge, skills and abilities) are insufficient. The following situations are possible.

- *Conflicts among the demands of one role* - occur in middle-level managers who are at the same time members of the management teams at higher levels. They are expected to represent simultaneously the interests of their organizational units and those of the organization as a whole.
- *Conflicts of many different roles* - a classic example of this conflict is the clash of the roles of a working woman, whereby the roles of wife, mother and housewife face the role of an individual responsible for a particular work in the organization.
- *The conflict between the personality and roles* - occurs in a situation where an individual is unable to fulfil the expectations required by the role he/she plays in the organization. Sooner or later, the gap between expectations and opportunities will lead to a conflict the consequence of which is the resignation, replacement or dismissal from work.

Group conflicts are also related to the personality of the members of the organization and may be expressed within the group, among its members. These are intra-group conflicts. They occur when group members act contrary to the interests of the group, that is, when they do not respect the rules, standards and norms of the behaviour and work of the group.

Conflicts between various formal and informal groups in the organization are referred to as *inter-group conflicts*. The participants in this type of conflict are groups, organizational units, and departments of the company. This conflict can be caused by failures in the organization, but also by the inability to meet the needs and perform the roles of certain groups in the organization⁶.

Conflicts can be divided into *cognitive* and *affective* ones. A *cognitive conflict* is a form of disagreement among group or team members on a particular prob-

⁶ D. Nelson, J. Campbell, *Organizational Behavior – foundations, realities and challenges. Conflict at work*, Fourth Edition, Thomson, South-Western, USA, 2003.

lem, for the solution of which they have different opinions, attitudes and ideas. It is a form of constructive behaviour that results in a larger group or team cohesiveness, greater job commitment, and higher quality decisions. *An affective conflict* is a form of destructive behaviour, which results in poor decision making, less commitment, less cohesiveness and poor performance. In contrast to the cognitive conflict that is linked to the problem, the affective conflict is related to personality, personal intolerance, envy and hatred. Its effects are extremely negative one, often dramatic for the individuals, leading to high-intensity stress, anxiety and depression. This form of conflict is very unhealthy and undesirable in the organization, as it leads to loss of reputation of the organization.

Conflicts can be observed and classified as *functional* and *dysfunctional*. The main criterion of this classification of conflicts is their effect on the organization. *Functional conflicts* are related to the concept and functioning of the very organization and can be said to increase the degree of functionality and efficiency of the organization. Some authors consider functional conflict to be a 'creative tension' without which the organization would be doomed to stagnation and decline. *Dysfunctional conflicts* are any confrontation between individuals and groups that harm the organization or hinder the achievement of organizational goals. They are the result of abusive behaviour, and a factor of instability and disorganization. Significantly, the nature of the conflict can be changed during the conflict. Thus, a functional conflict can be transformed into a dysfunctional one if the behaviour of the participants in the conflict changes and they start insisting on their interests only, taking an aggressive stand toward the other side⁷.

In addition to the above classification of conflicts can be seen as:

- *conflicts of interests,*
- *conflicts of values,*
- *conflicts of interests and values.*

Conflicts of interests arise in the struggle for funds and resources in the company that are not sufficiently to fully satisfy the desires of individuals. The opposing parties in fact have very similar interests, values and desires.

Conflicts of values are based on differences in values, aspirations and evaluation of employees, which essentially divide the opposing parties.

Conflicts of interests and values arise when the conflicts and struggles of interests escalate into conflicts of values. This expansion of the conflict is the

⁷ M. Petković, B. Bogičević, *Organizacioni konflikti. Organizacija*, Čugura print, Beograd, 2005, pp. 354-356.

result of the need of employees to begin to look at the opposing side, with which they fight over the interests, attitudes and values, as an enemy⁸.

5. Conflict Phases and Consequences

The conflict process in the organization has the following phases:

- 1) *phase of creating the conflict conditions or the phase of the latent conflict*
- 2) *the perception phase and experience of conflict,*
- 3) *the behaviour and intentions creation phase or open conflict phase*
- 4) the result of the conflict phase or the post-conflict phase

During the first phase of the conflict development the creation of favourable conditions for the formation of the first causes of the conflict takes place. The creation of the causes of conflict, for example, may mean that some resources become scarce, leading to conflicts over their distribution in the organization. The contents of the first phase of the conflict can be a gradual differentiation of organizational units that leads to differences in their perspectives and goals, which is an ideal situation for a conflict. Lack of communication can also lead to conflict at this phase. It is important to note that at this stage only the conditions for the appearance of conflict emerge, but these conditions do not have to mean the actual appearance of conflict.

In the second phase the opposing parties become aware of the existence of the conflict appearance conditions, and then through the process of perception they make its selection and organization, on the basis of which they attach meaning to the conflict and understand its meaning. After the perception process, the participants get emotionally involved in the conflict process itself, which results in the emergence of anxiety, aggression, frustration and tension. During this phase of the conflict the opposing parties personalize the conflict, i.e. they identify the opposing side in the conflict that can be an individual or a group, and develop negative feelings for it. However, there is still no open conflict between the opposing sides.

The third phase is the one in which the conflicting parties decide on the action. In the initial part of this phase, when the intentions of one of conflicting parties are still hidden and no concrete action has taken place, there is a risk of misperception of intentions of the other party. It often happens that one party should take dramatic action against the other in the conflict just because it has misinterpreted the intentions of the other party, assuming that these intentions will be much more dangerous for it than they actually are. In the second part of this phase of the conflict the intentions are turned into behaviour and openly

⁸ M. Jovanović, M. Petković, "Vrste konflikta u organizaciji", *Organizaciono ponašanje – novi koncept vođenja preduzeća*, Megatrend univerzitet, Beograd, 2002, pp. 121-122.

shown. The actions of the conflict participants can be of varying intensity - from minor disagreements to open the fight to the death.

In the last phase or the post-conflict phase when the conflict is overcome in some way, there are certain consequences for interpersonal relationships in the organization. What will the consequences be, largely depends on how the conflict will be overcome. If it is resolved by participation and to the satisfaction of all parties, it is likely to lead to the improvement of human relations in the organization, as well as its climate. But if the conflict is resolved through its suppression or through the victory of one of the conflicting parties, the chances are that the negative effects on the organization emerge in the post-conflict period⁹.

According to contemporary views on conflict, it could be said that the consequences of conflicts can be functional when a conflict improves the performance of the group, or dysfunctional, when the conflict interferes with the performance of the group. The positive, i.e. functional effects of conflicts in the organization appear in situations where low to moderate conflict intensity can improve the performance of the work group.

Functional effects of the conflict are:

- improving the quality of decision-making process because it allows for all opinions to be considered, especially the unusual ones and those of minority when making important decisions;
- stimulating creativity and innovation among members of the group;
- promoting organizational change;
- motivating the conflict participants to achieve a particular result;
- increasing work transparency and intensifying communication;
- preventing group blindness and intensifying group cohesion.

Dysfunctional effects of the conflict are:

- disturbance of normal functioning of the organization;
- reduction of cohesiveness and group productivity;
- communication slowdown;
- diverting attention from organizational to personal goals;
- emphasizing emotions in decision-making;
- causing a number of adverse reactions related to members of organizations such as: high intensity of stress, frustration, depression, anxiety and a series of other negative psychological and physical conditions.

The effect of the conflict on an organization depends primarily on its intensity. Despite the numerous negative consequences of conflicts, there is an opinion that it is useful for the organization to have a certain optimal level of conflict

⁹ S. Robbins, *Proces sukoba. Bitni elementi organizacijskog ponašanja*, Mate, Zagreb, 1992, pp. 176-183.

that would lead to necessary organizational changes. It is also pointed out that the level of conflict in the organization must not be of high intensity, since it results in the state of chaos and disorganization, whereby the changes are completely blocked and no concerted action can be taken¹⁰.

6. Conflict Resolution and Management

Various approaches, tools, methods and means are used for resolving conflicts in practice. Which of them will be used depends on the severity of conflicts, the working environment and the conflicting parties. It is not only the way in which conflicts emerge that is important, but how people treat them, carrying the elements of culture and cultural differences in them. Each type of conflict requires an appropriate approach and method to overcome and resolve it. In this way, the positive and constructive effects of conflicts are encouraged, while the negative or destructive ones are simultaneously removed. Resolving a conflict in the organization depends on its type, nature, scope and intensity. Whether the conflict will be permanently resolved or only postponed depends on the method of its resolution.

In organizational theory, three approaches are applied to resolving conflicts with the different stages. The first way to resolve a conflict situation is that *one party wins over the other* in conflict. In this case, the 'winning' side meets their interests and goals, while those of the conflicting side are suppressed. This method of conflict resolution is based on a 'win-lose' system, since in fact one of the conflicting parties wins, while the other side loses in the conflict.

The second method involves *reducing and calming down* the conflict, and is applied when the opposing parties are ready to accept a solution or compromise acceptable to all parties in the conflict. In this case no party is not considered a winner or defeated, whereby further tensions and escalation of conflict are avoided. However, this method does not represent the most appropriate solution for the achievement of the organizational objectives.

The most effective method of conflict resolution is known as *the method of complete solution*. It refers to readiness to remove and reduce differences and misunderstandings between parties, as well as establishing and developing common goals and interests within the organization¹¹.

A new behavioural approach to conflicts is based on numerous studies, from which the following assumptions are taken into account:

- conflicts are unavoidable;

¹⁰ S. Robbins, T. Judge, *Organizacijsko ponašanje. Konflikt i pregovaranje*, Mate d.o.o., Zagreb, 2009.

¹¹ M. Jovanović, M. Živković, T. Cvetkovski, "Sukobi i konflikti u organizaciji", *Organizaciono ponašanje*, Megatrend univerzitet, Beograd, 2003, pp. 172-174.

- conflicts are conditioned by structural factors;
- conflicts are an integral part of changes;
- a minimum level of conflict is the optimal.

Given the inevitability of conflicts and their functional role in organizations, it is the task of management to effectively manage such processes¹². In situations of apathy in working groups, careful encouraging of a functional conflict can significantly increase creativity. These situations are referred to as programmed conflicts and aim to enhance critical thinking.

In the application of programmed conflicts the best known are the two following techniques:

- a dialectic method (this method encourages the debate on different views with the aim of better problem understanding);
- ‘the Devil’s Advocate’ (a method the task of which is to prevent group thinking, whereby the ‘devil’s advocate’ is a person whose role is that of a critic).

Besides these two most commonly used methods for stimulating conflicts, there are some other possibilities that can be applied, such as: communication, inclusion of new members into the group and the organization restructuring¹³.

Using two dimensions of *cooperation* (the degree to which one party attempts to satisfy the interests of the other) and *selfishness* (the degree to which one party attempts to satisfy their own interests), five orientations of behaviour are identified in managing interpersonal conflicts:

Competition – a selfish and uncooperative behaviour, when one party seeks to achieve certain goals, regardless of how this will affect the other side. This fight can be represented as a ‘victory – defeat’ situation.

Collaboration – a selfish and cooperative behaviour, whereby each party in conflict wants to fully meet the interests of all parties and, therefore cooperation appears that is of mutual benefit. The behaviour of the conflicting parties aims at solving problems, whereby many possibilities are considered, and therefore this approach to conflict resolution is referred to as ‘win – win’ situation.

Avoidance – a selfless and non-cooperative behaviour, when there is a lack of interest or desire to avoid open display of dissent. Avoidance means that the conflicting parties accept physical separation, and if this is not possible, the conflicting parties can keep their differences.

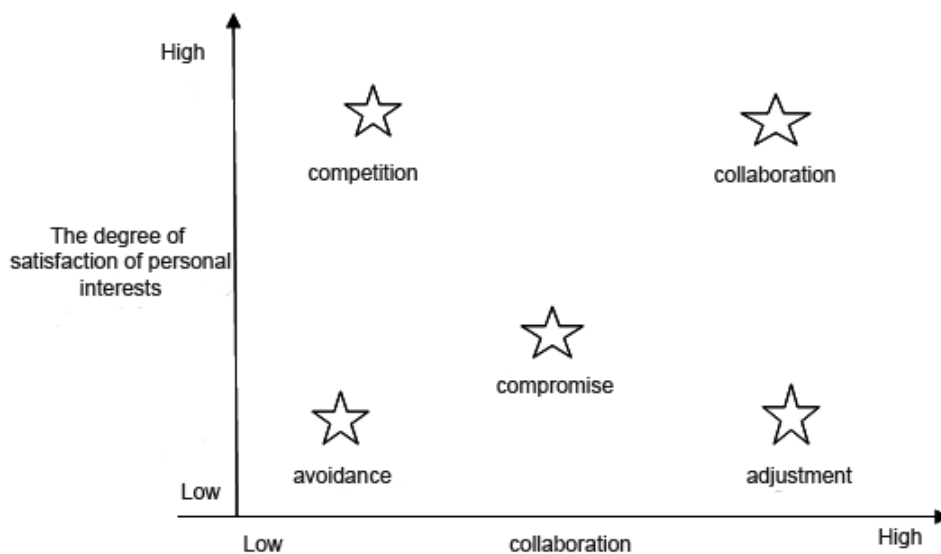
¹² R. Vecchio, *Organizational Behavior, Core Concepts*, Fourth Edition, The Dryden Press, 2004.

¹³ S. Mc Shane, M. Von Glinow, *Organizational Behavior. Organizational Conflict and Negotiation*, McGraw-Hill Irwin, 2002.

Adjustment – a selfless and cooperative behaviour when conflicting parties try to calm down their opponents, and are willing to put their opponents' interests above their own.

Compromise – a middle ground, whereby both sides in the conflict have to give up something in order to achieve a compromise. In these situations there are no clear winners or losers¹⁴.

Graph 1: *Conflict management strategies*



Source: M. Jovanović, M. Živković, T. Cvetkovski: 'Upravljenje sukobima i konfliktima', *Organizaciono ponašanje*, Megatrend univerzitet, Beograd, 2003, p. 183.

7. A Methodological and Hypothetical Framework of Research

The research conducted in Zaječar, during September and October 2011 included a sample of 100 respondents employed in the Zaječar branch of Commercial Bank, the Cultural Centre of Zaječar, The Timocka Television and Radio, The Timok Youth Centre and the 'Hidromreža' Company from Zaječar. As a basic research instrument the anonymous questionnaire: 'What is your strategy

¹⁴ V. Zimanji, G. Šušnjar, *Organizaciono ponašanje. Pomoć, saradnja i konflikti u organizacijama*, Ekonomski fakultet, Subotica, 2005.

for managing conflict¹⁵’ was used. The questionnaire contained 15 questions to determine the primary strategy in managing interpersonal conflict, as well as the questions relating to the general information of the respondents (gender, type of education, age, and years of work experience).

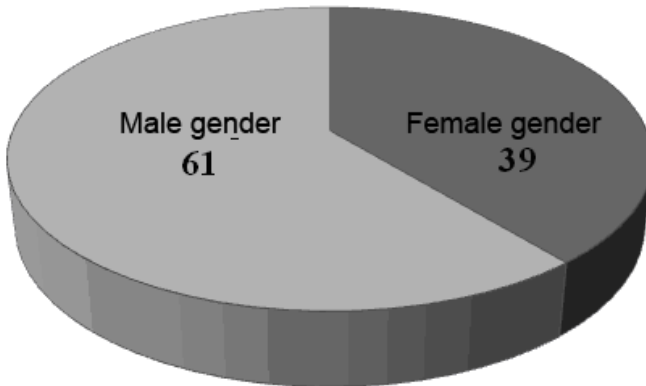
The aim of this research was to determine the primary strategy in managing and resolving conflicts among employees, that is, to determine whether the most commonly used tactic of conflict management was the tactic of conflict cooperation, adaptation, competition, avoidance or compromise.

The survey started from the basic assumption that in the resolution and conflict management the priority is given to the strategies of cooperation, adaptation and avoidance, given the collectivist and feminine values of our national culture which emphasizes collective responsibility and good human relations.

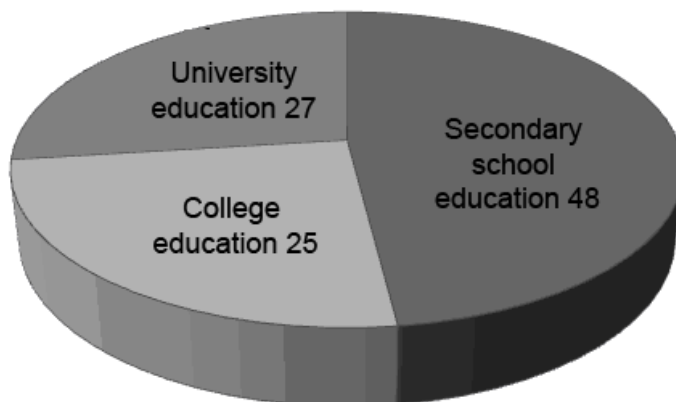
8. The Research Results

The sample included 39 female and 61 male subjects, 48 of whom were with secondary education, 25 with college education, while 27 respondents possessed a university degree. The average age of female respondents was 38 years, and of male respondents it was 39.84 years. The average length of work experience for female subjects was 15.27 years, and for males 17.43 years.

Graph 2: *Distribution of respondents according to gender*



¹⁵ D. Nelson, J. Campbell, “What is your Conflict-Handling Style”, *Organizational Behavior – foundations, realities and challenges*, Fourth Edition, Thomson, South-Western, USA, 2003, p. 449.

Graph 3: *Distribution of respondents according to degree of education***Table 2:** *Exploration of data based on age and respondents' years of work experience*

	The number of respondents	Average value	Std. dev.	Minimum	Maximum
age	100	38.85	10,436	21	62
Years of work experience	100	16.26	10,378	1	40

Table 3: *Exploration of data based on age and respondents' years of work experience in relation to gender*

	Gender			
	Male		Female	
	average	Std. dev.	average	Std. dev.
Age	39.84	10.913	38.00	9.957
Years of work experience	17.43	10.818	15.27	9.901

Table 4: The responses to the question: ‘What is your strategy for managing conflict?’, expressed in percentage

		The respondents’ answers				
		Rarely 1	Sometimes 2	Occasionally 3	Often 4	Always 5
1.	I discuss with colleagues the correctness of their views.	2%	4%	21%	26%	47%
2.	I negotiate with colleagues to achieve a compromise.	3%	3%	27%	34%	33%
3.	I try to meet my colleagues’ expectations.	1%	13%	16%	41%	29%
4.	I resolve the current issues in a mutually acceptable manner.	2%	1%	17%	33%	47%
5.	I am determined in realization of my views.	7%	18%	43%	26%	6%
6.	I try to keep a conflict with colleagues to myself yourself and avoid its disclosure in public.	0%	9%	11%	46%	34%
7.	I try to solve the problem on my own.	1%	6%	24%	46%	23%
8.	I rely on the ‘give-and-take’ principle with the aim of compromising.	15%	22%	26%	28%	9%
9.	I exchange accurate information with colleagues with the aim of joint problem resolution.	0%	4%	16%	40%	40%
10.	I avoid open discussion with colleagues on my differences in relation to others.	16%	19%	41%	17%	7%
11.	I adapt to my colleagues’ wishes.	0%	6%	24%	36%	36%
12.	I put forward the facts openly with the aim of more efficient problem resolution.	0%	3%	14%	39%	44%
13.	I propose a middle solution with the aim of moving from a standstill.	0%	3%	23%	46%	28%
14.	I accept my colleagues’ suggestions.	0%	10%	16%	38%	36%
15.	I try to keep disagreements with colleagues for myself in order to maintain good collegial relations.	10%	23%	20%	26%	21%

After appropriate scoring of the received responses, we obtained the following results.

Table 5: *The total number of points obtained in questions relating to the strategy of cooperation*

Collaboration	
Questions	Points
4.	422
9.	416
12.	424
Total	1262

Table 6: *The total number of points obtained in questions relating to the strategy of adjustment*

Adjustment	
Questions	Points
3.	384
11.	408
14.	400
Total	1192

Table 7: *The total number of points obtained in questions relating to the strategy of competition*

Competition	
Questions	Points
1.	412
5.	306
7.	384
Total	1102

Table 8: *The total number of points obtained in questions relating to the strategy of compromise*

Compromise	
Questions	Points
2.	391
8.	294
13.	399
Total	1084

Table 9: *The total number of points obtained in questions relating to the strategy of avoidance*

Avoidance	
Questions	Points
6.	405
10.	280
15.	325
Total	1010

The order of interpersonal conflict management strategies, ranging from the strategy with most points to the strategy with least points is the following:

- 1) Cooperation (collaboration)
- 2) Adjustment
- 3) Competition
- 4) Compromise
- 5) Avoidance

This leads us to conclude that with the respondents in our research collaboration is a primary strategy in managing interpersonal conflict.

9. Conclusion

The research and studies of the employees' behaviour of in organizations, conflict is one of the main areas of interest, with many authors emphasizing its great influence on group behaviour. There is no black and white conflict classification, and thus no conflict can a priori be determined as functional or dysfunctional. The only criterion for distinguishing these two types of conflict is the result of the group. Although conflict can have a negative impact on the organization, by hindering communication and coordination, it often yields positive results such as: bringing problems to light, understanding the attitude of the opposing party, considering new ideas, better decisions and greater loyalty to the organization. Contemporary understanding of conflicts represents a belief that conflict is not only a positive force of one group, but it is also absolutely necessary for the achievement of group efficiency. It is necessary to maintain a minimum level of conflict, which is enough to make a group vital, self-critical and creative.

Since we are group-oriented beings, we have to learn to live with conflicts if we want the cooperation with other people to be productive. It can be argued that for the effectiveness of any organization no skill is as important as a constructive management and resolution of conflicts. Given the inevitability of con-

licts and their functional role in the organization, it is the priority of management to manage these processes efficiently, rather than to eliminate them, since the absence of conflict in the organization leads to apathy, stagnation and the inability to adapt to organizational changes.

The results of the research have proved the initial hypothesis and shown that collaboration and adjustment are the dominant strategies in managing interpersonal conflict in the group of respondents. Cooperation, i.e. collaboration is a 'win – win' approach to conflict resolution, where each conflicting party wants to fully meet the interests of all parties, while adjustment appears when the conflicting parties try to calm down their opponents are willing to put their interests above one's own. These results were expected given the collectivist and feminine values of our national culture. In collectivist cultures there is a strong social structure, in which social relations are very intensive, whereby individuals are expected to take care not only of themselves, but also of members of the collective they belong to. In cultures in which the so-called women's values are dominant and where our national culture belongs as well, good interpersonal relationships, balance and harmony with the social environment are the values respected in the first place.

The survey showed that more than 80% of respondents always or often resolve the current issues in a mutually acceptable way, sharing accurate information with colleagues to solve common problems. Also, most respondents try to put forward the facts openly with the aim of efficient problem solving. All this contributed to the collaboration, i.e. cooperation is a primary strategy with the respondents for managing conflict in the group.

It is interesting to note that a low level of advanced techniques knowledge of conflict resolution in respondents such as the method of 'give and take', in order to achieve a compromise, which is otherwise successfully used in organizations around the world. It may be noted that respondents are willing to negotiate with colleagues to a smaller extent to achieve a compromise and propose a middle solution in order to move from a standstill.

The least present strategy for managing conflicts is the avoidance strategy, which is otherwise often represented in collectivist cultures with dominant female values. With this strategy of conflict management there is a lack of interest or desire to avoid open display of disagreement. According to survey results, it can be concluded that respondents do not avoid open discussion with colleagues on their differences in relation to others, whereby their disagreement with colleagues they do not keep for themselves in order to maintain good collegial relations.

A recommendation to companies' management that participated in the study is the necessity of specific employees training in order to develop strategies and techniques for conflict management.

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PETAR BABIĆ, M.A.*
“Privredni savetnik“ Ltd., Belgrade

OLD VS. NEW BRANDS IN TRANSITIONAL ECONOMIES: A STUDY OF CONSUMERS IN SERBIA

Summary

This article analyses values, equity and heritage of traditional (“old-socialistic”) brands in a transitional regional markets of South East Europe, namely in Serbia and the republics of former Yugoslavia. Presented data provides an answer how important, the brand equity values of traditional brands really are, and how can they become a valuable asset for utilization due to their uniqueness, history merit and special “emotional” relations with customers.

According to my findings, objective measurement of “emotional response” is of a critical importance for proper evaluation of brand equity; estimated influence of emotionally nostalgic stimuli (actual evaluation of traits/actual purchasing decision factor) present actual range (useful value) of these emotions over consumer purchasing behavior; “nostalgic” feelings could prove “stronger” than impact of ethnocentrism and brand patriotism (positive feelings-affection stronger than negative-hatred-refusal); the basics of trust toward “old-socialistic” traditional brands are not being found in really - greater consumer’s convictions toward superior values of these brands but in their emotional background. Depicted elements of traditional brands “hidden equity” indicate possible ways for their most effective usage. Recommendations given here could be also applied in other transitional post-communist countries that went through similar political-historical processes (such as USSR and Czechoslovakia for example), and other transitional countries in general.

Key words: *traditional brands, consumers, emotional response, transitional economies, Yugoslavia, heritage, nostalgic stimuli, brand equity*

JEL classification: M31, P36

* E-mail: privrednis@privsav.rs

1. Introduction

The idea of investigation of one of the least researched domains in contemporary studies of brands - phenomenon of traditional ("old-socialistic") brands also arouses from interesting and controversial effects that these brands still evokes in a "hearts and minds" in transitional region of former Yugoslavia. Starting from the fact that the depth of a certain symbol in the trace of the memory is closely related to amount of feelings that evokes in people or, as above mentioned "heart response", we can conclude that, at Serbian and at overall market of former Yugoslavia (including Croatia, Slovenia, Bosnia and Herzegovina, FYR Macedonia and Montenegro), that trace in memory still hold and appreciate so called "old brands" that had been created during the 50 years of "brotherhood and unity". Phenomenon's of sustained brand awareness and, most interestingly, brand loyalty, which has been created in that period, survived even in time of civil war in former Yugoslavia (1991-1995/1999).

So, what it is the primary reason for such a strong embodiment of these brands in a mind and hearts of these people, and what conclusion could we generate in order to understand the "higher" meaning of the phenomenon of a brand? Is it just about the brands itself, their properties or quality, or is it something else? The answer to these questions, in the case of former Yugoslavia, could be found in a collective memory of their nations regarding one "happier" period of time which leftovers are scarcely and symbolically represented by Yugoslav "traditional brands".

Thus, the main purpose of this article is to provide the critical factors that comprise the overall equity of these brands, their merit of uniqueness and heritage behind them. Properly presented research findings could not only contribute in understanding of phenomenon of "traditional" brands but in overall understanding of true nature of brands. One of the most important questions that arise from this issue is to explain how is it possible, for these "traditional" brands, to survive and to retain their popularity among consumers in different republics, in spite of recent historical events and political turmoil. Objective evaluation of their specific traits could contribute, not just theoretically, but also in practical application of presented findings. For example, recommendations given here could be also applied in other transitional post-communist countries that went through similar political-historical processes (such as USSR and Czechoslovakia), and in other transitional countries, as well.

2. Data and methods

Methodology and data collection method required and applied here were based on the relevant data collected through qualitative, exploratory process. The author examined four focus groups made of five participants chosen by per-

sonal network and analyzed by maximum variation sampling method. Additionally, results of focus groups analysis were presented to the three experts (personal interviews, critical case-sampling method) in order to analyze their opinion regarding acquired results.

The most appropriate data collection method of achieving targeted research objectives in this case is group interview. Proposed data collection method envisaged interviews of two sample groups: consumers and experts. First sample group - consumers, were interviewed through four focus groups each consisting of five participants (total of 20) and analyzed by method of maximum variation sampling. Second sample group - experts were interviewed through the personal interviews of three participant and analyzed by method of sampling technique called critical case. Research questions stated in group interviews through interview questions (total of 20) were presented to interviewees in first sample group. Concerning questions for second sample group (experts), the results acquired from interviews in first sample group (consumer-focus groups) were presented to experts from second sample group to comment on in an in-depth personal interviews and interactive way with author. The participants were chosen among the consumers from Serbia and from the Republics of former Yugoslavia (approximately consistent with population ratio in former Yugoslavia: Serbs - 11,5 million (60% participants), Croats - 3,5 million (20% participants), Bosnians - 2,5 million (15% participants) and Slovenes - 1,5 million (5% participant), (other nationalities, Albanians, citizens of FYR Macedonia and others - 4,5 million, were excluded due to unavailability of these participants).

First sample group was examined and interviewed on a base of following rules: first focus group - age between 18 and 25, second focus group - age between 26 and 40, third focus group - age between 41 and 55 and fourth focus group - age between 56 and 65. Further on, they were analyzed by gender (ratio Male: Female, 9:11 or 40:60), educational (ratio High school: University degree, 8:12 or 40:60) and geographical (nationality) groups (Serbia, Croatia, Bosnia and Slovenia, ratio 12:4:3:1 or 60:40:15:5). Second sample group, experts, consisted of three participants' - marketing and business consulting experts with age ranging 32 - 59.

3. Theoretical approaches

Even today, almost two decades since the collapse of communism, academic research and information regarding consumer behavior in a transitional region of SEE is still very scarce. Lacking experience in operating in the competitive, open market conditions, local industries have been strongly impacted by foreign entrants, leading to unemployment and a decrease in discretionary income for some people, and yet to new entrepreneurial opportunities for others. As a

result, many SEE countries are experiencing not only growing economic stratification of the societies, but also altered hierarchies of consumer values, standards and needs.¹ So, what about branding solutions in such situation? Do we have something from “the old arsenal”, that we could use in building effective branding strategy in SEE transitional markets, or not? Practitioners acknowledged that effective advertising, which helps build powerful, lasting brand relationships, is a balance of “head and heart”. Little investment in research and theory development, however, has been dedicated to measuring the heart response². While research on brand equity has gone a long way, research that focus on branding in the transitional markets started much latter³.

Therefore, connected need for a “more investment in research and theory development of measuring the heart response” and “focused research on transitional branding”, has produced an idea of investigation of one of the least researched domains in contemporary studies of brands - phenomenon of traditional (“old-socialistic”) brands in former Yugoslavia. Reasons for belief in importance of a such study arouses from interesting and controversial effects that these brands still evokes in a “hearts and minds” in this transitional region. In addition, importance of brand research in the transitional markets of former Yugoslavia, lays in a fact that such type of research and research findings are very scarcely available to this point. Important part of brand recognition process is a brand awareness. Brand awareness indicates the strength of the brand node or trace in memory, as reflected by consumers’ ability to identify the brand under different conditions⁴. So, what it is the primary reason for such a strong embodiment of these brands in a mind and hearts of these people, and what conclusion could we generate in order to understand the “higher” meaning of the phenomenon of a brand?

Since the process of brand recognition and recall are important for consumer’s choice of brands⁵ and the level of brand influence is directly connected to the attached brand image, the brand image is commonly viewed as consumers’ more or less coherent set of associations with regard to a brand⁶. The coherent set of associations to a certain brand defines consumer relationship with the brand

¹ W. Nasierowski, *Emerging patterns of reformations in Central Europe: the Czech Republic, Hungary and Poland*, *Journal of East-West Business*, Philadelphia, 1996.

² T. Plummer, *How Personality Makes a Difference*, *Journal of Advertising Research* 24. London, 1985.

³ R. Batra, *Executive insight: Marketing issues and challenges in transitional economies*, *Journal of International Marketing*, London 1997.

⁴ L. Percy, J. Rossiter, *A Model of Brand Awareness and Brand attitude Advertising Strategies*, Psychology & Marketing, London, 1992.

⁵ W. Hoyer, S. Brown, *Effects of Brand Awareness on Choice for a Common, Repeat-Purchase Product*, *Journal of Consumer Research*, Chicago, 1990.

⁶ D. Aaker, *Building Strong Brands*, The Free Press, New York, 1996.

and the attitude toward the brand is a function of (a) the strength of beliefs about a brand, and (b) the evaluation aspects of these beliefs⁷. The brands are not just differentiating marks that help consumers to choose one brand against another, but are also—and indeed more significantly cultural signs that supply people with individual identities⁸. Furthermore, brands express community identity⁹, convey self-identity¹⁰ and express family identity¹¹. Another important aspect of brand evaluation is a possibility for identification.

Starting from an assumption that the person perception is influenced by one's attitude toward the category or schema to which the target person belongs¹², perception of tradition and belongings to the culture (embedded in traditional brands) could create a bondage that surpasses the affective attitude toward foreign brands. When we argue about the negative perception of these traditional brands, we can determine that the main danger evolves from a previously stated common belief, confirmed in many research studies of transitional markets that “the domestic brands are of poor quality and generally poorly designed”.

If it is true that consumers imbue brands with human personality traits¹³, in the case of former Yugoslavia, this claim could be expanded in “Consumers imbue brands with the traits of culture and history of one country”. Thus, consumers can form beliefs about non-featured attributes through various inferential processes¹⁴, and create emotionally attached form of relationship toward particular traditional brands. These elements, besides the specifically qualitative properties typical for that product, represent the core of the context behind the brand loyalty potentially attached to one “traditional” brand.

Attitude toward particular brand is also affected by level of affective reaction. Thus, the origins of affective reactions may differ for novel and familiar

⁷ M. Fishbein and I. Ajzen, *Belief, Attitude, Intention, and Behavior*, Addison-Wesley, Reading, MA, 1975.

⁸ R. Elliott and K. Wattanasuwan, *Brands as symbolic resources for the construction of identity*, International Journal of Advertising, Oxfordshire, 1998.

⁹ A. Muniz and T. O'Guinn, *Brand community*, Journal of Consumer Research 27, Chicago, 2001.

¹⁰ S. Fournier and J. Yao, *Reviving brand loyalty: a re-conceptualization within the framework of consumer-brand relationship*, International Journal of Research in Marketing, 14, 5, London, 1997, pp. 451-472.

¹¹ B. Olsen: *Brand loyalty and lineage: exploring new dimensions for research*, Advances in Consumer Research 20, New York, 1993, pp. 575-579.

¹² T. Fiske, *Schema-triggered affect: Applications to social perception*, In M. S. Clark & S. T. Fiske (Eds.), *Affect and cognition: The 17th annual Carnegie symposium on cognition* (pp. 171-190), Hillsdale, NJ, 1982.

¹³ J. Aaker: *Dimensions of Brand Personality*”, Journal of Marketing Research 34 (August), 347-356, Boston, 1997.

¹⁴ J. Alba and W. Hutchinson: *Dimensions of Consumer Expertise*”, Journal of Consumer Research 13 (March), Chicago, 1987, pp. 411-454.

brands¹⁵. Moreover, those exposed to an advertisement for a familiar brand may experience a certain affective response as a result of brand-related thinking¹⁶. Such brands include additional social “attachment” that could form a particular form of brand community – consumers congregate around brands towards which they exhibit a socially motivated attachment, in what has been coined “brand communities”¹⁷. When brands are associated with specific favorable user stereotypes, consumers may obtain a favorable social classification by using these brands. Thus, we can conclude that vital elements that are directly responsible and important in a process of creation of brand loyalty are: understanding of consumer’s value systems and trust. Since much of branding involves creating and sustaining a desired image or personality, which has been linked directly to consumer choice¹⁸, the main question is, how can we properly sustain already created image and personality along with its positive traits? Is it wise to change brand identity, and if so, in what measure? Identity that was formatted in a course of past time should be carefully nourished and sustained in order to win long-term victory for acquiring and/or regaining the brand loyalty.

4. “New” vs. “old” brands

Being a transitional country, Serbia experiences new global, regional, even local brands claiming large parts of the market against “old”-traditional brands operating in the country since the communist regime. Some of them survived and still holds good market position comparing to similar foreign brands. For example, “Soko Štark”, old and traditional Serbian brand of snacks and chocolates, is trying to survive in a competitive market against giants like “Milka” and successfully manages in such an aim (mostly due to their famous products: “Smoki” flips and “Najlepše želje” chocolate); “Knjaz Miloš” sparkling and mineral water brand is still number one at domestic market; “Plazma keks” top level biscuit from Bambi, Požarevac; “Jaffa cakes” from Crvenka; “Eurokrem” chocolate cream from “Takovo”, Gornji Milanovac. Similar examples from other ex-Yugoslavia republics (Croatia) proves that “old” brands values still survives: “Vegeta” (food complement), “Podravka” soups; “Eva” tinned fish - (well known and famous brands originally from Podravka, Croatia, which are very popular in

¹⁵ J. Cohen, *Attitude, Affect, and Consumer Behavior in Affect and Social Behavior*, Bert S. Moore and Alice M. Isen, eds., Cambridge: Cambridge University Press, Cambridge, 1990, pp. 152–206.

¹⁶ P. Homer, *Relationships among ad-induced affect, beliefs, and attitudes*, *Journal of Advertising*, vol. 35, no. 1 (Spring 2006), Memphis, 2006, pp. 35–51.

¹⁷ S. Brown, V. Kozinets and J. Sherry, “Teaching old brands new tricks: retro branding and the revival of brand meaning”, *Journal of Marketing*, 67, 3, Chicago, 2003, pp. 19–33.

¹⁸ J. Aaker, *ibidem*.

Serbia and other republics of former Yugoslavia); “Kiki” candies and “Bajadera” bonbonnières from “Kraš” Zagreb; “Cedevita” vitamin beverage and “Zdenka” melted cheese. Slovenian famous brands like “Fructal” fruit juice, “Mura” clothing brand, “Gorenje” home appliances, “Elan” ski equipment, “Mercator” retail brand, “Cocta” non-alcoholic beverage; “Radenska tri srca” (“Radenska three hearts” - mineral water), are more than recognizable and successful.

Depicting and analyzing the main factors that leads to preservation and successful “life” of these brands should reveal exactly how much is their uniqueness and history merit important for their success. Proper examination of how consumers perceive these brands in comparison to “new”- global brands should reveal the new ways for effective utilization of “traditional” brands values.

One of the most important questions that arise from this issue is to explain how is it possible, for these “traditional” brands, to survive and to retain their popularity among consumers in different republics, in spite of recent historical events and political turmoil.

Thus, it is important to determine how consumers perceive and compare traditional-domestic (“old-socialistic”) brands to new Serbian brands and foreign (“new-global”) brands; if traditional-domestic (“old-socialistic”) brands should keep some of their characteristics and which to abandon, should we just copy the foreign (“new-global”) brands or is there still merit in their uniqueness and history, are there any special (historical) relations with customers, and with what type of customers; the specific level of ethnocentrism and brand patriotism in Serbia and republics of former Yugoslavia; evaluate the effects of brand heritage and suggest ways by which traditional (“old-socialistic”) brands should evolve in order to survive.

“New-global” brands, in context of this study, are all foreign imported brands and products in period from 1945 until now (2010) and beyond, consumed on the regional market of former Yugoslavia. By evaluating their historical impact and perceived consumer attitude toward these brands, we can conclude that these foreign brands had been perceived in a form of a “scarce luxury”. The term “foreign brands” comprised items such as: Levi’s jeans, nylon stockings, French brandy, Whiskey, Rock ‘n’ Roll records etc. In a first 20 years, until mid 60’s, the availability of these items was indeed very limited and only a narrow number of people in Yugoslavia could afford them. During late 60’s and afterward, the immigration policy became liberal, and these items and brands were more available to broad masses but their general popularity was not diminished. Unlike other ex-communist countries of eastern block, Tito’s Yugoslav nation has enjoyed relative freedom that included free immigration policy, frequent shopping in Trieste (Italy) and consummation of foreign “Western” brands. It resulted in high awareness of foreign brands, “Western” mass-popular culture and other “undesirable influence of rotten capitalism”.

4.1. Economic and political factors of Serbia and former Yugoslavia

For the purpose and oriented toward the objectives of this work, we will examine the political, cultural and economical characteristics of Serbia and former Yugoslavia and their influence on regional national markets and brands of presently independent states that has been created upon its dissolution.

Republic of Serbia is a country in Southeastern Europe bordered by Hungary on the north, Croatia and Bosnia and Herzegovina on the west, Albania, FYR of Macedonia and Montenegro on the south, and Romania and Bulgaria on the east. With its capital Belgrade, Serbia is positioned in a central part of the Balkan Peninsula.

Serbia has an economy based on services, agriculture and industry. Before, and at the beginning of the process of economic transition (1970 – 1990), its position was favorable, but it was deeply impacted by economic sanctions (1992-1995/2001). Above all, lost market of former Yugoslavia has damaged already ill Serbian economy. In addition to that, the damage to industry and vital infrastructure during the NATO air strikes in 1999 was considerable. After the political changes in 2000, Serbia experienced faster economic growth but not as expected. Main economic problems included (and still include) high unemployment rate, high export/import trade deficit, considerable national debt and insufficient amount of economic and legislative reforms. Serbian currency, stable dinar and a restructured financial sector demonstrate the relative success of stabilization policies.

Former Yugoslavia (or formally Socialist Federal Republic of Yugoslavia, November 29th 1943 – June 25th 1991) was a second of a total of three political entities with such name that existed in the 20th century in Balkan area. Successor of the Kingdom of Yugoslavia (December 1st 1918 – April 17th, 1941) and predecessor of Federal Republic of Yugoslavia (April 27th, 1992 – February 4th, 2003), was a communist state that comprised the area of the presently independent states of Serbia, Croatia, Slovenia, Bosnia and Herzegovina, Republic of Macedonia and Montenegro. With the total population of 23,724,919 (July 1989 est.) and area of 255,804 km², Yugoslavia was a regional power.

Socialist Federal Republic of Yugoslavia was constituted during the Second World War and under the leadership of its lifelong president Josip Broz Tito. Second Yugoslavia (so called “Tito’s Yugoslavia”) used to be described as “a small country with big problems: seven neighboring countries, six republics, five nationalities, four languages, three religions, two alphabets and one political party”. The country that has been severely affected by the destruction of the Second World War and hard nationalist sentiment became united in so-called Tito’s “socialist paradise of Brotherhood and Unity”. He attempted (Tito), at the very least, to forge a united nation from a host of competing, often antagonistic ethnic groups, each with its own aspirations in terms of economic and cultural

development, religion, language and political awareness¹⁹. Common goal, besides political reasons such as establishing Yugoslav “way to Communism” was also forming a common entity “that could protect all Yugoslav nations”. Communist dictatorship temporarily “iced” nationalistic tendencies by brutal force but these issues remained unsolved. Unlike other Eastern and Central European communist countries, Yugoslavia, under the leadership of President Josip Broz Tito was independent of the USSR, and was a member of neither the Warsaw pact nor NATO. Instead, Yugoslavia (in 1961), became a founding member of the Non-Aligned Movement. New federal constitution (1974) ratified more autonomy to the individual republics and created a fertile ground for a future secessionist problem (each republic officially had the option to declare independence from the federation). President Josip Broz Tito died in 1980, and it was not long before serious tensions between the Republics started to grow. Slovenia, Croatia and Republics of Macedonia decided to become independent states in 1991 (Bosnia and Herzegovina in 1992), which marked the end of the second Yugoslavia. Following civil war erupted immediately between various nations: Serbs and Croats (in Croatia) and Serbs, Croats and Muslims in Bosnia and Herzegovina. The reasons: question of status for minority nations in secessionist Republics and unsolved “payback” from the past. The civil war lasted from 1991 to 1995.

In a nearly 50 years of living in that country, these nations has shared, among other, the typical Yugoslav brands that has been developed and created in that period. Such brands had engulfed the main cultural and other important environmental properties attached to this country. As such, these brands, beside their qualitative properties, also represent a symbolic “piece” of that time and evoke certain emotions. Emotional sentiment toward these brands is especially strong in countries (and nations) that has considered Yugoslavia the most as its own common country (Serbia, Montenegro and Bosnia and Herzegovina). For the people in these countries, (as well and for much of other people from different Republics of former Yugoslavia), these brands represent emotional bondage and ticket to “one happier time”.

The economy of second Yugoslavia, was considerably different from economies of the Soviet Union and other Eastern European countries²⁰. At the very start, the level of destruction in Second World War left Yugoslavia’s infrastructure devastated. Already very rural, it had the little industry capacity to start with. Helped by US credits, the country’s economy prospered formidably in the next 30 years. Companies were socially owned and managed with workers’ self-management (unlike Soviet system – companies owned by the state). Yugoslavia was one of the first Communist countries to introduce elements of market social-

¹⁹ D. Andelman, *Yugoslavia: The Delicate Balance*, The New York Times, New York, 2001.

²⁰ M. Milovanovic, *Property Rights, Liberty, and Corruption in Serbia*, The Independent Review, v. XII, n. 2, London, 2007, pp. 213-234.

ism²¹. Unemployment rate was low (due to free emigration), the education level of the work force was high and domestic companies exported to both Western and Eastern markets. The economy was reorganized (during 1970's) according to the theory of associated labor, so called system of "workers self-management" (the right to decision making and a share in profits of socially owned company is based on the investment of labor - the workers are the owners of company, so they are responsible for its future and profit). The reason for that reorganization lied in a fact that communist nomenclature has realized that the system of socially owned companies is highly ineffective, so they tried to invent something else in order to stay at power and provide a notion of prosperity. Off course, it was only a short-term solution. In practice, the appointment of managers and strategic policy was subject to political and personal influence peddling. In fact, during the Cold War, the West supplied ample resources to Yugoslav Communists, who channeled them into private consumption, creating a false impression that the system was viable. In addition, "Yugoslavs were free to travel abroad, which created a force of more than a million migrant workers by the late 1960s. The emigrants sent remittances and thus substantially raised living standards at home. The system supposedly supplied the best possible solution to the imagined trade-off between economic efficiency and social justice. Upon the gradual stop of foreign aid inflow, the Yugoslav economy in 1980's started a prolonged stumble which had worsened since Tito's death and absence of firm control over various nationalistic nomenclatures. The civil wars and loss of market brought further economic problems for all former republics in the 1990s. The currency of the second Yugoslavia was the Yugoslav dinar.

4.2. Brands in Serbia and region

During the 1980's, second Yugoslavia had three major brands: "Elan" skies, Josip Broz Tito and Dubrovnik²². In the meantime, situation has changed: "Days after the name Yugoslavia was dropped by Serbia and Montenegro, the nostalgia industry is in full swing...and to take a walk along the aisles of Serbia's newest and biggest supermarket (Slovenian "Mercator") is to take a stroll down memory lane. There is the "Fructal" fruit juice from Slovenia. The fine Dalmatian hams from Croatia. Macedonia supplies the "Tikveš", bone-dry red wine, Serbia itself the fresh meat and vegetables, while Montenegro declares its presence with shiny fish fresh from the Adriatic..." "Mercator's" - "Friends Forever" is the cheeky slogan for the Slovene chain, a deliberate joke since Serbs and Slovenes were bitter enemies in the wars that erupted in 1991, a conflict prefigured by Slobodan

²¹ M. Milovanovic, *ibidem*.

²² T. Nikolovski, *German Slivowitz and Bulgarian Kajmak*, Politika, October 22nd 2007, Belgrade, 2007.

Milosevic when he decreed a Serbian boycott of Slovene goods”²³. Newly opened Slovenian shopping mall represented an astute exercise in exploiting old brand loyalties to make money; it triggered an intense bout of nostalgia for the old Yugoslavia and bittersweet emotions that are also being stirred by sport, film and pop music²⁴. Concerning chocolate cream “Eurokrem”, just before the end of 2006, leading Croatian media conducted an survey which stated a question: “By what do you remember Yugoslavia?”, and the answer of majority of people was “By “Eurokrem”²⁵.

In order to understand how consumers perceive these types of brands we must define these categories of brands in this context. By Traditional (“old-social-istic”) brands in this context, we assumed the brands that has been conceived and created during the so-called second or “Tito’s Yugoslavia” in period from 1945 - 1991. Discussing the values of average Yugoslav consumer attitude toward the “old-traditional” brands, we must acknowledge that the attitude toward these brands has been changed from initial period of their creation and “active” life. In that period (1945 - 1991), these brands had been regarded as “necessity” in the absence of more qualitative brands and products. Only a few of them had perceived properties evaluated as a “superior one” or “scarce luxury”. On the other hand, foreign brands and products had been perceived exactly like that - a “scarce luxury” comprised items such as Levi’s jeans, nylon stockings, French brandy, Whiskey, Rock ‘n’ Roll records etc. During 70’s and up to late 80’s, the situation and consumer’s perception regarding this issue was pretty much the same, albeit the fact that up to that time some domestic brand achieved the “cult status” among Yugoslav consumers. Domestic brands such as: “Jaffa cakes”; “Eurokrem” chocolate cream, “Vegeta” (food complement), “Podravka” soups; “Eva” tinned fish; “Kiki” candies and “Bajadera” bonbonnières; “Cedevita” vitamin beverage; “Zdenka” melted cheese; “Fructal” fruit juice; “Mura” sweaters; “Gorenje” home appliances; “Elan” ski equipment; “Cocta” non-alcoholic beverage; “Radenska tri srca” (“Radenska three hearts” - mineral water), were very successful and appreciated brands in this period. Consumers in Serbia and at the area of former Yugoslavia regard domestic brands as “inferior” in comparison to the imported well-known global brands. The reason for such attitude lies in a common belief that “everything that comes from the west must be of better quality than domestic”. The fact that domestic brands were generally a good (even in some cases superior quality) had not much influence on such a belief. Exception to the rule is some sort of food products and beverages made out of natural ingredients that managed to withstand the image of superior products and brands in comparison to global brands.

²³ I. Traynor, *Memories of Happier Days*, Guardian, Published: 2/13/2003, London, 2003, p. 13.

²⁴ I. Traynor, *ibidem*.

²⁵ E. Novakovic, *Into the world with brand*, Vecernje novosti, January 7th 2007, Belgrade, 2007.

Depicting the main properties of “old” ex-Yugoslavia popular brands, and their brand values, we can conclude that they reflect following properties: they are relatively unplanned, strong, distinctive, well targeted, tired, positive and alive. In order to achieve full understanding of these brands and decision making process, we are highly dependable upon information on the country of origin. In a present time, after the civil war and political turmoil that wrecked the country, these brands, interestingly enough, not only preserved their former “glory” but also achieved additional dimension of attractiveness through some sort of emotional virtue.

5. Results

Participants stated their favourite ex-Yu brands in a following order (highest frequency - most favourite one - on the top of the list): Plazma (biscuit from Bambi, Požarevac, Serbia), Kraš (products of candy industry from Zagreb, Croatia, generally, their bonbonnières, chocolate cubes - “bajadere”, “Bronhi” bonbons, Kiki bonbons and 505 sa crtom bonbons), Soko Štark (products of candy industry from Belgrade, Serbia, generally), Zdenka (melted cheese - dairy products industry from Belje, Croatia), Elan (ski equipment - sport equipment industry Maribor, Slovenia), Eurokrem (chocolate bar, product of candy industry from “Takovo”, Gornji Milanovac, Serbia), Mura (sweaters and suits - fashion industry from Slovenia), Rašica (sweaters - fashion industry from Slovenia), Gorenje (home appliances - industry from Slovenia), Zastava (products of automobile industry from Kragujevac, Serbia, their models: Yugo and “Kec” - Fiat 101), Smederevac (furnaces from “Milan Blagojevic” factory, Smederevo, Serbia), Varteks (fashion products from Varazdin, Croatia);

Participants stated their opinion regarding important traits of ex-Yu brands in a following order (highest frequency- on the top of the list): Good quality, Poor design, Good design, Durable, Good quality (in the past). Ability to describe important traits of ex-Yu brands also followed above mentioned pattern;

Participants stated their favourite new Serbian brands in a following order (highest frequency - most favourite one - on the top of the list): Voda Voda (mineral water), Grand kafa (coffee), Next (juices), Don cafe (coffee), Beba kids (kids fashion), Radovanović (vines), Soko Štark (products of candy industry from Belgrade, Serbia, generally), Žuta osa (plum brandy), Aqua viva (mineral water), Prolom voda (mineral water), Zlatiborac (hams), Stara Sokolova (plum brandy). These brands were depicted as brands of Good design (visually attractive);

Participants stated their favourite global brands in a following order (highest frequency - most favourite one - on the top of the list): Nokia, Mercedes, Lancome, Toyota, Heineken, Nestle, Zara, Milka, Mitsubishi, Samsung, Sony, Armani, Coca Cola, BMW, Pepsi, Toblerone, Nivea and Volvo. These brands

were depicted as brands of Top quality, excellent and very good quality, Expensive brands, brands with Long tradition and brands of Perfect-modern design;

Such (combined) results showed that consumers from transitional markets of former Yugoslavia prefers group of brands that they evaluate mostly by “emotional-nostalgic” approach: Ex-Yu brands. They know that the Ex-Yu brands, in many cases, presented just a “legends”, a nice story, but nevertheless, they “want” to believe in “this story”, so they give them relative-small advantage in comparison to Foreign (“new-global”) brands. Secondly, affection toward Foreign (“new-global”) brands is their rational statement made in order to “compensate” for previous “irrational” one, for which they are “sub-consciously” aware of. Overall relative unpopularity of New Serbian brands also indicates that the New Serbian brands are largely unavailable in certain markets of former Yugoslavia (namely Croatian and Slovenia) due to political reasons.

Relatively high percentage of indecisive answers indicates that this issue was also the point where patriotic reasons (affection) toward former Yugoslavia and evaluation of real qualities of Foreign (“new-global”) brands collide;

Participants of Focus Groups ABCD, in order to provide their answer concerning their feeling(s), attitude toward possible heritage, uniqueness and historical value(s) of Ex-Yu brands, as well as reasons for such attitude, gave following results: they have largely Positive feeling (warm emotion/acceptance) over Negative feeling (negative attitude/want to forget them) toward Ex-Yu brands, relative majority of them think that Ex-Yu brands are unique. Relatively bigger majority of them do not consider Ex-Yu brands as brands which have historical value.

Such results showed that consumers from transitional markets of former Yugoslavia have positive feelings toward Ex-Yu brands. For them, the Ex-Yu brands present “a ticket” to their youth, careless-cotton times of Yugoslavia socialism and one-better period. Consistently, they showed positive attitude toward their uniqueness, but not to the historical value of these brands.

Combined results indicate that these brands are deeply incorporated into their memory and that the reflection of these brands still emulates old purchasing habits and strong positive feelings toward them.

Participants of Focus Group ABCD, in order to provide their purchasing decision between (available) Ex-Yu brands, New Serbian brands and Foreign (“new-global”) brands, (Simplified question: “In case of similar quality and price, what would you buy, and why would you make such decision?”), presented their attitude in following order:

- 1) Ex-Yu brands or Foreign (“new-global”) brands = Ex-Yu brands;
- 2) New Serbian brands or Foreign (“new-global”) brands = Foreign (“new-global”) brands;
- 3) Ex-Yu brands or New Serbian brands = New Serbian brands

Such results showed clear inconsistency in purchasing behavior of all groups with mixture of “patriotic/ethnocentric” and “rational” reasons, at ratio 2:3. Thus, the specific level of ethnocentrism and brand patriotism, in this case, is at low-medium level.

Asked, do they buy a new Serbian brands and if so, why, majority of them answered that they do buy them, with exclusion of participants from Croatia and Slovenia who stated that “They are unavailable in Croatia/Slovenia“;

Participants of Focus Groups ABCD, in order to provide their answer whether or not ex-Yu brands should retain their specific characteristics (does some of their specific characteristics should be abandoned or changed), as well as reasons for such attitude, gave following results: relative majority of them stated that Ex-Yu brands should retain their specific characteristics (quality), but also most of them stated that Some of their specific characteristics should be abandoned or changed (design and marketing approach).

Elevated attitude (slightly toward copying 55:40), has been provided toward issue of “copying” the global brands. Participant’s attitude was that Ex-Yu brands should evolve (marketing, design and packaging) and that the changes of brands at Serbian market are a positive process (creates better competition).

Such results showed that consumers from transitional markets of former Yugoslavia are in favor of keeping some important quality traits of ex-Yu brands, but also, that, they are in favor of visual and marketing changes. They are slightly in favor of copying the global brands, but also want to keep visual identity of ex-Yu brands recognizable. They consider the process of evolving affirmatively (technologically, in design and advertising style), as well as changes of brands at the market (beneficial).

Combined results indicate high-moderate level of openness toward changes in all four groups.

Concerning geographical (national-regional) division of combined results (Focus Groups ABCD), we can observe following patterns:

- 1) Participants from Bosnia prefer Serbian, Slovenian and Croatian products (in that order), they buy new Serbian brands (if available), (results for global brands are same for all four region), medium-high “patriotic/ethnocentric” tendency;
- 2) Participants from Croatia prefer Croatian, Slovenian and Serbian products (in that order), they do not buy new Serbian brands (unavailability of new Serbian brands in Croatia), (results for global brands are same for all four region), medium-high “patriotic/ethnocentric” tendency;
- 3) Participants from Slovenia prefer Slovenian, Croatian and Serbian products (in that order), they do not buy new Serbian brands (unavailability of new Serbian brands in Slovenia), (results for global brands are same for all four region); medium “patriotic/ethnocentric” tendency;

- 4) Participants from Serbia prefer Serbian, Slovenian and Croatian products (in that order), they buy new Serbian brands (daily needs), (results for global brands are same for all four region), medium “patriotic/ethnocentric” tendency;

Concerning gender division of combined results (Focus Groups ABCD), we can observe following patterns:

- 1) Male participants prefer following types of brands: cars, home appliances, cell phones, food and beverages (in that order), they are less nostalgic and emotional (more rational), more “patriotic/ethnocentric”;
- 2) Female participants prefer following types of brands: make-up, fashion items, food, beverages, cell phones and cars (in that order), they are more nostalgic and emotional (less rational), less “patriotic/ethnocentric”;

Concerning educational division of combined results (Focus Groups ABCD), we can observe following patterns:

- 1) Participants with high school educational level prefer less technologically advanced brands (oriented toward traditional brands and beverages), they are more nostalgic and emotional (less rational), more “patriotic/ethnocentric”;
- 2) Participants with university degree educational level prefer more technologically advanced brands (oriented toward global brands and healthy products), they are less nostalgic and emotional (more rational), less “patriotic/ethnocentric”.

6. Conclusions

Results showed that consumers from transitional markets of former Yugoslavia prefer group of brands that they evaluate mostly by “emotional-nostalgic” approach: Ex-Yu brands. They know that the Ex-Yu brands, in many cases, presented just a “legends”, a nice story, but nevertheless, they “want” to believe in “this story”, so they give them relative-small advantage in comparison to Foreign (“new-global”) brands. Secondly, affection toward Foreign (“new-global”) brands is their rational statement made in order to “compensate” for previous “irrational” one, for which they are “sub-consciously” aware of. Relative unpopularity of New Serbian brands also indicates that the New Serbian brands are largely unavailable in certain markets of former Yugoslavia (namely Croatian and Slovenia) due to political reasons. Combined results indicate that these brands are deeply incorporated into their memory and that the reflection of these brands still emulates old purchasing habits and strong positive feelings toward them. Elevated attitude (slightly toward copying) has been provided toward issue of

“copying” the global brands. Participant’s attitude was that Ex-Yu brands should evolve (marketing, design and packaging) and that the changes of brands at Serbian market are a positive process (creates better competition).

Combined results of conducted research indicate that youngest generation (which are not emotionally attached to ex-Yu brands) is not interested too much in “legends”, while emotional attachment of older participants appears very strong (they grew up alongside with these brands). Reasons for emotional attachment of older generations lies in fact that these participants still (want to) believe that we have lived “one happier period of time back then”. In that context, it is normal that they appreciate type of the values they believed in the past. For example, Serbian consumers highly evaluate Slovenian brands such as Gorenje, in spite of political problems, due to their inbound production and design qualities, a phenomenon that was expected to be founded as a result of a conducted research. In addition, participants ranked Ex-Yu brands in front of global brands in direct comparison. Consciously, they are aware of reality, but their actual purchasing decision will be inconsistently different from expected. Estimated influence of emotionally nostalgic *stimuli* (actual evaluation of traits by actual purchasing decision factor), present actual range (usefull value) of these emotions over consumer purchasing behavior. In the case of Serbian and other ex-Yu consumers, estimated influence of this factor ranged from medium-high to medium (for both groups respectively). Difference in influence between these groups clearly indicate that the Serbian consumers are slightly more nostalgic toward these brands, a fact that should be strongly considered and exploited in future marketing strategies deployed at Serbian market. Marketing strategies deployed in other markets of ex-Yugoslavia should also consider that approach but with a dose of caution (especially in Croatia and Slovenia due to various political reasons).

Positive response toward uniqueness and negative toward historical value was detected in participants answers as well. They evaluate them as different but not that important to become “historical one”. This result also reflect interesting evaluation of these brands: they are good enough to be “unique” but not serious enough to become “historical one”. Thus, their, subconsciously presented “emotional value” goes “hand by hand” with uniqueness but not with perceived “historical value”.

Inconsistency in purchasing behavior presented no surprise because people from this region frequently made their decisions compusivly (emotionaly) without “consulting” rationality. The specific level of ethnocentrism and brand patriotism registered in this research (low-medium level), presented a proof that cultural bondage and heritage of common ex-country, was stronger than legacy of civil war. High-moderate level of openness toward changes could be seen as a specific “request” (need) for changes (technological and visual ones).

Global brands were depicted as brands of Top quality, excellent and very good quality, Expensive brands, brands with Long tradition and brands of Perfect-modern design. Such results indicate that ex-Yu consumers evaluate brands by that scale and order. It also shows that the high quality of global brands is more important, for them, than their “high price”, tradition or design. It appears that they are willing to pay more but “wants to be sure” that they have bought a top quality brand.

Overall relative unpopularity of New Serbian brands (in comparison to ex-Yu and global brands) additionally indicates the value and impact of emotional-nostalgic feelings, of which these brands do not have attached to themselves. They are new, relatively unknown and participants are not sure in their overall quality. It also indicates that the New Serbian brands are largely unavailable in certain markets of former Yugoslavia (namely Croatian and Slovenia) due to political reasons.

Relatively high percentage of indecisive answers (toward comparison between ex-Yu and global brands) indicates that this issue was also the point where patriotic reasons (affection) toward former Yugoslavia and evaluation of real qualities of Foreign (“new-global”) brands collide. Clear inconsistency in purchasing behavior of all groups with mixture of “patriotic/ethnocentric” and “rational” reasons, showed noticeable collision between “image and reality” concerning these issues. Consumers from transitional markets of former Yugoslavia are in favor of keeping some important quality traits of ex-Yu brands, but also, that, they are in favor of visual and marketing changes. They are slightly in favor of copying the global brands, but also want to keep visual identity of ex-Yu brands recognizable. They consider the process of evolving affirmatively (technologically, in design and advertising style), as well as changes of brands at the market (beneficial).

Specific political issues in former Yugoslavia and complicated Balkan history, as factors which deeply affected (and still affects) regional consumers’ attitude toward brands, presented additional interesting challenge to deal with. Impact of these issues over specific values of ethnocentrism and brand patriotism, in this case, proved to be closely connected with “emotional attitude” that was generated in former Yugoslavia.

Revealed research data indicates that one of the reasons for such “subconsciously” reflected “positive” attitude is common cultural and political heritage of former Yugoslavia. In the same time, investigation of specific values and impact of this heritage also provided measured values of “emotional involvement” emitted from these consumers. Consumer’s attitude toward so-called “new-domestic” brands additionally reflects the difference in “affection” which occurs due to the absence of “heritage-emotional” effect. Consumer’s attitude toward global brands, on the other hand, reflects the difference in attitude toward “domestic” and “foreign” and “traditional and new”, emitted through “conscious” evaluation of their traits.

Generally, ex-Yu brands should withhold, sustain and improve their positive properties embodied in their hardly earned brand loyalty, trust and emotional message. Persistently preserving their image, traditional brands should be always oriented toward consumer's choice and follow his emotions.

The basics of trust toward "old-socialistic" traditional brands are not being found in really - greater consumer's convictions toward superior values of these brands but in their emotional background. Creating a good and well-known brand at the market is not an easy task. It helps when you get to the "heart" of the problem.

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MILETA TOMIĆ, M.A.

Ministry of the Interior of the Republic of Serbia, Belgrade

MOBBING: THE INCIDENCE OF MOBBING ACTIVITIES AND DIFFERENCES REGARDING WORKPLACE AND GENDER

Summary

The total of 369 respondents (215 men and 154 women) working both in manufacturing sector and administration participated in the survey. The following mobbing activities have been investigated: non-recognition of work, inadequate compensation, rejection, ignoring/isolation, humiliation, gossiping, mockery, unjustified criticism, bad assessment of work, excessive control, work overload, assigning tasks employees are overqualified for, giving worse workspace, work assignments that impair health, not allowing employees paid time off, not allowing employees days off, threats, unjustified accusations, a position of a scapegoat, sexual harassment. The results of the research show that 80.87% of respondents were exposed to at least one mobbing activity, regardless of their workplace. 78.72 % of all respondents working in administration and 82.81 % of those working in manufacturing sector were exposed to at least one mobbing activity. The rank of exposure to mobbing activities is the following: 1. inadequate compensation, 2. excessive task assignment – work overload, 3. insufficient recognition of work and achieved results, 4. work tasks that impair health and 5. not allowing employees to use paid time off when it suits them, without disturbing the work process. The rank of exposure to mobbing activities of employees working in administration is the following: 1. inadequate compensation 2. insufficient recognition of work and achieved results 3. excessive task assignment – work overload, 4. performing tasks they are overqualified for and 5. unjustified accusations. Women from both groups of workers point out insufficient recognition at work as a mobbing activity much more frequently than men.

Key words: *mobbing, mobbing activities, workplace differences, gender differences*

JEL classification: J71, J83

1. Introduction

A widely accepted definition of mobbing is the following: “Mobbing is a psychological terror in working life; it involves hostile and unethical communication which is directed in a systematic manner by one or more individuals, mainly toward one individual, who, due to mobbing, is pushed into a helpless

and defenseless position and held there by means of continuing mobbing activities. These actions occur on a very frequent basis (statistical definition: at least once a week) and over a long period of time (statistical definition: at least six months' duration). Because of the high frequency and long duration of hostile behavior, this maltreatment results in considerable mental, psychosomatic and social misery."¹

Leymann's definition has, in some of its segments, been adjusted to social and cultural milieu of the environment, especially when it comes to the factors of recognizing mobbing. Thus, the Swedish National Institute for Protection and Hygiene at Work provided the following definition of mobbing, called "victimization": "Victimization is a repetition of extremely negative or reproachable actions which are directed towards employees and can lead to their exclusion from the community in the workplace."

Interantional Labour Organization (ILO) defines mobbing as "offensive behavior through vindictive, cruel, malicious or humiliating attempts to undermine an individual or groups of employees. People team up against a certain employee; he/she is mobbed and exposed to psychological harassment. Mobbing includes continuous negative remarks, criticism, office gossiping, spreading false information, which socially isolates employees."

According to French Social Modernization Law of 2002: "mobbing is psychological violence that occurs while performing certain activities; its objective and consequence is degradation of working conditions which can violate human rights and damage human dignity, damage physical or mental health or discredit the life and professional future of the victim."

In Serbian Prevention of Harassment at Work Act mobbing is defined in the following way: "harassment is every active or passive behaviour towards an employee or group of employees that is repetitive, and which intends or presents violation of dignity, reputation, personal and professional integrity, health, employee position and which causes fear or creates a hostile, humiliating or insulting environment, worsens the conditions of work or leads to employee isolation or causes an employee to terminate employment or employment agreement at his/her own initiative. Harassment, pursuant to this act, is encouraging and inciting others for behavior stated in paragraph 1 of this article."

2. Mobbing is a form of violence

Types of violence are the following: physical, verbal, social, sexual, emotional, gender, self-directed violence and violence by means of modern technology. The elements of all forms of violence can be found in the workplace.

¹ H. Leymann, *The Mobbing Encyclopaedia. Bullying: Whistleblowing. Information about Psycho terror in the Workplace*. 1992; <http://www.leymann.se/>

Physical violence involves hurting the body of another person. It can have various forms: punching, kicking, pushing, strangling, pulling, arm twisting, hitting with arms, legs or objects, hurting others with weapons, murder, locking up, abduction and destruction of possessions... Although mobbing is primarily defined as psychological violence at workplace, physical attacks of mobbed employees are also common.

Verbal violence involves the use of words and verbal symbols in order to hurt someone's feelings. It includes the following: offending (when someone tells others they are stupid, ugly, calls them names), mocking (when someone mocks others because of height, weight, background...), humiliating (when someone tells others they are worthless, that nobody loves them...), when one is blamed for something he/she did not do, or when someone is threatened. These forms of violence are very common in the workplace.

Social violence occurs when someone is gossiped, excluded from group activities, when lies are told about him/her or others are talked into ignoring them. All the activities that are forms of social violence can be seen in the workplace.

Sexual violence occurs when someone receives nasty comments, or is touched on his/her intimate parts without their will, shown nasty pictures, forced to have sexual intercourse. Sexual harassment at work is a mobbing activity.

Emotional violence is intentional hurting of someone's psyche. It can be verbal and non-verbal. Emotional violence can leave severe and long-term consequences on the personality of a victim. This form of violence is common in the working environment where communication is bad. Hurting other's psyche is common at the workplace, regardless of who commits it – whether it is a superior or victim's colleagues, or both.

Economic violence involves stealing money or other material possessions. An important form of economic violence is violence towards employees in a company, when they receive inadequate compensation or are paid irregularly. Salary cutting, against the regulations or the contract that an employee concluded with an employer, with the aim to provoke objection of the employee, so that he/she is proclaimed undisciplined, is also a form of violence at work. Provoking of this sort can result in disciplining of an employee, with the ultimate aim that he/she eventually self-willingly leaves the organization they work for. Economic violence, as a form of mobbing, is exclusively reserved for top management.

Cultural violence is committed against people who are in some way culturally different, most commonly by customs or habits, social attitudes, religion or race, or other ethnical community or sexual orientation (most commonly homosexuality). Cultural violence in the function of mobbing is more common in multiethnic, multicultural and multiconfessional societies. Gender violence is committed against the opposite sex; gender violence against women is more common than against men. As surveys suggest, mobbing is also more common against women.

Violence by mobile phones and the internet is when one, without permission, records others by telephones and sends the content to others, or disturbs people by phone calls, texts or e-mails. Violence by means of modern technologies is widespread among the young and in technologically developed countries. All forms except physical violence can be committed by means of modern technologies. The most common form of mobbing in the workplace is leaving rude and offensive messages on the computer, together with mocking and humiliating on social networks. This way, mobbing activities are relocated from working environment, but the aim is the same: to humiliate the victim of mobbing and psychologically hurt him/her.

Some people who have problems expressing their feelings, reacting properly and do not commit violence against others, direct it against themselves. The ultimate act of self-directed violence is suicide. The warning signs of self-directed violence are the following: multiple suicide attempts, continuous use of alcohol or drugs, threatening by suicide or talking about suicide and death, isolation, withdrawal, substantial changes in sleeping and eating habits, feeling of hopelessness, inability to control aggressive behavior, aggressive behavior, loss of interest for everyday activities, problems with the law, problems with authorities, perfectionism. That way a person conveys a message that he/she will be gone in the near future. If that message is registered in due time, suicide can be prevented. Suicide can be a result of mobbing, when a victim of mobbing can no longer find a way out and when he/she has no understanding and support from the environment.

3. Most common victims of mobbing

Analysts who studied mobbing tended to define the most common victims of mobbing and found that these are the following:

- 1) upright employees who witnessed and reported various irregularities at work;
- 2) invalids with different degrees and forms of body invalidities;
- 3) young employees, at the beginning of their careers, and older workers who are about to retire;
- 4) employees who ask for better work conditions and more freedom at work;
- 5) employees who require recognition of their position or pay rise after years of impeccable work;
- 6) employees who are made redundant;
- 7) religious minorities (in the European countries Muslims are mocked about leaving work for praying – they pray a couple of times a day);
- 8) ethnic minorities;

- 9) employees of different sex – a woman in a group of men or a man in a group of women; employees whose sexual orientation is different from that of majority;
- 10) extremely creative individuals;
- 11) eccentrics;
- 12) the sick – absences because of illness cause discontent of employers; sometimes employers are burdened on their ‘weak points’ (e.g. employees who have back pain are made to carry heavy loads);
- 13) the newest employees, those who came last in the company feel jeopardized by potential competition; a group of employees starts humiliating, isolation and mobbing new employees.

4. Ways of carrying out mobbing

There are numerous ways of harassing employees at work. Leymann found even 45 subtle activities that can be recognized in the process of mobbing. They can be divided into the following categories:

- 1) Disabling adequate communication– superiors and/or colleagues restrict the ability of victims to express themselves, victims are interrupted when speaking, non-verbal contacts with victims are rejected – avoidance of eye contacts and signs (e.g. a sign that a victim wants to say something, like raising hand for a word, etc.);
- 2) Denying the right of establishing social relations – mobbed victims are constantly isolated and ignored; colleagues act as though they did not exist, they are relocated to offices that are distant from their colleagues’ offices, they are not invited to meetings and informal social gatherings...
- 3) Attacking one’s reputation- when stories about victims and their private lives are made up; when they are mocked, gossiped, or when unfavorable comments about negative aspects of their personalities are made;
- 4) Criticizing professional qualities– constant criticism, complaints, offences, excessive control, bad assessment of work and punishments. Victims are not given tasks, they are taken away tools for work like telephone or computer (“empty desk” syndrome); employees are assigned tasks which are disproportional to their educational potentials or professional qualification– they are either too simple or too hard, with the aim that the victim makes a mistake. The same effect is achieved with task overload and giving unrealistic deadlines (this is the “full desk syndrome”), together with constant changing of work tasks.
- 5) Impairing health – this form of mobbing means that employees are forced to perform work and tasks that damage their health or worsen already impaired health; they are not given paid time off (when it does not dis-

turb the work process), they are threatened by physical violence, verbally or sexually harassed, etc.

5. Our survey: exposure to certain mobbing activities

The survey was conducted during 2010 in a few Belgrade companies using questionnaire. A certain percentage of surveyed respondents work in manufacturing sector (137 men and 85 women), while some of them work in administration (78 men and 69 women). The total of 369 people participated in the survey- 215 men and 154 women.

Table 1: Incidence of mobbing activities at work/in production

Mobbing activity	men		women		total	
	%	rank	%	rank	%	rank
Nonrecognition of work	23.0	5	58.7	2	36.6	3
Inadequate salary	57.8	1	86.8	1	69.4	1
Rejection	1.6	20	9.6	19	6.0	21
Ignoring/isolation	7.4	16	22.2	10	13.4	14
Humiliation	16.4	10	20.5	12	13.8	12
Gossiping	8.0	14-15	21.9	11	13.6	13
Mocking	6.0	19	13.9	18	8.5	19
Bad work assessment	6.5	18	17.0	15	10.6	17
Excessive control	7.0	17	15.9	16	11.1	16
Work overload	17.5	9	19.0	13	18.3	10
Tasks inappropriate to qualification	29.6	4	58.0	3	39.8	2
Worse workspace	19.6	7	29.3	5	24.9	7
Health impairment	15.5	12	18.0	14	17.2	11
Deterioration of health	20.5	6	46.6	4	30.7	4
Not allowing employees to use PTO	18.7	8	27.1	6	21.8	8
Not allowing staff to use days off	29.8	3	26.8	7	27.3	6
Threatening	31.4	2	22.6	9	27.7	5
Unjustified accusations	10.6	13	6.3	20	7.4	20
Scapegoat	16.0	11	24.9	8	20.8	9
Sexual harassment	8.0	14-15	14.2	17	11.2	15
	0	21	1	21	0.5	22

We examined the exposure to the following mobbing activities: insufficient work recognition, inadequate salary, rejection, ignoring/ isolation, humiliation, gossiping, unjustified criticism, mocking, bad work assessment, excessive control, work overload, assigning tasks which are inappropriate to the qualification level, giving worse workspace, assigning tasks that impair health, banning employees from using paid time off and days off, threats, unjustified accusations, position of a scapegoat, sexual harassment.

According to the results of the survey, 80.87% of all the respondents have been exposed to mobbing, i.e. to at least one mobbing activity, regardless of their workplace. 78.72% of all the respondents working in administration and 82.81% of all the respondents who work in manufacturing sector have been exposed to at least one mobbing activity.

75.0% of all the male respondents have been exposed to at least one mobbing activity- 71.23% of men who work in administration and 77.37% of men who work in manufacturing sector. When it comes to female respondents, 88.96% have been exposed to at least one mobbing activity- 86.76% of them work in administration, while 91.67% work in manufacturing sector. The results of the survey are given in the table, which shows the percentage of respondents exposed to every mobbing activity, the rank that certain mobbing activities have according to its frequency when it comes to both men and women, and the total number of respondents in administration and manufacturing sector.

Table 2: Incidence of mobbing activities in administration

Mobbing activity	men		women		total	
	%	rank	%	rank	%	rank
Nonrecognition of work	22.1	5	35.1	2	31.9	2
Inadequate salary	48.9	1	71.0	1	63.3	1
Rejection	4.9	20-21	7.0	15-16	5.0	17
Ignoring/isolation	13.4	9	15.8	8	10.7	11
Humiliation	11.6	10	13.4	9	13.0	8
Gossiping	17.7	6	6.4	17	13.9	7
Mocking	1.9	20-21	7.1	14	5.0	18
Bad work assessment	10.4	11	5.1	18	7.3	15
Excessive control	8.2	13-15	7.0	15-16	7.9	13
Work overload	8.2	13-15	3.0	20-21	5.1	17
Tasks inappropriate to qualification	30.9	2	25.0	3	27.1	3
Worse workspace	23.8	3-4	24.9	4	22.1	4
Health impairment	9.4	12	13.0	10	12.1	9
Deterioration of health	15.3	7	19.8	5	14.9	6
Not allowing employees to use PTO	13.5	8	8.4	13	8.0	12
Not allowing staff to use days off	5.8	17	18.7	6	11.3	10
Threatening	5.6	18	9.2	12	7.1	16
Unjustified accusations	7.4	16	3.0	20-21	3.6	19
Scapegoat	23.8	3-4	16.8	7	19.1	5
Sexual harassment	8.2	13-15	9.9	11	7.8	14
	0	22	4.0	19	1.4	20

6. Conclusion

Based on the obtained results, the following conclusions can be made:

- a) Mobbing is a very common phenomenon in our environment. A large number of employees claim they are victims of at least one form of mobbing activities in their organization, whether mobbers are top managers (which is referred to as vertical mobbing), or mobbing is carried out by colleagues of mobbed employees (which is horizontal mobbing), or mobbers are both superiors or colleagues on the same hierarchical level as the mobbed employees (this is vertical and horizontal mobbing at the same time).
- b) 80.87% of all respondents who participated in the survey were exposed to at least one mobbing activity, regardless of their workplace.
- c) 78.72% of all respondents who work in administration and 82.81% of respondents who work in manufacturing sector were exposed to at least one mobbing activity.
- d) There is virtually no mobbing activity which is not present in our working environment– the only exception is sexual harassment of men in both surveyed sectors.
- e) When it comes to mobbing activities and women, both in manufacturing sector and administration, there is no mobbing activity they are not exposed to at the workplace. The rank of exposure to mobbing activities of employees in manufacturing sector, regardless of gender, is the following:
 - 1) inadequate salary;
 - 2) work overload;
 - 3) insufficient recognition of work and achieved results;
 - 4) assigning tasks that impair health;
 - 5) not allowing employees to use paid time off when it does not disturb work process.
- f) The rank of exposure to mobbing employees in administration, regardless of gender, is the following:
 - 1) inadequate salary;
 - 2) insufficient recognition of work and achieved results;
 - 3) work overload;
 - 4) assigning tasks inappropriate to qualifications;
 - 5) unjustified accusations.
- g) The rank of exposure to mobbing activities of male employees in manufacturing sector is the following:
 - 1) inadequate salary;
 - 2) not allowing employees to use days off;
 - 3) not allowing employees to use paid time off;
 - 4) work overload;
 - 5) insufficient recognition of work.

- h) The rank of exposure to mobbing activities of female employees in manufacturing sector is the following:
 - 1) inadequate salary;
 - 2) insufficient recognition of work;
 - 3) work overload;
 - 4) health impairment;
 - 5) assigning tasks inappropriate to qualifications.
- i) The rank of exposure to mobbing activities of male employees in administration is the following:
 - 1) inadequate salary;
 - 2) work overload;
 - 3) assigning tasks inappropriate to qualifications;
 - 4) unjustified accusations;
 - 5) insufficient recognition of work.
- j) The rank of exposure to mobbing activities of female employees in administration is the following:
 - 1) inadequate salary;
 - 2) insufficient recognition of work;
 - 3) work overload;
 - 4) assigning tasks inappropriate to qualifications;
 - 5) impairment of health.
- k) A great majority of respondents pointed out inadequate salary- 53.5 % of all male respondents, regardless of the sector they work in, and 78.8% of all women, which implies that there is a significant difference in perception of a material position in companies, as well as considerable gender differences in rewarding performance in our environment, despite proclaimed gender equality.
- l) A logical consequence of such a state – unequal opportunities for men and women to earn, despite official proclamation on gender equality is a conclusion of respondents about (non)recognition of their work: women in both surveyed groups– manufacturing sector and administration, point out insufficient recognition of their work significantly more frequently than men.

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ASSISTANT PROFESSOR MIRJANA VUKSANOVIĆ, PHD*
Health Center "Dr. Milutin Ivković", Belgrade

IS MANAGER'S GENDER AN IMPORTANT FACTOR IN SELECTION TO A POSITION?

Summary

Management is a complex activity. As social psychology interprets, management is a form of governing a group in which a person who has the greatest social power - the leader - alone or in cooperation with other group members participate in group decision-making in order to achieve successfully the objectives of the group and meet the needs of members in the best possible way. A manager is a person who runs and controls business. Their duty is to manage a part or the whole company and their career as well. Manager as a profession implies an expert for organisation and management in business. Competence, which involves continuous and systematic education and training, is the first condition which should be fulfilled by an individual or group of managers who make up the management team. That is why it is very important what characteristics a person in a position of a manager will have. Besides personality characteristics such as intelligence, communication, morality, fairness, and emotional stability, adequate knowledge and the need for continuous improvement, gender has a significant role in the selection of managers. Research which gathered 89 men and 98 women showed that 53.06% of respondents of both genders would choose a man for the manager, although male and female candidates have equal abilities; 24.49% of respondents would choose a woman for the manager, and 22.45% of respondents said that it did not matter whether the manager was a man or a woman.

Women executives are more unwelcome as leaders among women than among men. The vote for a man is given because of tradition and habit that the manager should be a man. This argument is primary in respondents of both genders. Negative, sexist responses of a part of men stated that women in general were less capable and smart, that they were unable to be in managerial positions. Women who were against women in managerial positions cited negative characteristics that are often attributed to women as reasons: pettiness, hysteria, a tendency to gossip and mutual disagreement. Both men and women in this research who gave their vote to women mentioned positive female features: greater flexibility, greater cooperation, honesty and personal understanding.

Key words: management, personal characteristics, gender, tradition, stereotype

JEL classification: M12, J71

* E-mail: vuksanovici@vektor.net

1. Introduction

1.1. *The concept of management*

Management is a very complex activity. As social psychology interprets, management is a form of governing a group in which a person who has the greatest social power - the leader - alone or in cooperation with other group members participate in group decision-making in order to achieve successfully the objectives of the group and meet the needs of members in the best possible way.

Nowadays, the term “governing” is increasingly replaced by the term “management”. Management is defined as a process of governing that is implemented in accordance with certain rules, respecting proven principles and implementing appropriate techniques.

Management is the English word and it means control, work control.

The term includes:

- an activity or ability to manage and organize activities of a company or organization;
- a group of people who have the task to manage a company or organization
- an activity or ability to resolve certain situations that should be controlled

If we analyze this seemingly complex definition, we conclude that management is not really a new phenomenon or a new profession - it is just a redefinition of business terminology, the widespread use of earlier suppressed term for governing (suppressed because it was “western” or capitalistic).

Management generally involves a form of hierarchical organization in business management in which highly specialized experts are bearers and initiators of research, planning, organization of work processes, marketing and distribution of the results of this work - goods and services.

In Campbell's Dictionary of Finance it is said that the concept of management is treated differently in theory and in practice. The general meaning of the term usually includes leadership, skill, workmanship, which is not sufficiently precise definition. It is necessary to determine what is important in the concept of management. It is known that for work management or solving a task, preparation and realization are necessary, which can be achieved by division of labor activities, analyzing and making appropriate decisions for taking action. Management consists of: planning, organization, management and evaluation.

Managers, who are generally called directors and executives in our country, realize the function of management. The manager is a person who leads and controls the business. His duty is to manage a part or the whole company, but also to manage a business career.

Manager as a profession involves a specialist for the organization, leadership and management in business. Competence, which represents continuous and

systematic education and training, is the first condition that the manager should fulfill as an individual or group of managers who make up the management team. In modern management systems, the emphasis is on the team - the team work requires knowledge, expertise, skills, creativity, cooperation, harmony, agility and respect for hierarchy. It covers the field of ideas, research, designing, planning, operationalization, implementation, management and analysis.

Naturally, if you want maximum performance and efficiency, the way to find the most favorable conditions and the best solution should not be a conformist, habitual, patterned, but creative and rational one.

1.2. Governing - the most complex function of management

In the modern world of work, due to rapidly increased amount of knowledge that mankind possesses, the increasing complexity of tasks and often very tight deadlines, more work is done by teams.

In various stages of project development and task realization, it is necessary to involve experts of various profiles, and they, according to their skills, take over process management in stages in which they can offer most.

In addition to multi-disciplinary and specialized knowledge, it is necessary to develop quality relationships and positive atmosphere in the group and optimal motivation for work and cooperation in order to achieve successful management, especially team management.

Managing people is the most complex function of management, and its purpose is to influence people so that they contribute to the common objective. Since all employees participate in work realization and achievement of the common objective, one must take into account the motivation of all participants, their respect and dignity. The task of managers is to discover optimal methods and techniques to motivate their staff and ways of dealing with and overcoming conflicts that might occur.

This is an ideal which should be aspired. Knowledge can be acquired and science can be traced, but there is something which is almost constant, which is very difficult to change and that is a personality of a manager. The way of management, therefore, cannot change, because personality traits are relatively permanent characteristics of an individual. If a management style of an individual who manages a group does not correspond to the group and if because of that there are no results, it is easier to replace the manager and find the one whose personality and management style correspond to the group.

1.3. What characteristics should a good manager have?

The most important factors of leadership are personal characteristics of the individual who aspires to be a leader, characteristics of subordinates and envi-

ronmental characteristics. Regarding the personal characteristics of leaders, these are important:

- Developed perception - it is important that the leader sees things the right way, that he is not biased and has no prejudices; perceptual ability is subject to learning.
- Defined system of values - understanding the individual about what is right or wrong, morality, honesty and fairness: according to their system of values, a leader selects organizational performances.
- A tendency towards risk - this is the feature by which managers differ from other employees; they have more confidence in their entrepreneurial ability than in the "fate".
- The background of the leader is important, more than it is believed - family background and culture; among other things, the attitude to authority depends on one's origin.
- Developed interpersonal and communication skills – they have to have an impact on others and the ability to be followed, to know to choose the right way to influence others, to know when and whom to reward, and when and whom to punish.
- One of the important features is the choice or preference of decision-making models - whether you choose "top down" model of decision making, which emphasizes speed and efficiency, or the opposite "bottom up" model that emphasizes informing of employees and their efficiency.

We rarely choose bosses, directors and other managers on our own. We all think that we know exactly what they should be like and what features they should have. Numerous studies, especially psychological ones, have dealt with the most and least desirable characteristics of managers and leaders.

Summarizing the results of these studies, we can conclude that a manager has to possess certain characteristics in order to carry out numerous tasks of high complexity. The characteristics follow:

- Intelligence - given that a leader is expected to solve different problems quickly, skillfully and appropriately, he needs to possess a higher level of general intelligence.
- Professional ability - adequate education, expertise, efficiency, experience, proper use of funds.
- Specific planning ability - good planning is essential for successful operations.
- Communication skills - skills in interpersonal communication are an important requirement for a clear definition of objectives and their presentation to team members; without good communication there is no successful resolution of conflicts; it is necessary for active listening and getting feedback from group members.

- Flexibility in thinking and behavior, which include openness to suggestions of other participants in the work.
- A tendency toward informing team members about his knowledge and experience, rather than selfishly retain the knowledge for oneself in order to hold the position of superiority.
- Kindness and courtesy in dealing with others, but also a firm stand when a situation requires.
- A good relationship with group members – a group leader will have more support of team members, greater impact on them and a better position if he develops a good relationship of trust and respect with team members.
- Keeping the distance - the authority is lost if a leader is too intimate with some team members; privacy of a leader and team members should not be questioned.
- Giving one's own example - a leader should demonstrate examples of positive behavior, such as cooperativeness, diligence, punctuality, sincerity, openness and honesty.
- Taking into consideration the abilities of people with whom he is in any kind of business communication - do not delegate routine tasks to highly skilled team members and communicate with them at their level; explain in detail what less skilled workers are expected in work process and adapt vocabulary and style of presentation to their level.
- Determination in leading the group, which is specifically required in the complex and critical situations.
- Avoiding the delegation of tasks in a way that they cannot be done and not insisting on tasks which some group members are unable to perform, because it undermines the authority of the leader.
- Emotional stability - only emotionally stable leader may cope with stress which is often related to managing operations.
- Ability to establish and maintain control over a situation - in conditions of good control decisions are made better and their success can be foreseen in a better way; in cases of highly qualified and motivated team the control should not be too great, because it can stifle new ideas.
- Ability to maintain discipline in a team - it is better to develop self-discipline among team members than impose a discipline outside, so it is necessary to avoid public penalties and criticism and try to find causes of problems and solve them. Public criticism causes a feeling of humiliation, which reduces the motivation for work. Excessive praise and rewards are not good either, especially when they are always addressed to the same team members, because other team members may feel neglected and less valuable. This does not mean that in some important situations tougher sanctions should not be applied.

- Positive internal motivation for performing management tasks - just a good salary and social status are not good enough motives for management. That is the so called external motivation. Internal motivation involves the love of work, interest in the profession, the need for acquiring new theoretical and practical knowledge and professional development. The worst possible motivation for management is the will for power.
- A leader must not be narcissistic and omnipotent – thinking that he is the best and that he knows everything - this refers to managers who accept appointments to leadership positions for which they are not qualified or do not have knowledge and previous experience, those who “get lost in the profession”, meeting their own needs to dominate as well as needs of groups (mostly not professional, but different political parties and clans) who elect them and achieve their goals through them.

No part of the research which tells about the optimum and most desirable characteristics of a manager states basic demographic category, the gender of manager who manages or is elected to manage an organization, although we know from experience that this is one of the most important elements that influences the selection. In addition to gender, other demographic characteristics are important: age, education, marital status.

2. Research: Is it better that a manager is a man or a woman?

2.1. Problem definition

Setting this issue can be characterized as sexist. However, in practice we almost always face the question of which sex is a candidate for a manager, even before questions about one's professional and personal qualities. In a survey, I have asked respondents: “Is it better that your manager is a man or a woman, and why?” It is interesting that respondents have answered very openly, without hesitation or reservation to the female interviewer, even when they have not favorably talked about female managers (probably because the interviewer has no managerial position).

2.2. The sample of respondents

Respondents are employed, adult, both male and female and with different levels of education (from primary school to higher education), married and single. 89 male and 98 female respondents were surveyed - a total of 187 respondents. The sample was appropriate - it was composed of employees who for some

reason had been referred to the assessment of work capacity (initial employment, periodic and targeted appraisals).

2.3. Time and place of survey

The survey was conducted in the Department of Functional Diagnostics of Health Center "Dr. Milutin Ivkovic," in Palilula, in Belgrade in 2011.

2.4. Survey techniques and processing of results

The main question in the survey was: "Is it better to have a man or a woman for your immediate supervisor and why?" The responses were analyzed with regard to the following demographic characteristics: gender, age, education and marital status. By crossing these data, profiles of respondents were formed with specific attitudes about the importance of gender on the preference and selection of managers.

3. Results of survey

The results of the survey are classified into two broad categories: responses and attitudes of male respondents, and responses and attitudes of female respondents. We formed profiles of respondents, giving a better overview of attitudes towards the surveyed phenomenon - the preference of the manager according to the gender, based on the demographic characteristics of respondents.

Interestingly, the education of the respondents did not influence the attitudes about the desirable gender of the manager. Therefore, the variable of education was not specifically analyzed. Besides the gender of the respondents, age and marital status were also important.

3.1. Responses of male respondents

- Married young men, up to age 30, in equal numbers (33.33%) say that it is better that a manager is a man or that it is better that a manager is a woman, or that they do not care which gender is a manager.
- Married men, older than 30 years, in 50 % cases 'vote' for a man, in 20% cases 'vote' for a woman and the rest say they do not care which gender is a manager.
- Unmarried men, age 30, by two-thirds majority (66.66%) vote for a man in a leadership position; others (33.33%) are for a woman. There are no those who do not care which gender is a manager.

- Unmarried men, over age 30, vote for a woman in a leadership position. However, there were only five of these respondents, but all five (100%) said that when they could choose, they would choose the female manager!

3.2. Responses of female respondents

- Married young women, up to age 30, said that they would choose to have exclusively women as their managers. Here we have a relatively small number of respondents - only nine, but they all (100%) opted for women in managerial positions. None "voted" for a man, none was neutral.
- Married women, over age 30, voted in a different way: more than 58 % of them would choose a man for a manager, more than 8 % a woman and a third (33,33 %) do not care if a manager is a man or a woman.
- Unmarried women, up to age 30, in 37.5% of cases would like to have a male manager, 37.5% stated that they did not care, and only one in four would like to see a female person in a managerial position.
- Unmarried women, over age 30, only want a male manager! No woman in this group thinks about the possibility of having a woman as a manager. Also, none of them said that they did not care which gender was the manager.

4. Arguments by which respondents explain their attitudes

Respondents were asked to explain their answers and justify their attitude about a desirable gender of their manager by the question: "Why do you think a man / a woman would be a better manager?"

4.1. Arguments of male respondents

- a) Male respondents, who said that they would like to have a male manager, explained their attitudes in the following ways:
- women are not capable of being in a leadership position;
 - it is a custom that a man is a manager;
 - men are more responsible and disciplined;
 - women are too demanding;
 - we choose a man because men understand each other better;
 - we have more respect for male authority, that is a custom in our country; it may not be justified, but such is a tradition;
 - men are more capable in every respect;
 - men are less hairsplitting;
 - we are accustomed to men.

-
- b) Male respondents who “voted” for a woman in a managerial position stated the following reasons:
- women are less severe;
 - I prefer women;
 - women are more capable than men, I have a female manager and she is excellent;
 - my two sisters are managers and they really do well, they run two companies much better than men;
 - I have a male boss who harasses me, a woman would be better;
 - women are more flexible than men.
- c) Male respondents who stated that they did not care which gender was the manager said:
- gender is not important, it is important that work is done normally;
 - it is important that a manager is a good person and a good expert;
 - it is the same: women are more emotional and men are more serious;
 - it does not matter, whoever is the manager, he or she has to work.

4.2. Arguments of female respondents

- a) Female respondents who “voted” for a man in a managerial position said:
- I prefer men, I would tolerate a woman only if I was concerned - that I manage;
 - men are not negative in relation to women, women may be bad in a superior - subordinate relationship;
 - women are inharmonious, there is no conversation with them;
 - a man should manage and make decisions;
 - I think that women are evil, when they get authority, it goes too far;
 - I was brought up to have male authority, respect him and I would be more complete and ambitious as a worker with a male manager;
 - I have a bad experience with women executives, when women have a chance to command other women they are worse than men;
 - men have backing authority;
 - men are less complicated and less gossip;
 - men are generally less prone to hysterical outbursts in our society; I prefer women in personal communication but they proved to be poor managers;
 - I prefer men to women;
 - I have always had male managers, only one woman - God forbid that something like that happens again; I always understand male managers;
 - men have different interests from women at work, women look at things that have nothing to do with work.

- b) Female respondents who “voted” for a woman in a managerial position stated the following arguments:
- women are more honest; now I have a female manager and she is excellent;
 - women are more reasonable;
 - women are easier to cooperate with;
 - women better understand other women and their needs and problems;
 - men show that they are bad.
- c) Female respondents who stated that they did not care which gender the manager was said:
- good communication is important, not gender;
 - it is important that a person is capable as a manager;
 - it is important that we make progress and that we all feel better;
 - it is important that people are normal and that there is good cooperation;
 - it does not matter –it is important that a person is a good professional and has stable personality, who will not surround oneself with weaklings and poltroons and will not give primacy to members of political parties.

5. Conclusion

- If we look at surveyed men and women, regardless of gender (male + female, a total of 187), they would choose a manager according to gender as follows: 53.06% would “vote” for a man, 24.49% for a woman, and 22.45% of all respondents said that they did not care which gender the manager was.
- Surveyed men, married or unmarried, young and old, a total of 89, if viewed as a group, would “vote” for a man as a manager in 52.17% of cases, for a woman in this position in 30.43 % of cases, and 17.39% of them said that they did not care about the gender of the manager.
- Surveyed women, married and unmarried, old and young, a total of 98, considered together, would “vote” for a man in 53.85% of cases, for a woman in 24.49% of cases, and 22.45% would not opt for the gender.
- In all these categories, more than half of respondents gave preferences to male managers. Female managers have a much lower “rating” among women than among men (19.23% to 30.43%)! Women, age 30, would ‘vote’ for female managers, more often married than unmarried. Unmarried women over age 30 want only a man for a manager.
- From arguments that justify their choice, it can be seen that the vote was given to a man because of tradition and habit that a manager is a

man. This argument is primarily present in respondents of both genders. Responses of a part of men are negative and sexist, stating that women are generally less capable and smart, that they are unable to be in managerial positions. Women who are against women in managerial positions give as reasons negative traits that are often attributed to women (although that is not proven!): pettiness, hysterical outbursts, a tendency to gossip and mutual disharmony.

- Men who would like to see a woman in the place of the manager usually have positive examples of women who are successful leaders. A part of the surveyed women had a bad experience with male managers, so they would “vote” for women. Both men and women who gave their vote to women in this survey identified as positive female traits: greater flexibility, greater cooperativeness, honesty and personal understanding. Unmarried men “vote” more for women as managers than married men.
- Finally, the “voice of reason” has prevailed in almost a quarter of respondents, who were guided by the idea that gender is not important and that manager’s personal and professional characteristics, which are listed at the beginning of this paper, are more important.

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ASSISTANT PROFESSOR JELENA BATIĆ, PHD*
Graduate School of International Economics, Megatrend University, Belgrade

THE EFFECTS OF THE WORLD FINANCIAL CRISIS ON ECONOMIC MIGRATION TRENDS IN THE EU

Summary

International migration increases and decreases depending on the phase of economic cycle and so do the attitude and policies toward immigrants. History teaches us that it is expected and natural for the global recession to increase anti-immigrant sentiment and the possibility of encouraging new obstacles to migration. The current global economic crisis has directed public attention to the process of immigration. The shaken labour markets in the EU have begun to impose greater restrictions on potential competition from immigrant labour, while the 'inflated' fiscal deficits have increased concern about the additional burden of the welfare state system. Since a longer-term future is very uncertain, it seems that only severe and prolonged recession could have a substantial, long-lasting effect on migration flows. If the recession remains moderate or even weak, on the other hand, many factors that affect immigrants' return home during its duration should be reversed over time, once economic conditions improve. Factors such as continued demand in the labour market, demographic changes, considerations of international competitiveness, and a network of immigrant communities will provide the ongoing net immigration flows of various but significant extent.

The aim of this paper is to determine the impact of economic migrants in the labour market, what limitations and barriers they face, to what extent they compete with local labour and what the implications of the world's global financial crisis are for their survival in the destination countries? Will it reduce the volume of economic migration, or will it help increase the human capital in host countries in the years to come?

Key words: *global financial crisis, the EU members, economic migration, labour market, unemployment, migration policy*

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* E-mail: jbatic@megatrend.edu.rs

1. Introduction

Migration plays an important role in population dynamics of European societies. In recent years, population growth in the EU countries has mainly been caused by high rates of net migration¹. The share of international migration in overall population growth in the EU has fluctuated.

Unlike the self-proclaimed immigration countries of the new world - the USA, Canada, Australia and New Zealand - in Europe the issue of migration is much more complex. Many parts of European societies were reluctant to accept and incorporate immigrants, especially those who do not come from OECD countries, which are thought to have very different cultural and ethnic background. Anti-immigrant feeling was manifested in public support for restrictive immigration and asylum policies, the negative reports and articles on immigrants and asylum seekers in the popular press, discrimination against ethnic minority groups and anti-immigrant or racist harassment and violence.

2. Development and characteristics of migration policy in the EU

Very widespread, mostly poorly educated and low-skilled immigration forces from the 1950s and 1960s constituted a crucial component of the post-war reconstruction in Western Europe. Today, labour migration fills the critical 'gaps' in the IT sector, the construction sector, engineering, agriculture and food processing, health care, education, tourism and domestic services.

Placing migration policy under the jurisdiction of the European Union is a new trend. The Schengen Agreement of 1995, which binds thirteen of the fifteen current members, proposes the abolition of controls at internal borders of the Union. At the same time a common visa regime is established, the controls at external borders are strengthened and the Schengen Information System (SIS)² adopted. It contains the identities of persons who are prohibited from staying in the EU territory, and it is available for inspection at all points of entry into the Schengen zone.

¹ The term 'total net migration' in the EU members differs from the term 'total net migration into (from) the EU as a whole'; the first term also includes the international migration between the EU member states. The population of Germany and France increased by 16% and 17% respectively as a result of migration. The increase of over 10% can also be seen in Belgium, Spain, Austria and Sweden, while in the UK migration contributed only by 5% to the increase of the total population. Portugal (-21%) and Bulgaria (-14%), on the other hand, would have a larger population without migration. In the case of Italy, recent immigration has compensated for the effects of emigration losses by 2007.

Source: EUROSTAT: Key figures on Europe, 2010, p 50.

² M. Morokvašić, 'Migracije u Evropi: zabrinutost povodom proširenja EU na istok', *Stanovništvo*, 1-4, Beograd, 2003, p. 133-135.

With the Amsterdam Treaty from 1997 the Member States' competence on asylum and immigration becomes a part of common European policy. However, harmonization remains difficult: due to the national interests, it is not easy for the member countries to renounce their legislation and become subject to European norms³.

Therefore the return to *individual initiatives* has become noticeable in the migration policy for the past few years, i.e. to the initiatives limited to national boundaries. What they have in common, however, is that they rely on market economy and openly recognize the necessity of immigration. For example, Germany, which has already practiced the 'exceptional employment' of foreigners through short-term contracts for more than 300 000 workers a year, admits openly that in the coming years it will need the immigrant labour due to demographic and economic reasons. To that end in 2002 it adopted the new law which provides a system of selection through points. This system favours the EU accession candidate countries' citizens, as well as the settlement of highly qualified persons (allowing them to obtain a 'green card').

France, which has long been practicing 'recruitment' and which periodically performs the regularization of illegal immigration, also takes into account the need for the qualified, 'useful' labour and tries to facilitate the entry of foreign students into the labour market. As for Great Britain, a system of selection based on points has been introduced there as well, which was already in place for the Hong Kong immigrants⁴. The new immigration countries from southern Europe have resorted to regularization on several occasions to absorb their illegal migrants. They adopted the legislation to enhance the selectivity of migrations and direct them to the regions where the demand for labour is especially high⁵.

Free movement of labour between countries within a region is a good way to improve labour market efficiency and promote greater labour supply and demand. In this respect, free flow of labour can be seen as good practice for labour migration and integration policy. However, it should be noted that mobility between EU countries and the region remains low⁶.

³ M. Tandonnet, 'Quelle régulation des migrations au niveau international?', *Cahiers français*, mars-avril, 2002, p. 87-92.

⁴ A. Favel, P. Hansen, 'Markets Against Politics: Migration, EU Enlargement and the Idea of Europe', *Journal of Ethnic and Migration Studies*, vol. 28, no. 4, 2002, p. 581-601.

⁵ J. Cavounidis, 'Migration in Southern Europe and the Case of Greece', *International Migration*, vol. 40, no. 1, 2002, p. 45-70.

⁶ Only 0.1% of the population changed their place of residence moving to another EU country in 2001. European countries were less optimistic regarding the mobility of the population from new member states, from Central and Eastern Europe, for fear of the rush of cheap labour and consequently, the transfer of domestic workers. See more on this in: C. Boswell, *Migration in Europe*, A paper prepared for the Policy Analysis and research programme of the global commission on international Migration, Hamburg Institute of International Economics, September, 2005, p. 22.

In 2004 the European Union faced the biggest enlargement in its history, i.e. the shift of its borders to the east, exactly to the point where these limits are not 'solid' enough. The old EU members were fearful of the consequences that the expansion could have on immigration flows coming from the Central and Eastern European countries, or passing through them, according to the principle of free movement⁷. Thus the free movement of the citizens of the new member countries within the Schengen zone was not only delayed, but the issue of the external borders control of was set as a condition: "There will be no common mode of movement if the candidate countries are not able to protect the external borders of the Union"⁸.

The Amsterdam Treaty, exactly the one that puts the immigration policy within the jurisdiction of the European Union, does not separate the immigration policy from the considerations of safety, on the contrary. The Schengen platform is included in that agreement (Schengen acquis) and the free movement was conditioned by the border control, prevention and fight against crime⁹.

Like other developed regions, the EU has a much higher proportion of educated and skilled workforce than the rest of the world, considered as a whole. This further suggests that Europe should focus its immigration policy towards unskilled workforce. Still why is there a trend in the opposite direction? There is a noticeable trend among European governments toward ever more selective immigration policies. At his previous job, the position of the French Foreign Minister, Nicolas Sarkozy agreed that the selective immigration was the expression of the French sovereignty: "Our country has the right, like all great democracies in the world, to choose which foreigners will be allowed to settle in our territory"¹⁰.

Meanwhile, the European Commission in Brussels was busy constructing an element of the common immigration system that would function at the EU level, as a whole. In the so-called Hague Programme, the EU has sought to adopt a set of immigration policies by 2010 that would be consistent across the partici-

⁷ On this occasion the EU signed agreements with countries that will soon accede through which the citizens of these countries are excluded from free access to the labour market in the European Union over a period of up to seven years after accession.

⁸ J. Widgren, 'Les politiques de la prévention de la migration illégale et du trafic de migrants', *Hommes et migrations*, no. 1230, 2001, p. 20-21; M. Tandonnet, 'Quelle régulation des migrations au niveau international?', *Cahiers français*, mars-avril, 2002, p. 87-92.

⁹ D. Bigo, "Europe passoire et Europe forteresse: la sécurisation/ humanitarisation de l'immigration", in A. Rea: *Immigration et racisme en Europe* (Bruxelles: Complexe), 1998, p. 203-241; V. Mitsilegas, "The Implementation of the EU Acquis on Illegal Immigration by the Candidate Countries of Central and Eastern Europe: Challenges and Contradictions", *Journal of Ethnic and Migration Studies*, vol. 28, no. 4, 2002, p. 665-682.

¹⁰ Ibid.

pating countries¹¹. So far the process has stagnated due to the differences among the member states governments in terms of types of immigrants who they wish to select. The idea of the EU green card is similar to that largely discussed and debated in the U.S., but it has not been adopted yet.

Also, one can identify another important factor that influences the establishment of restrictive immigration policy perhaps even more in relation to income and education. This is a potential burden on the welfare state, the costs of which are borne by the taxpayers of middle and higher income. If fiscal concerns dominate in people's heads, that certainly helps resolving the apparent paradox: why the countries rich in qualified labour want to discourage unskilled immigration. This view is often confronted with the fundamental goal: immigration is good for the budget. The conducted studies are related to the fiscal impact of immigration usually show that immigrants contribute more in taxes during their life in the host country, than they participate in receiving social benefits¹². But the results are very different for different levels of education and qualifications. Highly educated immigrants are huge net contributors, while the low-educated are net recipients. As the system of welfare states in Europe is generous, low-skilled immigrants pose significantly higher cost than it would be the case in the countries with more flexible labour market and less generous welfare state.

3. The influence of economic cycles on the migration process flows - the current global financial crisis

International migration has always responded to and followed the decline in economic activity and the flow of economic cycles. While the long-term trends of migration have been conditioned by economic and demographic fundamental factors, such as the income gap between the host country and country of the migrant, the cost of moving, and the cumulative series of migration effects, short-term variations of the trend have been driven by the temporary conditions in the labour market in both countries. In the great European migration from the end of the 19th century, when immigration policies were less restrictive than today, migration flows were quite volatile – more volatile than economic conditions of the country that they came from and the country that received them.

International migration increases and decreases depending on the phase of economic cycle, including the attitude and policies toward immigrants. History teaches us that it is expected and natural for the global recession to increase

¹¹ C. Boswell, *Migration in Europe*, A paper prepared for the Policy Analysis and research programme of the global commission on international migration, Hamburg Institute of International Economics, September, 2005, p. 22.

¹² J. C. Dumont, G. Spielvogel, S. Widmaier, *International Migrants in Developed, Emerging and Developing Countries*, An extended profile, OECD Social, employment and migration working papers No.114; Directorate for employment, labour and social affairs, 2010.

anti-immigrant sentiment and the possibility of encouraging new obstacles to migration.

The current global economic crisis has focused public attention on the process of immigration. The shaken labour markets have started introducing more restrictions on potential competition from immigrant labour, while the 'inflated' fiscal deficits have increased concern about the additional burden to the welfare system. Will the immigration pressure increase or decrease during the global recession? Will there be more severe reactions of immigration policy? What can history teach us¹³?

The instability of financial markets and slowing economic growth have filled the front pages and have been top news in developed countries around the world. The International Monetary Fund has predicted that developed economies will experience a decrease in economic activity by 0.3% - including a negative growth of 1.3% in the UK, 0.8% in Germany and 0.7% in the United States¹⁴. Meanwhile, governments around the world quickly prepare and bring some of the most extensive plans recorded in economic history to stimulate the economy.

As unemployment rates rise and household budgets shrink, policymakers, analysts and the public are beginning to wonder what consequences will immigrants themselves suffer and how this will affect the future course of the process of immigration. On no account should the implications of the global financial recession be underestimated. Immigrants make up a significant portion of the labour market; about every tenth resident in France, the Netherlands and the UK is of foreign origin, i.e. was born overseas; that number increases in Ireland and Spain – every eighth citizens is of foreign origin.

Given that a large part of immigrants are low-skilled labour, they are typically affected most during the recession, and because some immigrants (those not included in official statistics) are not eligible to receive various social benefits, they face difficulties and problems during the crisis. This may hinder their potentials in terms of social and economic integration.

Immigration still remains a hot political issue in Europe. Public expectations regarding the impact of immigration seem to become more acute during the period of economic crisis, particularly the concerns about the fact that immigrants take jobs from native (local) workers and burden the welfare state system

¹³ Decisions regarding migration are strongly associated with economic opportunities. *Economic migrants* move to the host country because they want to improve their personal capabilities (and of their families) and the chance 'to climb into the higher social strata'. Therefore, there are strong reasons to believe that the conditions prevailing in the labour market of the host country can influence the flow of immigrants. – Cited according to: J. C. Dumont, G. Spielvogel, S. Widmaier, *International Migrants in developed, emerging and developing countries*, An extended profile, OECD Social, employment and migration working papers No. 114, Directorate for employment, labour and social affairs, 2010.

¹⁴ D. Papademetriou, M. Sumption, W. Somerville, *Migration and the Economics Downturn*, What to expect in the European Union, Migration Policy Institute, January 2009.

at a time when public budgets are under pressure from public expenditure cuts. Whether or not this fear is justified, the economic downturn has the potential to create anti-migrational feeling which can be harmful to the further cohesion of the community.

The consequences that will affect the process of immigration and the immigrants will depend partly on the nature of the economic recession – a longer lasting and more severe economic downturn will produce sharper and more permanent implications.

What affects the influx of immigrants during the recession? Different types of immigrants have different reasons for migrating and face different barriers in the process. These factors influence the probability that the economic recession in the countries receiving immigrants will affect and shape the flow of migrants¹⁵.

- Is migration labour-oriented, connected with the workplace? For some immigrants, the decision to immigrate is purely economic. For others, the personal, social or political factors are more important and therefore the conditions that exist in the labour market will be less relevant (although they still have a role).
- Is there still a 'differential opportunity'? It is expected that economic migrants should move if they perceive that their chances in the host country are much better than those at home. If the employment rate and the amount of earnings decline in the home country at the same pace as in the host country, the recession will not lower the motivation for migration, having in mind that there is no necessity.
- How long is the administrative delay in the process of visa issuing? Long process of visa issuing could reduce the extent to which the number of applications reflects the current economic conditions.
- Does a visa require a job offer, or a work place offer? Even for a visa with limited administrative delay or in case of overbooking, the natural decline in the inflow of immigrants would be expected for a visa related to a job offer, because it is harder to get such deals during the period of recession.

What affects the drain of immigrants? Drain, i.e. departure of immigrants is inspired by similar motivational and institutional considerations. Many factors influence the inclination of immigrants to leave the country during the period of recession¹⁶.

- How strong and effective is the labour market in the original home country? Migrants are hard and reluctant to return home, unless they believe that their chances are much better there.

¹⁵ Ibid.

¹⁶ J. Duran, 'Economic downturn impacts most on migrant workers', Eurofound, October, 16, 2008, <http://www.eurofound.europa.eu/ewco/2008/09/ES08090791.htm>

- Is the migration intended to be temporary or permanent? While the line between temporary and permanent migration is unclear and blurred, the migrants' intentions are very important for any decision to return home during the recession. Immigrants who intend to immigrate permanently are harder to decide to return to their home countries; those who were planning a temporary stay on the other hand, may decide to shorten their stay.
- How strong are the social and family ties in the host country? Strong family ties in the host country will discourage 'return' migration.
- How much time has elapsed since immigration? The combination of the first two issues means that a longer stay is mostly usually associated with a lower rate of return migration during the period of economic recession.
- How expensive is the return home¹⁷? Circular migration is the most common for immigrants from the geographically closest countries.
- Will every individual be able to return once the economic recession is over? An immigrant who is unable to return to the host country will certainly think twice before leaving that country. This will depend on the status of the immigrants themselves and the rules of immigration policies of host countries.
- Is the immigrant qualified (eligible) for a variety of social benefits? Many immigrants do not qualify for social benefits (depending on their immigration status and specific rules of the host country) - Workers who are not eligible to receive benefits can not find employment.

4. The effects of the global financial crisis on economic migration in the EU

Economic and social conditions affect the demographic trends sooner or later. Migration as a component of demographics is vulnerable to the changing economic and social conditions, both in the countries that migrants leave, as well as the countries which they come to. Previous economic recession has provided evidence that the emigration of local residents and foreigners increases when the economic and social conditions in the host country deteriorate¹⁸.

In most European countries, unemployment is typically higher among immigrants in periods of normal economic activity and economic growth, and

¹⁷ J. P. Casarino, *Patterns of Circular Migration in the Euro-Mediterranean Area: Implications for policy-making*, CARIM Analytic and Synthetic Notes 2008/29, Circular Migration Series, European University Institute, Florence, 2008.

¹⁸ Data for EU-27 countries with the highest rates of emigration show that the volume of emigration from Germany began to grow in 2007 and 2008 and stabilized in 2009. Although the volume of immigration in Germany in 2008 and 2009 was among the highest in the Member States, the number of emigrants was higher than the number of immigrants, resulting in negative net migration.

this problem is even more pronounced when the economy falls into recession phase. The following table shows unemployment rates of the local population as well as those of foreign nationality in the first quarter of 2007-Q1 (as accurately as possible) in the first quarter of 2009, for the countries where data was available. On the basis of this data five groups of countries can be identified depending on how the unemployment developed in the domestic population and foreign nationalities in the past four years¹⁹.

Table 1: Unemployment rates of population of domestic and foreign nationality

	2007 Q1		2009 Q1	
	Population of domestic nationality	Population of foreign nationalities	Population of domestic nationality	Population of foreign nationalities
Austria	3,9	10,8	3,9	10,7
Belgium	7,1	16,6	7,2	15,3
Cyprus	4,7	5,5	4,0	7,5
The Czech Republic	6,0	5,7	5,8	5,5
Germany	8,6	17,3	7,2	15,4
Denmark	4,2	9,1	4,9	10,6
Estonia	4,4	10,0	10,1	17,4
Spain	7,8	12,6	16,0	28,0
Finland	7,4	20,2	7,5	15,8
France	8,2	17,2	8,4	18,5
Greece	9,1	9,3	9,2	10,7
Italy	6,2	9,7	7,7	10,5
Luxembourg	3,7	5,4	2,9	8,1
The Netherlands	3,7	7,8	3,0	5,9
Portugal	8,2	12,9	8,5	17,2
Sweden	6,5	13,1	7,5	15,4
Great Britain	5,2	8,5	7,0	7,7

Source: Eurostat: *Labour force survey 2009*.

- 1) Stable, i.e. unchangeable unemployment rate both in domestic and foreign nationality population (+/- 1.5% up or down); Austria, Belgium, Czech Republic, Denmark, France, Greece, Italy and Switzerland.
- 2) Constant unemployment among the domestic population, declining unemployment rate in the foreign nationality population (more than 1.5% decrease of the unemployment rate), Germany, Finland, The Netherlands.

¹⁹ Source: Eurostat, Labour Force Survey, 2007 Q2, 2008, Q2, 2009 Q2.

- 3) The increase in unemployment among the population of foreign nationality (more than 1.5% increase in unemployment), unchangeable rate of unemployment among local population, Cyprus, Luxembourg, Norway, Portugal, Sweden.
- 4) The increase in unemployment of the local population, unchanged unemployment rate in the foreign nationality population; Great Britain.
- 5) The increase in the unemployment rate both in the local citizens and the citizens of foreign nationalities, Estonia, Spain.

Within the European Union Spain stands out concerning the severity and consequences of the crisis; Spain has attracted an unprecedented number of migrants in the previous decade in order to stimulate the economic boom based on the construction sector and services. But since the global crisis has hit these sectors migrants have been most affected (although not even born Spaniards have been much better off). The unemployment rate among the Spaniards rose from 8.5% in Q4 of 2005 to 17.4% in Q1 of 2009, and from 10.2% to 28.4% during the same period with those who are of foreign nationalities²⁰. Spain recorded the highest unemployment rate in the EU starting even from July 2008, and half of the job losses in the EU during the first six months since the outbreak of financial crisis have occurred in Spain - 8600 jobs per day on average. Different EU countries have entered into recession at different times - most in the second half of 2008, while other countries, like Denmark, have entered into a recession even earlier, in June 2008²¹.

In addition to Spain, Ireland was probably most severely hit by the global recession in the European Union. Like Spain, Ireland has attracted a record number of immigrants for the past few years in order to stimulate economic growth. Although Ireland does not publish unemployment rates for the foreign origin population, how big the human impact of the crisis on immigrants is can be found out on the basis of the registry of the Central Bureau of Statistics (Live register - Administrative Budget of people who have registered for assistance, unemployment compensation, benefits and other rights guaranteed by the statute).

The economic recession that hit the world economy was turned into a 'crisis of working positions (jobs)' for migrants in mid 2008. As a result, after many years of continuous growth, the decline in labour migration has become obvious since the second half of 2008, virtually in all EU countries, due to a significant drop in international recruitment by employers²². Since the economic crisis hit

²⁰ Source: The data for the first quarter of 2009, Instituto Nacional de Estadística, Encuesta de Población Activa – the data were published by The Institute for Migration Policy.

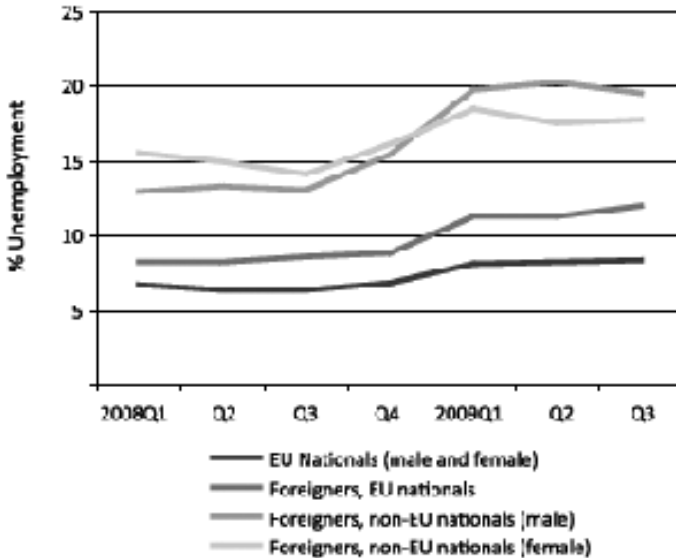
²¹ M. Pajares, *Inmigración y mercado de trabajo: Informe 2009*, Ministerio de Trabajo e Inmigración, Madrid, 2009, http://extranjeros.mtas.es/es/ObservatorioPermanenteInmigracion/Publicaciones/contenido_0002.html

²² OECD: *International migration Outlook*, SOPEMI, 2010.

particular manufacturing sectors such as industry, construction and retail trade, it had a strong influence on specific categories of workers, including the young, low-qualified, and men more than women.

Data based on reports of the European workforce reveals that, while the unemployment rate increased in workers who were of European nationality who worked in the EU but were originally from another country, the largest increase in unemployment and loss of jobs was experienced by migrants originating from countries outside the EU. The average unemployment rate of workers of the EU nationality increased by 2.5-3% in the period from early 2008 until the third quarter of 2009, while the unemployment rate for men and women who were of the nationality of some of the third countries rose by about 8% for men (from 13.5 to 20.2% for men), or 3.5% (from 15.1 to 18.6% for women) respectively. It is presented in the following chart.

Graph 1: Unemployment rates in the EU27 in 2008/09



Source: Eurostat: *Labour force survey*, 2009.

Generally speaking, migrants have been hit harder by the economic crisis than the national labour force. According to the report of International Organization for Migration, the unemployment rates of migrants (they were higher than those of domestic labour even before the crisis) rose faster in 2009, reaching between 9.4 and 10.75% in Austria, Greece and Italy, and 27.5% in Spain (which is an increase of more than 16% compared to 2007). According to the same report, while the employees of Irish nationality made an overwhelming majority who received compensation in the event of unemployment, the number

of foreigners who received a comparable compensation in Ireland rose to 77.500 in December 2009, whereby more than half of them belonged to the nationalities of some of the new member countries. This makes an increase of 173% from June 2008 until the end of 2009²³.

The unemployment of immigrants from the new EU-10 member states many of whom were employed in the construction sector increased from 2.3% in February 2008 to 8.2% in the same month of the next year, 2009, compared with an average rate of unemployment, which rose from 3.3% to 6.6%. The economic crisis had an impact, albeit of a limited scope, on the migration to the EU-10 countries, as well as the countries to join the EU. In 2009 the Czech Government has adopted and initiated two special voluntary return programs for legal and illegal migrants, and they were terminated in December 2009²⁴.

The overall rate of unemployment in the EU-27 reached 9.6% in 2010. Compared with the rate of unemployment in 2009, it grew by 0.6%. This is still a lower growth than the one that occurred from 2008 to 2009, due to the economic crisis, when the rate rose by 1.9%. The impact of economic crisis on unemployment in the period between 2008 and 2010 has now completely nullified the reduction of unemployment rate experienced by the EU between the 2004 and 2008²⁵.

The unemployment rate rose in all member states between the 2009 and 2010 except in Germany, Luxembourg, Austria and Malta. The largest decrease in unemployment was recorded in Germany, where the unemployment rate fell by 0.7%. Belgium, France, Romania, Finland, Sweden and the UK also had a good performance, showing only a moderate increase (less than 0.5%) between the 2009 and 2010. While Estonia and Lithuania were among the countries with the highest growth, they saw a drop in unemployment in the second half of 2010. A large increase in unemployment was recorded also in Greece, Spain and Slovenia²⁶.

Long-term unemployment is one of the major problems and causes the most concern for economic policy makers. Regardless of its financial and social effects on personal life, long-term unemployment has negative impact on social cohesion and in particular may limit and slow down the economic growth. In total, 3.8% of the workforce in the EU-27 in 2010 was unemployed for more than a year; almost half of them, 1.8% of the workforce, were unemployed for more than two years²⁷.

²³ Ibid.

²⁴ Source: Eurostat: *Demography report, 2010*, Migrants across generations, 2011, p. 43-45.

²⁵ J. Duran, "Economic Downturn Impacts Most on Migrant Workers", *Eurofound*, October, 16, 2008, <http://www.eurofound.europa.eu/ewco/2008/09/ES08090791.htm>.

²⁶ Spain has remained to be a country with the highest unemployment rate in 2010; it was 20,1 %. The unemployment dispersion across EU-27 continued during 2010. Source: Eurostat: *Demography report, 2010*, Migrants across generations, 2011, p. 43-45.

²⁷ The unemployment rates for men were higher than the corresponding ones for women in 14 out of the 27 member states. The Eurozone the unemployment rate for women remained higher than the unemployment rate for men. The gap between unemployment

Among the EU member states there is strong competition in attracting and retaining highly skilled labour, but at the same time there is also a deficiency or lack of lower skilled jobs in the labour market. The need for labour for low-skilled jobs can partially be met through the migration process. Managing low-skilled labour migration is one of the key challenges facing the EU. The main task concerns the long-term employment of low skilled labour migration and their integration in host countries. The temporary immigrants' employment programs have already been implemented in many countries. The growing importance of temporary migration has generated an increased and renewed interest in the return immigration and its impact on the development of the countries from which it comes.

5. The impact of economic immigrants on the labour market in the host country during the recession

The impact of immigrants on the labour market - Political debates about immigration process in the most developed countries place an emphasis on how immigrants affect the labour market. There is no evidence convincing enough to confirm the fact that immigrants reduce wages or take jobs from the local labour²⁸, although much of the public has such an opinion. Experience shows that in the periods of high unemployment rates public and economic power become more concerned about the potentially negative effects of immigration on local population opportunities. As it has already been said, the increase in unemployment in Spain led to the creation of a program in late 2008 which pays immigrants to return home. Increasing tensions and concerns in particular in the countries where conflicts related to immigration arise, have already become evident. For example, in September 2008 The Statistics Agency of the Republic of Italy publicly blamed the immigrants for rising unemployment in the country²⁹.

Intuitively, one might expect the impact of immigration on local population to increase during recessions, given that the increase in unemployment creates a more fierce competition for jobs. At the same time, immigrants have a greater need to be employed in comparison with local people, if they are not eligible to receive social benefits and have no savings. This contributes to

rates for men and women varied from 6.3% in Greece to 7.2% in Ireland. The first time since statistical calculations of unemployment had been made in the EU-27 that the unemployment rate for women was lower than that for men was in 2009, and it remained unchanged for the next year.

²⁸ German Marshall Fund: *Perspectives on Trade and Poverty Reduction, A survey of Public Opinion*, Key Findings Report 2007, <http://www.gmfus.org/economics/tpsurvey/2007TPSurvey-Final.pdf>

²⁹ J. Thornhill, R. Atkins, G. Dinmore, 'Eurozone's economic chill leads to Jobless Rise in France and Italy', *Financial Times*, September 30, 2008.

the situation that the immigrants 'undermine' local employees more often by accepting low wages.

5.1. Counterarguments: cyclical immigration employment and return migration

On the other hand, two factors illustrate that immigrants compete less with local labour during the recession. First, immigrants have *stronger cyclical employment rate* than the national labour force, they quickly lose their jobs in a period of economic activity decline and quickly regain them in the period of economic growth³⁰. All this leads to the conclusion that immigrants have a potential to adapt to cycles that take place in the labour market (limited, of course, by their relatively small share of total market).

Second, *return migration* of low-skilled workers may have a counter-cyclical effect. This is particularly relevant in countries with a large influx of workers from Eastern Europe, who seem to respond to the recession most often by returning home. An adviser to the Polish Government recently put forward the fact that 400 000 Poles in Great Britain and Ireland are likely to lose their jobs during the current economic recession³¹ and that many will choose to return home to Poland.

Fiscal impact - Although immigrants lose jobs in large numbers during the period of recession (and therefore would be expected to burden the welfare state), inability, i.e. ineligibility to obtain social benefits and return migration can be counter-balance to financial costs in many EU member states. It is difficult, therefore, to predict exactly how the current fiscal impact of immigrants can be changed while the recession is still going on.

Integration into local communities - In the absence of solid evidence that immigrants 'undermine' national workers in the labour market, probably the biggest concerns are of social and political nature. In the light of growing economic instability, immigrants become 'scapegoats'. This poses a special problem in the countries that already face difficulties in the integration process, such as Italy, Germany, France and the Netherlands.

³⁰ C. Dustmann, A. Glitz, T. Vogel, *Employment, Wage structure and the economic cycle; Differences between Immigrants and natives in Germany and UK*, Discussion Paper Series, No. 06/09, Center for Research and Analysis of Migration, University College, London, 2006.

³¹ 'Polish Workers likely to leave Britain I Drove', *Sydney Morning Herald*, October, 24, 2008. <http://www.smh.com.au/news/world/polish-workers/likely-to-leave-britain-in-droves/2008/10/23/1224351449793.html>

6. Will the global financial crisis have long-lasting effects on migratory flows?

Reducing the number of immigrants seems quite certain when considered in the short term, especially for certain types of migration. Should it be expected that the speed of the process of immigration will continue in the long term future?

Given that a longer-term future is very uncertain, it seems that only severe and prolonged recession could have a substantial, long-lasting effect on migration flows. First, the scope and depth of economic downturn is associated with the inevitable economic restructuring (and with the job change, i.e. turnaround from declining to growing industries) and certain types of immigrants may not return. Second, a sharp recession (includes a wide range of unemployment of immigrants) may interrupt the chain of labour market information that allows immigrants to find new jobs, thus requiring a longer recovery period before immigrants can again obtain significant and useful information regarding the labour market³². Third, and related to what was previously said, during the current recession, jobs, or working positions lag behind and slow down economic recovery; many immigrants therefore remain for some time outside the labour market of the host country.

If the recession is moderate or even weak, on the other hand, many factors that affect immigrants' return home during its duration should be reversed over time, once economic conditions improve. The leading generators and reasons for migration in the long run will not significantly change after the economic recession. Factors such as continued demand in the labour market, demographic changes, considerations of international competitiveness, and a network of immigrant communities will provide the ongoing net immigration flows of varying but significant extent.

It is believed that business cycles have a larger and more significant impact on immigrants than on local citizens for several reasons³³:

1. Immigrants are disproportionately poorly educated and trained. A comparative analysis of countries, according to the proportion of immigrants and non-immigrants by educational level reveals two key facts. One is that (with the exception of Canada and Australia as well as the UK) the proportion of highly educated individuals among immigrants is roughly equal to that of the local population. The second is that, among immigrants in Europe, the proportion of low-educated individuals typically exceeds 40%, and many of them have very little education. The problem for European countries such as France, Germany, Denmark and the Netherlands, is not only to attract highly educated, but to discourage poorly educated and unskilled workers.

³² I. Awad, *The global economic crisis and migrant workers, impact and response*, International Labour organization ILO, International Organization for Migration, IOM, Geneva, 2009.

³³ Ibid.

Studies consistently show that less skilled workers often lose their jobs during the period of recession³⁴, when employers lay off workers with the lowest productivity and those that are easily replaced. Immigrants mostly represent the low-skilled labour in the EU countries that receive them³⁵. Language barriers also make them less productive compared to home employees, and therefore less needed, i.e. 'disposable'. One recent study, using data from the UK and Germany, confirms the thesis that the unemployment rates of immigrants are much more cyclical than those of domestic labour. In Germany, for example, the response of unemployment to macroeconomic shocks for immigrants with language training but no college education was twice bigger when compared to the national³⁶.

Recent experience in Spain has shown the following trends: 34% of immigrants in the Spanish labour market perform low-skilled jobs, compared with 11% of domestic labour. The sudden rise in unemployment in the labour market in Spain has severely hit especially the foreigners. Over the past few years, the unemployment rate of immigrants was, roughly speaking, 50% higher compared to that of Spanish workers³⁷.

Why is low-educated immigration a problem? First, one should analyze political and public opinion. A conventional opinion on low skilled immigrants is that they mostly come from poor and remote countries with different cultures - something that is superficially identified with religion and skin colour. The problem has been complicated in recent decades due to a sudden and large increase in asylum requests which usually come from poor countries; these people are often demonized as 'fraudulent, illegal refugees'. Due to a large number of asylum seekers (the exact proportion is not known) that enter a country illegally, it is considered that they disturb and disrupt a system that has previously been established to serve humanitarian purposes in order to 'jump the queue' in the labour markets in developed countries. It is not only the prejudices that determine official attitudes towards immigrants. Numerous studies that have been conducted in recent years suggest that those people of home population who are highly educated are less anti-immigration oriented. Based on the above, it can be

³⁴ S. Nightingale, M. Fix, D. Fix, "Economic and Labor Market Trends", *The Future of Children*, 14, no. 2, 2004, p. 49-59; D. Smith Nightingale et al., *The Employment Safety Net for Families in a Declining Economy, Policy Issues and Options*, Urban Institute, Washington DC, March 2001; H. Hoynes, "The Employment, earnings and income of less skilled workers over the business cycle", Discussion Paper no. 1199-99, Institute for Research on Poverty, University of California, Berkeley, October, 1999.

³⁵ Source: OECD, *International Migration Outlook 2008*, OECD SOPEMI, 2008.

³⁶ C. Dustmann, A. Glitz, T. Vogel, "Employment, Wage structure and the economic cycle: differences between immigrants and natives in Germany and UK", Discussion Paper Series, No. 06/09, 2006; Center for Research and Analysis of Migration, University College, London, 2006.

³⁷ J. Duran, "Economic Downturn Impacts Most on Migrant Workers", Eurofound, October, 16, 2008, <http://www.eurofound.europa.eu/ewco/2008/09/ES08090791.htm>.

concluded that those who face less competition from immigrants in the labour market, are less ready and willing to demand tougher immigration controls. It makes sense that the highly qualified, who are numerous in rich, developed countries (compared with the world as a whole), should favour the immigration of unskilled workers, for whom there is a relative need and who are insufficient in number in those countries.

2. Many immigrants are not eligible to receive various social benefits³⁸.

A large number of the newly arrived immigrants, as well as those unrecorded, are not eligible to receive most benefits. The immigrants who lose their jobs and are not entitled to receive benefits may have other options. For example, they can: a) rely on family members and other social contacts for financial support; b) rely on accumulated savings; c) accept any work for a very low pay, or d) return home. However, those who do not have sufficient and adequate family resources of support, or are unwilling or unable to return home, are exposed to particular risk and problems. In the worst case, if an immigrant does not have any savings or family support, no skills and training for self-employment and does not want to return home (for example, due to high costs, fear for their safety when they return or difficulties to come back later), faces a high risk of falling into poverty.

Although immigrants are typically more flexible than the national labour, more mobile³⁹ and more willing to change the economic sector in which they work, i.e. the type of job in order to remain employed, still they are those who lose most in the recession period. This has great implications for the integration process. First, many immigrants are aware that they can not afford to live without a job in the long run, and that makes them vulnerable and subject to exploitation by employers. Second, the evidence based on research shows that the level of immigrants' earnings catches up faster with the earnings of domestic workers in a period of expansion, and more slowly in the period of recession, suggesting that rising unemployment prevents immigrants from joining specific human capital of the host country⁴⁰.

³⁸ Spain does not allow access to unemployment benefits and social protection for certain categories of migrants. For specific variations for each country see in: Oxford Analytica: *Labor Migration Policy Index - Phase II*, International Migration organization, Oxford Analytica, Oxford, 2008.

³⁹ W. Somerville, *Immigration under new labor*, The Policy Press, Bristol, 2007.

⁴⁰ B. Bratsberg, E. Barth, O. Raaum, "Local Unemployment and the Relative wages of immigrants: Evidence from the Current Population Surveys", *The Review of Economics and Statistics*, 88(2), 2006, p. 243-263.

7. Conclusion

It is expected that immigrants will respond differently to the current economic situation, depending on which category they belong to. If immigration is connected with employment, i.e. finding a job, the crisis will produce a large number of returns to economic sectors that were most severely hit. At the same time, if conditions have worsened in the host country and become the same or similar to those in the home country, many immigrants will rather opt to return home and reunite with their families in the absence of financial resources and benefits. Family reunion will affect the decision of a permanent stay only if economic conditions in the host country become critical. Generally speaking, immigrants will go or stay, depending on family relationships, job security and the strength of social and cultural connection with the host country.

It seems that the economic reasons for migration of labour will become increasingly urgent in the coming decades for at least three reasons. First, European governments increasingly recognize and acknowledge the importance of different skills in generating productivity and economic growth. *Human capital* has become a key determinant of productivity increase and growth of knowledge-based economies. Highly educated and skilled workers are vital in ensuring innovation and productivity increase and, consequently, creating new businesses and jobs. This has contributed to the fact that some European governments are willing to facilitate and reduce the rules related to labour migration. On the other hand, there is a serious concern in many countries about whether Europe is sufficiently attractive for skilled workers, compared with North America.

Second, despite substantial structural unemployment in many European countries, European workers are often selective in the job choice, as well as the job location; they are also much more qualified than they were ten years ago. Although the proportion of low and semi-skilled workers is increasingly smaller (due to the production of new technologies and sources), there is a substantial gap in a number of these jobs - especially in agricultural and food industry and domestic services. There is also an acute shortage in many public sector jobs, because of inadequate salaries and low status. All this creates significant gaps in jobs such as health care and education - gaps that are filled largely by migrants.

Third, the aging population implies an increased rate of dependence in European countries, i.e. a higher proportion of economically inactive population compared to the active one. It will burden the welfare state systems as health care and pensions become more expensive. The aging of population also generates changes in terms of consumption, particularly in the increased demand for health care and leisure activities, which in turn will create additional demand for labour in these sectors.

If the rate of migration maintains at the current levels, active working population of the EU countries will increase by 1.9% between the 2010 and 2020

compared with growth of 8.6% in the previous period (2000-2010). Immigrants represent one third of the 'new' labour force, although the arrival of children and the elderly reduce their contribution.

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DANIELA MARAVIĆ, M.A.*

Intertravel, Subotica

ASSISTANT PROFESSOR NATAŠA MILENKOVIĆ, PhD

Graduate School of International Economy, Megatrend University, Belgrade

INTEREST-FREE BANKING AND ECONOMIC DEVELOPMENT**

Summary

The paper "Interest-free banking and economic development" examines the concept of Islamic banking and its specificity compared to conventional commercial banking. The causes of renewal of interest in the moral aspects of the economy, the theoretical basis of Islamic banking principles and the basis and mechanisms of operation of Islamic banks, as well as sources of capital of these institutions are analyzed in this paper. Significant place in the paper takes analysis of problems faced by modern Islamic banks, as well as opportunities to overcome them.

Key words: *Islamic banking, interest-free banking, commercial banks, the prohibition of interest*

JEL classification: G21, P42

1. Introduction

The way conventional commercial banks function nowadays is so widely accepted in most of the world that, although clients are more and more dissatisfied and the rating of banks ever more downgraded, rarely anyone wonders if banking business could possibly be organized in a different manner.

It is a general opinion, well-founded in every day practice, that the most important aim to be reached by banks is to maximize income against citizens and economy. Citizens are aware that banks, using interest rates, with one single signature, earn just as much as those taking loans and work for a decade or two in order to pay them off. It is clear that huge interest rates put off potential entrepreneurs from starting a new business, and owners of already active companies from their development.

* E-mail: daniela.lipovac@yahoo.com

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The problem becomes even bigger if banks in question are those with majority foreign capital (as the case is in Serbia). Experience of many countries with well-known world banks being “guests” is that they do not finance development, especially if production and export are concerned, while being completely disinterested in opening new work places, which is only natural. One thing foreign banks gladly grant credit for (on high interest rates of course) is citizens loans. Additional problem is that their huge profits are not even spent on the host country market, but are drained abroad.

Regardless of the above, rarely do we hear criticism concerning very principles residing banking business we are familiar with. General opinion is probably adopted that banks subsist on interest, without which they would cease to exist, and population and economy in that case would be forced to purchase only those goods they can afford with cash. The exact aim of this paper is to point out the delusion that we are sentenced to infinite exhaustion by “usurious” business of banks.

It is scarcely known that this is not the only way of banking operation. Incompliance with principles which are the basis of banking system in other environments already led to creation of alternative systems making slow but sure way to European territory. Majority of people nowadays probably cannot realize the fact that there are banks that endure based on principles different from banking system we are familiar with (for instance, interest ban principle), having entire boards to estimate *ethicality* (!) of certain financial transactions. It is the concept of *Islamic banking*.

Since Islam forbids interest, these banks are intended to develop and improve other sources of financing, having developed a whole new type of banking operation. Charging interest is forbidden for centuries, but efforts to institutionalize this principle have only recently been restored. Islamic banks exist in many Muslim countries and only several of them in non-Muslim countries, but the degree of their success and support given by religious and public authorities varies from one country to another.

Although Islamic banking is still a young concept, there are presumptions that the number of clients in these banks increases by 27 % annually. Dissatisfaction with the existing banking system and the expansion of such new concept itself emphasizes the need for this phenomenon to be studied further.

2. Need for Moral Restitution in Economy

It is well enough that people of the nation do not understand our banking and monetary system, for if they did, I believe there would be a revolution before tomorrow morning.

Henry Ford

In many philosophic, ideological and religious studies, theories and views, interest is considered unacceptable way of acquiring money. Even Plato and

Aristotle treated interest as “unnatural” way of beneficitation. In Judaism, Christianity and Islam, business with interest is considered a sin, because one makes earnings without work, that is, without making an effort, and no god may be satisfied with that. Torah says: “If you give the money to a poor man of my people your neighbor; do not act as a usurer and take no more than you give.” (...) It should be added though that Jews operate without interest between themselves, while using interest in business with other nations. Also, the Gospel of Luke cites: “Lend, hoping for nothing in return, and your reward shall be great”.

Noteworthy doctrines of modern economic thought, to begin with A. Smith and D. Ricardo, are based on fundamentals of *labor theory of value*, according to which only work represents the determinant of goods value. Marxist views on value and surplus value generated by labor should not be forgotten.

In Islamic world interest ban has been conducted more strictly than in other parts of the world. The Quran forbids usury or interest on lent amounts (*riba*). This is interpreted in the way that money may be used as means of exchange, but cannot be treated as goods or product. However, Islamic banking is not a rule even in Islamic world. Western system with interests and loans is predominantly in force over there also. Although a large number of Muslims have restrained themselves from depositing money into banks for religious reasons, various legal instruments have always been used in order to circumvent the interest ban. Even Ottoman banks charged and paid interest. In modern times, in many Muslim countries there was no need for such measures, but the ban was most often ignored. Having in mind that money as goods is inseparably linked to modern economy, general practice in modern times is to accept demands of economic necessity and cast aside the question of interest.

Nowadays, however, the attention rises for moral values in economy. The renewal has begun in Islamic world, already a leader in this respect, but producing unimposing and sporadic dissatisfaction and criticism shown in papers of non-Islamic, European theoreticians of contemporary banking concept, probably being a consequence of growing injustice both in international and internal economic relations.

We know for a fact that overall social wealth is ever more unequally distributed in the world; hence a very small number of people dispose of great fortune, while on the other hand there are millions of poor people. To be more accurate, according to World Bank, 1% of the richest world population makes larger income than 57% of the poorest population (World Bank, 2008). One of the reasons is the way of financing economic development in the third world countries, based on financing from outsource, although debt slavery in the past years has been transferred to Southeast European countries. Foreign loans represent a mode of help to developing economies, but on the other hand, simultaneously generate the problem of servicing debts created thereby. In vicious debt circle, interests paid surpass by far the amount borrowed, and there is no prin-

cial reduction (*Web of Debt*). Many countries take new loans every year just to pay interests for previous loans. On average, third world countries pay debt with interest every year being approximately 30 billion American dollars higher than the previous year.¹ Situation in European countries is somewhat better, but still extremely large drainage of money is involved. Serbia, for instance, should spare 2.9 billion this year for interests on outside debt only.

Equally unjust and avarice behavior banks express internally as well – towards economy and citizens creditors. It is commonly known that in long-term borrowing, with usual interest rate, debtor pays interest to bank in the amount of loan taken. For instance, in case of mortgage loans, citizens pay off the loan with interests in value of two apartments – one for themselves, and the other for the bank. New and extreme example, consequence of such financial business, is recent world financial crisis that actually began with American real-estate market crash, due to citizens' inability and failure to pay off loans overloaded by interests (although this is not the only cause of crisis). Very high interest rates are usual in European and North American states when citizen loan is in question, but considering economy financing, conditions are far more favorable than in our country.

According to data issued by the National Bank of Serbia, Serbia holds record in the region regarding the height of interest rates (real). Real interest rates are on average 14–19 % depending on the sort of loan. As quoted in the introduction, it is not of these banks' interest to motivate development of Serbian economy, thus financing entrepreneurs includes multiple interest rates compared to financing natural persons. Effective interest rates for short-term loans to entrepreneurs bonded by Euro reach 25% annually, and on RSD loans 30–35%. Investment loans mean interest rate over 22%. However, interest rate on loan with same duration for citizens, for car purchase for instance, amounts to 20%. Long-term (mortgage) loans for citizens have interest rates of approximately 5%, while long-term loan for buying office space have rates of over 10%. Let us add that citizen account overdraft debt is the most expensive mode of financing in Serbia, since effective interest rate ranges up to 40% annually. If banks take interest of 35 and 40%, the question is: why is usury forbidden?

Such high interest rate on loans to companies is one of the most important causes of lacking investment in economy, hence its inability to develop.

Banks, however, make remarkable profits. Once again, on the example of Serbia, in the first 6 months in 2008, banks made profit over 210 million of Euro. In course of 2007 profit made by banks in Serbia was approximately 300 million Euros. Overall assets of certain banks rise over 30% a year.

This and alike injustice in economic relations led to attempt to renew moral principles of economy first of all in Middle East countries and then in other Islamic countries.

¹ H. Sadek, *Finansiranje ekonomskog razvoja*, El-Kalem, Sarajevo, 1996, p. 55.

Adjective *Islamic* as determinant of a new and relatively different concept of economy is not of special significance for this study. It aims merely to remind creators of economic policy of one Muslim country of moral values entwined in their religion which is crucially important to these societies. Furthermore, those moral principles are not exclusively Islamic in any aspect. It is about common need for establishing humane economic relations and ethical principles in global economic flows... Therefore hereinafter, whenever possible, expression *interest-free banking* is used instead of *Islamic* in order not to leave the impression of the concept as something that "is of no concern to us"...

Islamic economy has several specific fundamental principles, but the concept of interest free banking is the one least comprehensible to a man from the Western world. The text further explains theoretical basis of interest-free banking, development and recent expansion of these banks, methods of their operation and sources of their financing. As already mentioned, religious connotation itself is irrelevant.

Analysis of this concept aims to imply some new potential of development, but firstly to illuminate special needs of fragile economy and society in transition such as those in Serbia. These are needs for additional support and protective stand towards the exhausted economy and population, especially in periods of crisis, which seem to be linking to each other in this country.

3. Theoretical Basis of Interest-Free Banking

Islamic banking is a part of wider concept of Islamic economy. For its ethical foundations, many Muslims consider it more than a system of commercial transactions. Unlike conventional economic system focused primarily on financial transaction profit, Islamic economy strives to express equally ethical, moral, social and religious dimension of relevant society. Islamic economy (if it existed in pure form) should, performing usual economic activities, always bear in mind benefit of the society as a whole, as well as help establish equality between people. The idea that Islamic banks are charity institutions operating without profit is to be cast off immediately. These banks make more profit by the year, have ever more clients, and financing sources apart from interest, do not significantly differ from classical commercial banks, which shall later be elaborated.

Islamic banking founds its principles on Quran that justifies only that fortune gained as a result of one's own work or entrepreneurship, as well as inheritance and gifts. Exchange of non-equivalent amounts of money is not allowed, as the case may be with loan transactions (interest). Contemporary Islamic economic thought, regardless if based on Sunni or Shia fundament and regardless certain differences in other spheres of religious life, is unanimous regarding interest. To agree upon beforehand fixed amount of interest return, means in

fact, to predict future events in time and space, which in Islam is strictly forbidden. Islam is clearly against all forms of conventional or “concealed” interest as profit foreseen in advance, even if interest rate is lower than 1% a year.

Abolition of interest is basic issue in contemporary discussions on Islamic financing and Islamic economy. According to Prof. Fikret Hadžić (2010) “Great part of merit for the development of contemporary Islamic financing system refers to theoreticians of Islamic economy. They have developed a special theoretical approach which helped implement the whole concept in practice.”

Until now there have been several trials of “reexamining” interest by Muslims who accept Islamic doctrine and wish to abide Islamic principles. Topics of discussions were as follows: what does interest ban stand for, is there a difference between interest and usury, is every form of interest forbidden etc. Debate on these questions is ended in modern Islamic literature, terms *riba* (interest) and *interest* are treated as synonyms, and interest ban continues to be considered as ban of any sort of interest.

Leading Islamic theoretician Abu Hamed al-Ghazali, in his famous work “Ihya’ul ulum al-din”, he points out that interest prevents the money from performing its function that the money should serve as measure of value and means of exchange, while function of the money as “means of fortune hoarding” is an unwelcome function of the money.² He believes that the money itself has no value; it enables goods exchange, and without that feature it would not have any role in man’s life. Money in Islamic finance is not goods, and may not be lent as such nor appear in exchange as a value, considering it is the measure of all other values. Should it be treated, though, as all other goods, it would be deterred from the use initially intended. In these facts he saw the basic reason to ban the interest.

Views of other Muslim theoreticians are similar, that is identical to Ghazali’s opinion on the issue of interest. They emphasize that no one should be privileged nor rewarded for the mere act of renouncing spending; that money is not the same as capital; that in practice interest is paid on money (not on capital) and Islam forbids that.

Distinct characteristic of modern Islamic banking institutions is the role of Sharia supervisory board being integral part of Islamic bank. It supervises operations of Islamic bank and has a task to prevent any transaction suspicious from Sharia point of view. These boards involve some of the most important contemporary Sharia theoreticians, and opinions of these boards are expressed in form of Fatwa. Moreover, International Association of Islamic Banks, an independent entity, supervises work of individual supervisory boards, while their Supreme religious authority reviews fatwas of supervisory boards of member banks to determine their compliance with Sharia.

² J. Halebić, *O kamati*, Naučnoistraživački institut “Ibn Sina”, no. 12, Sarajevo, 2001.

4. Expansion of Islamic Banking

Although Islamic banking is relatively new phenomenon, practice and principles, basis of Islamic bank, were commonly accepted worldwide centuries ago. For many the custom of keeping family money in form of women's jewelry made of silver and gold was traditional saving system.

It is obvious that Islam allows financial activities practiced back in middle ages (from Spain to Mediterranean and all the way to India), and that Muslim merchants were regular mediators in numerous commercial transactions and that many concepts, techniques and instruments of "Islamic finance" were later on accepted by European financier and businessmen. Still, organizations established as an alternative to conventional banks and financing institutions in their result are relatively new phenomenon (if we neglect the fact that in all Muslim world there have always been loan associations within humanitarian organizations lending money on interest-free basis). Its expansion is "...initiated in the period after the World War II, and accelerated since '70s of the 20th century",³ clearly indicating that realistic mainstay of this concept lays in strengthened petrodollar economies of that time. In this period Islamic economies were impartially in the position to express resistance to domination of western economic thought and so they did in materialization of Sharia provisos in banking reality.

Effort made by an economist Ahmad El Najjar resulted in opening of the first Islamic bank in Egypt, in 1963. The first Islamic bank – *Mit Ghamr Saving Bank* had the character of savings bank based on profit sharing. The bank in its operations did not charge interest, but rather invested in commerce and industry, directly or in partnership with others, and shared profit with its depositors. Therefore, it functioned as savings bank and investing institution, and not as a commercial bank. However, in 1967 it abandoned the experiment of interest-free business model and turned to conventional bank, mostly because of predominant politicized climate present in that period.

Another Islamic bank was also established in Egypt in 1972, *Nasser Social Bank*, only this time supported by Egyptian government, which enabled its continued existence. In fact, it was government's bank with aims more of social than commercial character.

Supported by Saudi Arabian government, in 1975 IDB – Islamic Development Bank was founded as Islamic lending institution for economic development and trade improvement between Muslim countries. Its headquarters are situated in Jeddah (Saudi Arabia). Bank's capital is estimated on the amount of 10 billion Islamic dinars. In that same year the first private Islamic bank was established – *Dubai Islamic Bank*. *Kuwait Finance House* was instituted in 1977, and in the first few years, this bank's deposits doubled almost each year.

³ B. Antić, "Model islamskog bankarstva: specifikumi i razvojna ograničenost", *Časopis bankarstvo*, 7/8, 2008.

In Asian Pacific region, *Philippin Amanah Bank* (PAB) was founded in 1973 by presidential decree as a specialized banking institution. In Malaysia, 1963 *Muslim Pilgrims Savings Corporation* was established – a financial institution that helped savings for Hajj. Although it did not stand for a bank, its success gave stimulus for establishing *Bank Islam Malaysia Berhad* which denotes the first Islamic commercial bank in Malaysia.

Nowadays, in 51 world countries operate more than 300 Islamic banks and other financial institutions (World Database for Islamic Banking and Finance), although we can discuss even larger number if insurance organizations are included, as well as leasing organizations, accounting control services, consulting companies... In these countries, of course, there are conventional commercial banks, apart from Iran, Pakistan and Sudan with only Islamic banks, while national conventional banks do not exist. To be exact, “all national banks operate in compliance with provisions of Islamic banking, whilst foreign banks may choose between western and Islamic way”.⁴

The number of Islamic banks and institutions is rising very quickly; therefore we may already talk about real expansion. These banks jointly constitute Islamic financial market with the value of assets estimated to the amount of 250 to 300 billion American dollars with annual growth rate reaching 15%. Malaysia is the largest world market of Islamic bonds, responsible for two thirds of overall issued Islamic bonds in the world.⁵ In many Arabian countries, especially in the area of Persian Gulf, the market share of Islamic banks has reached 50 percent.

The biggest Islamic bank is *El Rajhi Banking & Investment Company* from Saudi Arabia, with capital of approximately 1 billion dollars. It has its branch offices in London and Luxembourg.

Nowadays, Islamic banking is already integrated in British and German legal system. It is applied in Netherlands, France, Denmark, Luxembourg, and Australia. *Raiffeisen Zentralbank*, as the first bank in Austria, also offers bank account opening in compliance with Islamic regulations. In our region, the first Islamic bank has recently been founded in Bosnia and Herzegovina.

5. Financial instruments of Islamic banks

Interest-free financing does not mean renouncing all accomplishments in the area of banking, management, marketing, accounting, finance, finance management etc. Islamic banking does not accept interest as certain and fixed income determined in advance, but rather strives to participate by means of its business activities in sharing of profit and loss. Islamic financial system aban-

⁴ A. Marković, “Islamsko bankarstvo: pobožna zarada”, *Biznis i finansije*, n. 40, 2008.

⁵ M. Čihak, H. Hesse, *Islamic Banks and Financial Stability: an Empirical Analysis*, International Monetary Fund, WP /08/16, 2008.

dons the concept according to which a borrower is obliged to repay the debt that is borrowed capital, regardless the outcome of the job. Instead, a lender undertakes the risk of the borrower's business and takes part in profit and loss of that job. Applying this method, the principle of Islamic financing may take the form of *Profit and Loss Sharing Principle*.

Risk factor is the central argument in Islamic financing. Implementation of these principles of Islamic financing to banking system leads to risk sharing between bank and capital user. This principle led to numerous inventions of Islamic banks regarding creative financial solutions. They use in their operation some (or all) of the following forms of financial instruments: Mudarabah, Musharakah, Murabahah, Ijarah, Istis'na, Mukaredah and Kard Hasan.

In order to explain the mechanisms, it is time to draw a parallel with conventional banking of western type with terms in English:

- Equity-Based Models:
- Joint Venture (Musharakah),
- Trustee Partnership (Mudaraba);- Debt-Based Models:
- Cost-Plus Sale (Murabahah),
- Deferred Delivery Sale (Salam),
- Manufacture-Sale (Istis'na),
- Leasing (Ijarah);
- Benevolent Loan (Kard Hasan).

Mudarabah stands for joint involvement of Islamic bank and its client in certain project. This is a form of business cooperation where in completion of a project the bank provides capital, and other party provides ideas, know-how and work. The bank appears merely in the role of financier without active participation in business administration, while the entrepreneur undertakes responsibility of conducting business. Both the bank and the entrepreneur are free in deliberating profit share proportion, and loss in financial sense is entirely born by the bank, that is financier.

According to Islamic principles, it is not right to determine a fixed sum of money to be paid to one party, but rather to express the proportion of share exclusively in percentage.⁶ If all the profit was assigned to equity owner, Mudarabah would become plain investment (with physical and intellectual labor paid at market price), and if they agreed for entrepreneur to get entire profit, then it would be the case of so called Kard Hasan agreement (common interest-free loan), and not Mudarabah.

Loss is covered in proportion to the share of participants in business, in which case the bank loses a part of invested assets, and *mudarib* loses effort,

⁶ M. Siddiq, Al-Ameen Al-Dhareer: *Al-Gharar in contracts and its effecton contemporary transactions*, IDB – Islamic Research and Training Institute, Jeddah Saudi Arabia, 1997.

time, immaterial but also certain material investment (if any). In case of loss, everyone loses whatever they invested (Siddiq).

Considering that the bank gives certain amount to company, private undertaker, independent entrepreneur, that is its client, to invest that money as he see fit, the bank previously requires elaborate on intended investment on the basis of which the bank, after analysis, may even reject granting the requested loan. In case of loss, the bank investigates consciousness and commercialism of the client – *mudarib*. In case he did all in his power to avoid the loss, the bank does not request the money to be paid back. However, if the loss is a result of deliberate neglecting, unprofessional administration, misuse of assets etc., *mudarib* is obliged to reimburse the damages to the bank.

Musharakah, unlike *Mudarabah* which is a form of financing, represents Islamic form of joint venture. This is the form of financial instrument most consistent with already presented Islamic principles. *Musharakah* stands for business relationship between bank and its client where both parties jointly take part in financing and conducting the job. Profit or loss is shared by all the participants. Profit share participation to certain extent may derogate from percentage of investment in business, while loss is incurred exactly in proportion of individual investments.

Bank and its client having a certain capital agree upon decision to commence the business with certain share in capital, to jointly participate in project management, to dispose of equity and labor, as well as to share expenses, and at the end to share profit and loss of mutual participation in business.

There are various forms of *Musharakah* partnerships, with different characteristics, for instance unlimited and equal partnership where partners enjoy full equality, but in proportion to their investment. As in *Mudarabah*, ratio and manner of profit sharing must be agreed upon that is concluded in time of signing agreement. Eventual loss, besides the one arising from neglecting and irresponsibility, is incurred by both parties in the very ratio of their investments.

Murabahah is nowadays the most important and the most prevailing instrument of Islamic banking. It is the agreement on sale or resale of goods at purchase price inflated by certain profit. As explained by Prof. Hadžić⁷, bank buys equipment, goods, material needed for its client, since he has no assets. The client previously presents exact specification of necessities and contractually obliges to take the goods over from the bank after it procures them on most favorable conditions. This way the client is enabled to get the necessities at once, and pay in rates and subsequently. The bank will sell to client the subject matter of the agreement at a price higher than purchase price, because it must count with

⁷ F. Hadžić, *Islamsko bankarstvo: kratke naznake jedne bosanske šanse*, Glasnik Rijaseta IZ-e u RBiH, LVII/1995, no. 4-6, Sarajevo, 1995, pp. 94-96.

commission. Commission or profit of the bank in this business transaction is known in advance, agreed upon between parties. The bank's profit results from real service, and not based on payment due to period elapsed.⁸

Unlike Mudarabah and Musharakah this is less risky instrument, thus in recent years it has rapidly expanded in Islamic world.

Ijarah. As in Murabahah bank buys items necessary to its client, but afterwards instead of selling it to the client the bank leases it to him. It is a classic leasing business. After the lease period equipment becomes user's property, the user buys the subject equipment out.⁹ All the above proceeds from the assumption that the client shall be financially capable to buy the equipment out after the leasing period and that the bank shall not need the equipment leased to its client. Upon expiration of the agreement, the client has the option to return the subject matter of the lease to the bank and replace the existing equipment with new advanced one.

Salam proposes that buyer pays in advance for certain quantity and quality of product to be delivered on a certain date at an agreed price. This financial technique, similar to advance purchase agreement, is used when seller needs funds before being able to deliver the goods.

Istis'na presents an agreement where user commences production of a specific product "possible to make only subject to agreement, supervision and financial support by bank with secure agreement on particularities, with fixed price and fixed date of delivery".¹⁰ Buyer places order with producer for production of certain goods. It is not necessary though to pay the entire price in advance as in Salam.

This production undertaking includes a process of manufacturing, constructing, assembling or packing. Difference between istis'na and Murabahah, as financing instrument, is that in the first case sales may refer to something non existing in time of signing the agreement, while in Murabahah the subject of purchase may only be existing goods and possible to find at the market. When the producer begins works, the agreement may not be terminated unilaterally.

Istis'na is mainly used for mid-term financing of production or certain goods procurement such as: industrial equipment, machinery, commercial ships, oil tankers, fishing boats, engines, transport equipment, pipes and gas line construction, water and so on.

⁸ M. Štulanović, F. Hadžić, *Osnovi islamske ekonomije i finansija*, Islamski pedagoški fakultet – Ekonomski fakultet, Bihać, 2007.

⁹ F. Hadžić, *Islamsko bankarstvo: kratke naznake jedne bosanske šanse*, Glasnik Rijaseta IZ-e u RBiH, LVII/1995, no. 4-6, Sarajevo, 1995, pp. 97-107.

¹⁰ E. Bakšić, *Islamsko bankarstvo*, Ekonomski fakultet, Univerzitet u Sarajevu, 2002.

In Istis'na there is no reservation for the work to be completed by entrepreneur and may be done by third party under his control and responsibility.

Mukaredah. This technique allows bank to release guarantee – availed bill of exchange with the aim to finance specific project. Investors buying Mukaredah guarantee – availed bills of exchange, take part in profits of the project to be financed in this way, but equally share the risk of unexpectedly low profits or loss. They do not have a saying in project management and act in virtue of shareholders without the right to vote.

Kard hasan is the basic form of interest-free loan. Bank lends its client a certain amount, and he is obliged to restore principal only upon expiration of proposed term. These loans are granted without any associated conditions. The bank usually grants this kind of loan to those clients it already has regular business cooperation with established on principles of Mudarabah and Murabahah, or those it deliberately wishes to help with business completion, that is certain project realization. Kard Hasan is intended to:

- students,
- economically weaker clients,
- owners of investment deposit accounts,
- clients having relation with bank on basis of Mudarabah and Musharakah, already having faced problems in project realization,
- and others.

The concept of *kard hasan* should be recognized as an expression of solidarity. Advantage of such financial technique is also relatively easy maneuverability without great expenses. Many Islamic theoreticians consider this the best method whereby individual attitude towards common social aim may be modified.

Apart from the mentioned instruments of financing it is necessary to emphasize that Islamic banks offer all sorts of usual banking services such as: cash transfer, foreign currencies exchange at official rate, gathering and keeping deposit, commission works, assets buying and selling or managing investments. In other words, in this area Islamic banks offer completely successfully everything offered by conventional banks for fee or fixed price.

6. Capital source of Islamic banks

The modern banking system manufactures money out of nothing. The process is perhaps the most astounding piece of sleight-of-hand that was ever invented. Bankers own the Earth. Take it away from them, but leave them the power to create money, and with the flick of the pen they will create enough money to buy it back again...

- Sir Josiah Stamp

Ex governor of *Bank of England* 1928-1941

Islamic banks are not humanitarian organizations taking from the rich and giving to the poor to serve justice. Interest absence does not mean investment ban or loan granting without intention to make profit. On the contrary, interest-free banking is profitable. These banks gather money in order to invest in profitable projects intended to bring new value and make return. Investments, in addition to benefit for the bank, contribute to society by stimulating economic and commercial growth. Direct income from interest is surely absent, but on the other hand, interest absence strengthens citizens' trust in banks, scope of banking business and value of investments become bigger and bigger, economy becomes more stable¹¹, and thereby, in the long run, operations of these banks is profitable than business run by commercial banks of western type.

Therefore, if interest is excluded, capital sources of Islamic banks are similar to European and American. However, it is not "only" interest. At this point it is necessary to explain certain mechanisms of making profit in conventional banks. It is well known, although every government and every banker try to forget, that banks by giving loan **create** (only without printing) so called *deposit* or *bank* money. We may hear an expression "banking product".

Granting loans banks perform by cashless money transfer. Transferred money is created by banks themselves, it does not exist. Giving loan in fact generates new, fresh money that has never been printed, but is equally demanded and its value is equally high as the value of banknotes or coins. Banks create money by means of so called mechanism of asset monetization. According to Prof. V. Bjelica "Credit activity of banks enables the bank to create money by means of monetizing its assets. Most often and most typical case of creating money is when bank grants loan to some of its clients."¹² The fact of the matter is that banking asset is considered to be not only assets, but also debts. When a citizen signs loan agreement with a bank for, e.g. 100,000.00 euro, with down payment of 20,000.00 euro, the bank's assets include not only 20 thousand paid, but all 100 thousand that do not exist except as announced. Moreover, the bank freely disposes of that amount considering it its own property. Therefore, mere signature of the client in the loan agreement "creates" money for the bank.

Appearance of the banking system based on interest, nowadays the fundament of monetary system in every modern nation, is described by many economic experts and other leading people of their time. It was developed from goldsmiths' practice who established the first banks in Europe several centuries ago. Goldsmiths accepted gold money for safekeeping but they released receipts entitled to holder. In time people in mutual transactions started to pay back their debts or pay for goods and services by these receipts. Thus these receipts began to function as money. It is today's "bank money".

¹¹ World financial crisis did not affect institutions of this type, nor economies where they dominate.

¹² V. Bjelica, *Finansije*, Financing Center, Subotica, 1996.

Very soon it was obvious to bankers that there is no need to put gold into circulation, since those receipts were considered money in public. As time went by, bankers started printing receipts for which they had no coverage for in gold. That is how bankers even today “create money”. It is completely legal for banks to have coverage in money, gold or any other item, for merely 20-30% of the money they dispose of.

The “created” money itself, though, does not make profit of the bank, since it does not take or spend it, and when the debtor restores the debt it disappears. In usual electronic business, especially at inter-banking market, this non-existing money may circulate for quite a long time before somebody takes it over in material form. However (this is an important difference between Islamic and western banks now), for the period up to restoration of debt, that is until somebody takes this money in cash, the bank even charges interest on the non existing money. Giro money, along with interest, surpasses in scope by far the money mass produced and released by the state.

Islamic banks, also “create money”, but paying the debt back restores money mass to normal, while in western economies it constantly enlarges by new interest.

Another mechanism of money creation by banks is “deposit multiplication”. This is similar to “assets monetization”, but the fictive money is not generated at once here, but at first the real client’s money paid in cash on his account, first turns into notional, and then used further. In fact this is more brutal mechanism than the previous one, since it is some kind of a theft. The citizen has as much as he paid on the accounts, but in fact, that money has already been taken by the bank, without leaving written trace of course, and lent it another client. Taking interest, of course!

Let us go back to the beginning of bank financing source. Hence, if we exclude the interest, in Islamic banks there are all sorts of capital as in conventional ones:

- *Equity capital* as investors in other banks. As investors of equity capital, investors make profit on their investment in start-up capital of the bank.
- *Transaction deposits* that are formed firstly of savings investments. It was discussed in “deposit multiplication”. Islamic banks also use clients’ money, although with important difference since many Islamic banks have a rule that this is subject to depositor’s approval. Surely, the bank quarantines full amount repayment. Result is the same, but approval seeking principle is far more civilized. Furthermore, the client has the right to deny approval for the use of his assets. Savings deposit is treated as loan give to bank because its client renounces all benefits which may result from the use of his assets (IDB, 1985). The money from current deposit accounts is used the same way as in conventional banks, to pay on demand, and bank charges commission on other services it performs.
- *Investment deposits* – represent the main capital source for Islamic banks. They are accepted on fixed or unlimited time period. They do not have

fixed nominal value and are similar to ownership in a company. It is shareholders capital in a certain way, considering that these deposits are equal to equity capital and there is no fixed price of deposit pay back or guarantee for restoring that amount of deposit. Large share of money means from this third source of capital forces Islamic banks to approach much more seriously evaluation of economic and market justification of investment deposits and business ventures.¹³

7. Conclusions

Despite current expansion, future development of Islamic financial institutions shall depend on their successful solution finding for the mentioned flaws.

Regardless future outcome of Islamic banks, it is our intention to imply the possibility to make changes in the existing banking system. Based on previous analysis of Islamic banking fundamentals, as well as main mechanisms used in its operations, it seems that their influence on society is significantly more optimistic than the one produced by conventional banking. Interest-free banking and somewhat protective attitude towards citizens grows confidence in banks and public institutions stronger. In the long run, this is the way to enlarge the volume of savings in banks; state has closer insight in assets of citizens and companies and so on. Increasing purchasing power means expanding market and fighting unemployment.

Elements of Islamic banking which cannot fit laws and regulations need not be implemented, but many components of conventional banks may be adjusted to social demand for more ethical approach to operations. It is not enough to merely "abolish interest", nor does return to golden standard seem possible; besides it is not a desirable step back. It is necessary to introduce different business conscience to operations of commercial banks! Such action is not possible without greater changes in entire society, since banks are connected to all social sectors.

Basis and philosophy of founding and functioning of conventional commercial banks is purely "materialistic" concept, while new bank type would have to fulfill development and social tasks by means of financial services.

Practically, experienced bankers would probably find a range of ways for some new, different banks to fit the mentioned, useful for society, financial mechanisms into current legal-financial scope. Every society has experts who are capable to estimate which of the quoted principles and rules should be renounced, and which to accept, in order to respond to requests for economic development support and simultaneously attract clients. It is certain that such banks would have to offer a large scope of services before people invest money in them. To be competitive with conventional banks and to attract clients, the new

¹³ I. Ibreljić, "Kamata i lihvarstvo u teoriji i praksi i problemi tranzicije savremene islamske privrede u beskamatnu", *Znakovi vremena*, no. 13-14, Naučnoistraživački institut "Ibn Sina", Sarajevo, 2001/2002.

type of banks would have to offer good financing techniques and service variety; moreover, they would have to recede from some of the mentioned principles of Islamic banks. For instance, they would have to insure the money of depositors, and to guarantee their profit. This should ensure trust of one generation and practice of the succeeding. Consequently, investment of capital in these banks proposes investment only at minimum risk.

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ASSISTANT DARKO VUKOVIĆ, PHD CANDIDATE^{*}
Union - Nikola Tesla University, Belgrade
ASSOCIATE PROFESSOR ZORAN GRUBIŠIĆ, PHD
Belgrade Banking Academy, Belgrade
ASSISTANT PROFESSOR ANA JOVANOVIĆ, PHD
Union - Nikola Tesla University, Belgrade

THE USE OF MOVING AVERAGES IN TECHNICAL ANALYSIS OF SECURITIES^{**}

Summary

Technical analysis is based on the assumption that market patterns do not change frequently over time and that these patterns may be repeated and predicted in the future. Its foundation is on the negation of the theory of market efficiency to which the fundamental analysis is based on, considering that all market changes are included in the prices. In relation to this theory, technical analysis assumes that the market is adjusting according to the trends that are determined by the changing attitudes of investors with respect to a number of economic, monetary, political and psychological forces. Market changes cannot be immediately expressed by the price which is the basis for investors to achieve greater profits.

Refined version of technical analysis is based on the assertion that there are patterns of stock prices trends that can be explained, but after these patterns have been determined by investors and after their attempts to make profit on them, investors' trading activity affects prices leading to changes in pricing patterns. A moving average is the most reliable and most widely used technical indicator representing an average value in a given time interval. It indicates the signal to buy when price rises above the moving average and the signal to sell when the price falls below the moving average.

Key words: *technical analysis, moving averages, securities*

JEL classification: G12, G17

1. Introduction to the subject matter

One of the eternal questions in the analysis of investments in securities and portfolio management is whether technical analysis is an appropriate indicator

^{*} E-mail: vdarko@hotmail.rs

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of price movements. For decades, many authors¹ have almost contemptuously criticized technical analysis and its methodology in the study of price movements in the market. Research and evidence to show that it is possible to rely on the ability of simple rules to predict price movements in the market are contrary to previous theories. Although this evidence is not very convincing, it does show that technical analysis is not in the least neglected in the analysis of price trends.² Moreover, there is no single investor, broker or any other financial market participant that would initiate a serious analysis of financial assets, ignoring the technical analysis methodology. Brown and Jennings suggest that technical analysis is of great importance because the value of assets is not fully expressed in prices, adding that traders have rational predictions about price relationships and their signals.³

Most authors believe that the use of technical analysis methodology is based on two basic premises.⁴

Firstly, market patterns do not change much over time, especially long-term trends. While future market conditions may be different from the past, even to a large extent, the way the market respond to a whole new uncertainty is usually similar to the way the market has reacted in the past. It is assumed that the patterns in market prices are repeated in the future so these patterns can be used to predict a trend. Secondly, relevant investment pieces of information can be distributed fairly efficiently, but this distribution can not be totally perfect. According to Gencay and Stengos, even if this distribution were almost perfect, some investors would use technical analysis having an advantage over most other investors and would therefore react first.⁵

However, such statements should not diminish the importance of fundamental analysis. Fundamental analysis assumes that the market share price does not fully reflect its real market value, i.e. intrinsic value of the company. The importance of comparing the mentioned values is obvious for investors wishing to invest their funds in those shares (assets) whose internal value is greater than the market value, since it is expected that in the long run, the market value of shares will reach its real value. Fundamental analysis assumes that analyzed data, if well estimated, indicate the inherent value of the shares (for example, discounting dividend model), while technical analysis assumes that it is very diffi-

¹ E. F. Fama, M. Blume, "Filter rules and stock market trading profits", *Journal of Business* 39, 1966, pp. 226-241.

² B. LeBaron, "The Stability of Moving Average Technical Trading Rules on the Dow Jones Index", *Derivatives Use, Trading and Regulation*, Vol. 5 (4), 1999.

³ D. P. Brown, R. H. Jennings, "On technical analysis", *The Review of Financial Studies*, 2(4), 1989, pp. 527-551.

⁴ R. Gencay, T. Stengos, "Moving Average Rules, Volume and the Predictability of Security Returns with Feedforward Networks", *Journal of Forecasting*, 17, 1998, pp. 401-414.

⁵ R. Gencay, T. Stengos, *ibidem*.

cult to assess the inherent value and that it is virtually impossible to consistently receive and analyze quality information. There is particular skepticism when it comes to the value of analysis based on published financial statements.

For this reason, technical analysts prefer to focus on market data as indicators of factors of financial assets supply and demand. Today, many empirical studies emphasize the necessity of using both technical and fundamental analysis while observing the market. Chiarella, He and Zheng propose a model that uses both charter techniques (moving average method) and the idea of fundamental analysis in a dynamic financial market.⁶

The aim of this paper is to explain technical analysis by its most important method - moving averages (MA), where we will analyze the three major moving averages, with the actual data of price movement of the company "Microsoft", and also present the other methods used in this methodology. This paper will show that it is possible to notice pricing trends in a very simple and transparent way and make conclusions about dynamics and price movements. Selected data in the work and their analysis is the simplest method of moving averages (because it includes only 10 price data), which serves to explain the subject matter in the simplest and most transparent way. More complex analyses, involving a larger number of data, use the same methodology and settings.

2. Technical analysis

Technical analysis relates to the study of price movements in the market using charts and quantitative techniques to predict price trends. It represents a method of recording (usually in the form of charting) the trading history of a particular financial instrument (shares, futures, currencies) and on this basis it predicts potential future trends.⁷

It is based on publicly available market data and focuses on internal factors by analyzing trends in the entire market, industry average movements or the movement of stocks. According to Dugalic, technical analysis is a process, which formulates the position on future developments on the basis on the movement of stock prices in the past.⁸

This technique can be applied to any market where there is detailed history of price movements. According to technical analysts profit can be achieved by proper positioning in the direction of the price trend. If the trend goes up, then

⁶ C. Chiarella, X. Z. He, M. Zheng, "An analysis of the effect of noise in a heterogeneous agent financial market model", *Journal of Economic Dynamics and Control*, 35 (1), 2011, pp. 148-162.

⁷ D. R. Edwards, J. Magee, *Technical analysis of stock trends*, 7th edition, John Magee Inc, Chicago, Illinois, 1992.

⁸ V. Dugalić, "Teorijska fundiranost tehničke analize cena akcija", *Finansije*, vol. 57, 2002.

we should look for an opportunity to purchase; in the event that prices go down, we should be selling. Some authors believe that technical analysis is the general method of a huge number of securities trading techniques.⁹

Such analysis is sometimes referred to as market or internal analysis for its attempt to assess the supply and demand of securities or the entire market by monitoring the market itself. Therefore, technical analysts believe that the market is the best source of information about itself. It is most often based on publicly available data on the market and does not seek to analyze the technical data of the company, such as cash flows, dividends and projections of future dividends. As the market data consist of stock prices or market index level, the volume (number of securities traded), and technical indicators, many technical analysts believe that only those market data are relevant. According to the lead technical analyst Martin Pring, technical analysis assumes that the stock market moves according to the trends determined by changing attitudes of investors in respect of a number of economic, monetary, political and psychological forces.¹⁰

Analysts believe that the process of price adjustment to new information is a process of gradual adaptation to the new (equilibrium) price. As prices adapt from the old equilibrium the new level, so the price moves in the same way. The fundamental question is not why the changes happen, but the fact that they do. According to this method, stock prices indicate a noticeable trend that investors can exploit and there is a tendency to pay attention to changes in stocks movements and taking a position that allows the analyst to take advantage of the trend. The focus of technical analysis lies on the observation of changes in the movement of stock prices that tend to move in trends, because stock prices adjust to a new level of equilibrium. These trends can be analyzed and changes in them can be seen by studying the dynamics of price and trading volume in a given period. The emphasis is on the most probable price changes. Analysts tend to assess the overall situation on the securities market through the analysis of various indicators of price.

A refined version of technical analysis is based on the assertion that there are patterns of stock prices movement that can be explained, but after determining these patterns by investors and their attempts to make profit on them, their trading activity affects prices, leading to changes in pricing patterns.¹¹ Such influence of patterns on prices leads to constant price evolution, which means that only the best analysts are rewarded, because they are the first to detect new patterns. This idea bridges the differences between technical and fundamental analysis, because in some way it supports the concept of market efficiency. Namely, the idea allows the possibility of temporarily unused opportunities for profit (technical analy-

⁹ W. Brock, J. Lakonishok, B. LeBaron, "No Access Simple Technical Trading Rules and the Stochastic Properties of Stock Returns", *The Journal of Finance*, Vol. 47 (5), 1992.

¹⁰ J. M. Pring, *Technical Analysis Explained*, 2nd Edition, McGraw Hill, 1985.

¹¹ Z. Bodie, A. Kane, J. A. Marcus, *Essentials of Investments*, Data Status, Beograd, 2009.

sis), but also implies that market participants aggressively use that opportunity as soon as they find them out (the theory of market efficiency).

Technical analysis is based on three key principles:

1) *Price movements in the market take into account all factors.*

Technical analysis assumes that all the available information has already been included in the price and is therefore not necessary to explicitly analyze the fundamental economic, political and other factors which might affect the price. Since all possible information is already been included in the current price, only historical price movements should be studied.

2) *Prices move in trends.*

Although it has not been explicitly proven that the prices have to follow trends, technical analysis is based on empirical evidence and common sense to assess price trends. For example if property owners believe that interest rates will reduce the value of their homes, they will be inclined to sales. The prices of these properties are likely to fall until a balance between sellers and buyers is achieved. This gradual price movement (trend) is what technical analysis tries to identify and exploit. Anyone who does not believe that prices move in trends will not have much use of technical analysis. The basic idea is that the price trend is probably the most important concept of technical analysis.

3) *History tends to repeat itself.*

Technical analysis is based on the belief that investors collectively repeat the behavior of the investors that have preceded them. To a technician, the emotions in the market provoked by fear or greed may seem irrational, but their existence can not be denied. Because investor behavior is so repetitive, their actions based on price movements will also be repeated. i.e. patterns of price movements believed to predict the future will appear on a chart. Technicians use these surveys to help determine whether a trend will continue or if a new trend might develop. It is important to understand that the field of technical analysis is not limited to the study of charts. Technical analysis is always primarily engaged in price trends. All that can affect price trends is of the interest for a technical analyst. As an example, many technicians monitor the enthusiasm of investors. This way they try to assess the general attitude of investors, to determine whether the market is rising or falling.

3. Technical analysis methodology

Technical analysis uses numerous methods of monitoring price movements in order to more clearly observe patterns that allow the temporarily unused opportunity for profit making. These methods are much simpler than methods based on mathematics and in a very short time they give a clear picture of price movements. The most important methods are charting and technical indicators.

Charting is a method using charts of past stock prices and trading volume hoping to identify patterns that can be used to achieve profits. The best known techniques of this method are:

- a) line charts (Dow terija) – they determine long term price trends;
- b) bar charts - showing the highest and lowest prices in the given time interval and
- c) candlesticks – similar to bar charts, and in addition they show prices when opening and closing.

In addition to charting, technical analysts use technical indicators to assess the possibility of climbing or falling markets. According to Bodie, Kane and Marcus, there are three types of technical indicators: *sentiment indicators* - which aim to determine the expectations of different groups of investors (trin statistics, trading with incomplete lots, trust index, *Put/Call ratios*, cash position of open investment funds); *money flow index*- which measures the potential of different groups of investors in purchasing or selling shares, in order to predict the pressure on prices caused by these procedures (interest in short term selling and broker account balance) and *market structure indicators* - which follow price trends and cycles (moving averages, width and relative strength in the market).¹²

4. MA (Moving averages)

Moving average (MA) is a commonly used technical indicator and represents the average value in a given time interval. The main objective of this method is that, by removing current fluctuations, the basic flow of a phenomenon is highlighted.¹³ The simplest rule of this method indicates that there is a signal to buy when prices rise above the moving average and there is a signal to sell when prices fall below the moving average. The basic idea of this method is to provide a template for determining the general direction or market trend by examining data in the recent past.

If we, for example, want to determine what the average closing price has been over the last ten days, we get the figure by adding up 10 of these prices and dividing them by 10. Given that the closing price changes every day, so does MA line move reflecting the price changes. Moving averages can be considered as an artificial construction of time series in which all empirical data are replaced by mean value of this data, a number of previous and as many following data.¹⁴

¹² Z. Bodie, A. Kane, J. A. Marcus, *Essentials of Investments*, Data Status, Beograd, 2009.

¹³ A. Bradić Martinović, "Stock market prediction using technical analysis", *Economic Annals*, no. 170, 2006.

¹⁴ M. Žižić, M. Lovrić, D. Pavličić, *Metodi statističke analize*, Ekonomski fakultet, Beograd, 2003.

The general formula representing moving averages is as follows:

$$MA_t = 1/N \sum_{i=0}^{N-1} P_{t-i},$$

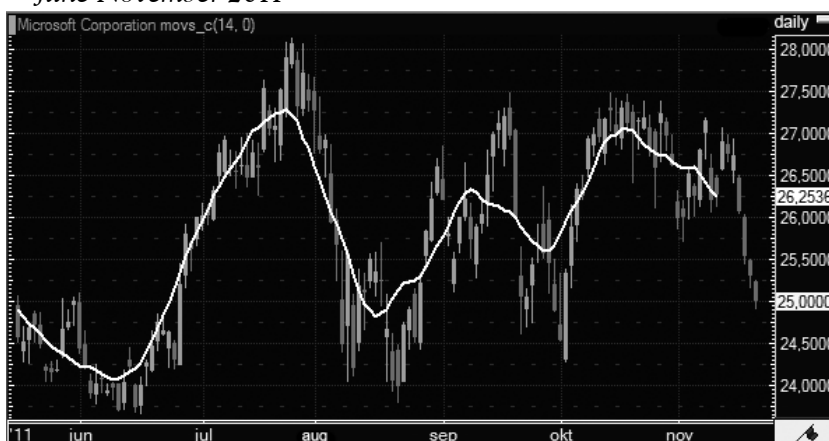
where MA_t represents a moving average, N – time period and P_{t-i} price in a given period of time.

The basics on the analysis says that, when P_t is higher than MA_t , there is a strong signal to purchase, whereas when P_t is lower than MA_t , there is a clear signal to sell.

MA is an indicator showing which direction the price moves. It can not be used to predict future prices i.e. it represents the only reaction to what is happening in the market, not on what is to happen in the future. What is the problem with technical analysis concerning MA is that it only shows what happened in the past (calculated by taking into account historical prices). This time delay (*time lag*) is less pronounced when the MA is calculated based on 20 previous closing prices (MA 20), rather than 200 closing prices.

In other words, this means that short MA shows a change in the trend much faster than MA, calculation being based on a longer time basis. MA use often raises the price issue, as it is used for calculating the moving average. Most technical analysts use closing, while others use midpoint value, which is obtained when the difference between the highest and lowest daily price is divided by two. Some even use closing price in combination with the highest and lowest daily price. These three values are divided by three and the result price is taken as the basis for calculating MA.

Figure 1: Moving average of Microsoft Corporation shares in the period from June-November 2011



Source: Programme TeleTrader Professional, 22/11/2011

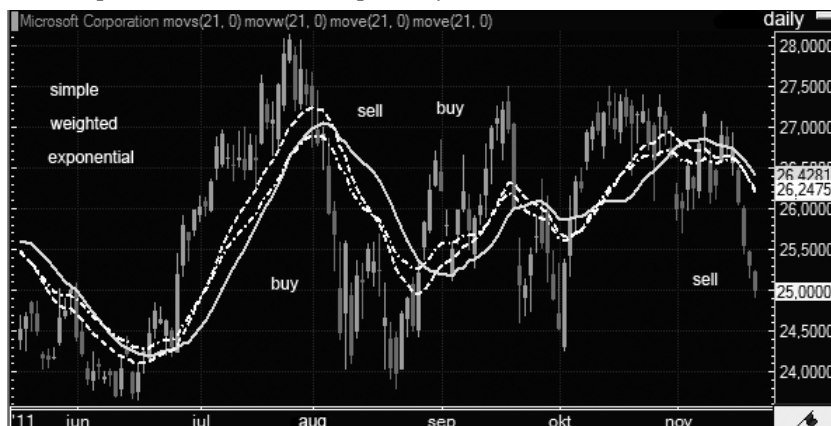
Figure 1 shows the moving average of the *Microsoft Corporation* shares in the period June–November 2011. The moving average is marked by a white line showing the average-moving trend of shares. The growth of the moving average line and the prices of stocks above this line indicate an upward trend, while the decline in the moving average line and the share price below this line indicate a downward trend.

4.1. Moving average analysis

There are several types of moving averages that are used as techniques of different variants of price trends. First, we consider three main moving averages (simple, weighted and exponential), and after that, we explain the other. For ease of comparison and analysis, moving averages will be shown through an example of the *Microsoft Corporation*, in the same time interval, on the fewer number of charts - for the sake of visibility and differentiation.

- *The Simple Moving Average* – is most commonly used in technical analysis (Figure 2). However, in this MA there are two problems. The first is that the MA gives the same weight to each price in the given period. When, for example, the MA for the past 10 days is calculated, the last day is as important as the first, i.e. each day has a significance of 10%. Many technical analysts do not agree with this, believing that prices in the last days should have much greater significance than the price at the beginning of the period for which the MA is calculated. Another criticism is that the calculation of MA takes into account only a defined period, not a long time period in which prices are formed.
- *The Weighted Moving Average* – in order to overcome the shortcomings of the simple moving average, technical analysts have constructed a weighted moving average (Figure 2). In this case, the closing price on the tenth day (we calculated the MA of 10) is multiplied by 10, the closing price on day by 9 and so on. Therefore, more importance is given to recently formed prices. The numerator is then divided by the value of the multiplier ($10 + 9 + 8 + 1 \dots = 55$).
- *The Exponentially Moving Average* also gives more importance to prices formed in closer time intervals (Figure 2). However, unlike the weighted moving average where the weights are predefined, there is a possibility for the analysts themselves to determine the importance to assign to certain days. It is carried out by giving a certain percentage to the last day, so based on that procedure, the difference up to 100% is added up to the penultimate day. For example, if the price on the last observed day is increased by 10%, the penultimate day automatically gets the value of 90%. Nowadays, traders have no great need to be burdened with the way of calculating the exponential moving average. It is enough to enter the number of days, whereas the computer automatically outlines the MA on a chart.

Figure 2: Simple, weighted and exponential moving average of the Microsoft Corporation shares in the period from June-November 2011



Source: Programme TeleTrader Professional, 22/11/2011

This graphic example clearly shows differences between the simple, weighted and exponential moving averages. The simple moving average is the farthest from the graphics. This means that the moving average trend shows the change only after big price movements, while it does not respond to slight price fluctuations. The weighted moving average is faster (the average line is closer and shows faster change in the trend), while the exponential moving average line is the closest to the graphics and this moving average is the fastest to indicate the formation of a new trend. To calculate the moving averages in our example (for simplicity we calculate the MA of 10 - moving averages for 10 prices), it is necessary to present information about share price of the Microsoft Corporation and to isolate the 10 most recent closing prices.

Table 1: Prices (open, high, low and close) of the Microsoft Corporation shares in the period 8/ 11 – 21/ 11/ 2011

Time	Open	High	Low	Close
8.11.2011	27.0100	27.2000	26.6850	27.1600
9.11.2011	26.5900	26.7500	26.0600	26.2000
10.11.2011	26.4700	26.5000	26.1200	26.2800
11.11.2011	26.5799	27.0750	26.5700	26.9100
14.11.2011	26.8799	27.0000	26.6500	26.7600
15.11.2011	26.5600	26.9400	26.4000	26.7400
16.11.2011	26.4700	26.5100	26.0400	26.0700
17.11.2011	26.0100	26.0400	25.4400	25.5400
18.11.2011	25.4800	25.5000	25.1500	25.3000
21.11.2011	25.2400	25.2500	24.9000	25.0000

Source: Programme TeleTrader Professional, 22/11/2011

Calculation of moving averages can be represented as follows (figures are chosen by the author, and they represent the Microsoft Corporation shares, in the period from 8/11-21/11/2011).

The simple moving average is represented by the following formula:

$$SMA = [P_{m_1} + P_{m_2} + \dots + P_{m_{10}}] / 10,$$

where SMA denotes the simple moving average, P_{m_1} – closing price on the first day of observation period, P_{m_2} – closing price on the second day, ..., $P_{m_{10}}$ – closing price on the last day. The calculation is as follows:

$$PPP = [P_{m_1} + P_{m_2} + \dots + P_{m_{10}}] / 10 = (27.1600 + 26.2000 + 26.2800 + 26.9100 + 26.7600 + 26.7400 + 26.0700 + 25.5400 + 25.3000 + 25.0000) / 10 = 26.19600$$

The weighted moving average is expressed by the following formula:

$$WMA = [NP_m + (N-1)P_{m_{-1}} + \dots + 2P(m_{-n+2}) + P(m_{-n-1})] / N+(N-1)+\dots+2+1$$

The weighted moving average, calculated by the same *Microsoft Corporation* data is $(27.1600*10 + 26.2000*9 + 26.2800*8 + 26.9100*7 + 26.7600*6 + 26.7400*5 + 26.0700*4 + 25.5400*3 + 25.3000*2 + 25.0000) / 55 = 26.4867272$

The exponential moving average requires a slightly more complex analysis, and can be represented by the formula:

$$EMA = [(P_t * \alpha_t) + (P_{t-1} * \alpha_{t-1}) + \dots + (P_{t-k} * \alpha_{t-k})] / \sum \alpha,$$

where P_t , P_{t-1} , P_{t-k} denotes share prices in the given periods, and α denotes weights. In our example, EMA is:

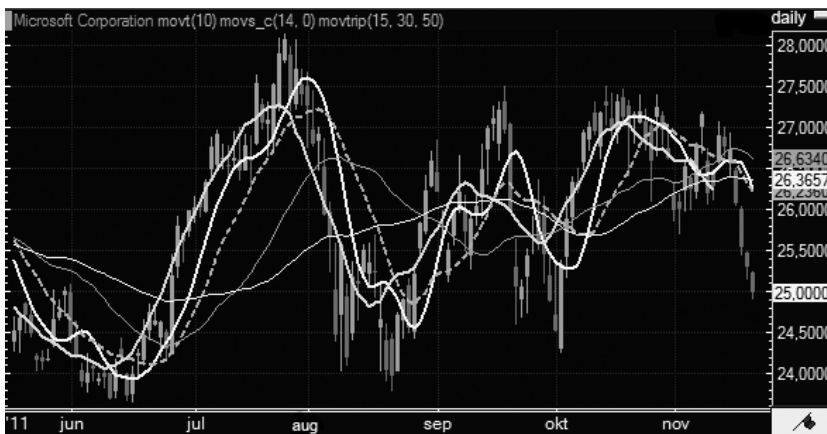
$$(27.1600*30 + 26.2000*20 + 26.2800*10 + 26.9100*5 + 26.7600*4 + 26.7400*4 + 26.0700*4 + 25.5400*4 + 25.3000*4 + 25.0000*4) / 89 = 26.49402$$

Based on the calculated data it can be concluded that in the initial period (8/ 11) the share price of the *Microsoft Corporation* was growing in relation to all three moving averages. This means that the trend was a signal to purchase. At the end of the period, the share price of the *Microsoft Corporation* was falling and it was below all three observed averages, indicating a favorable situation for the purchase (21 /11). The simple moving average has shown the lowest value of MA indicators, as it emphasizes the importance of new data. In this example they have shown the effect on its lowest value compared to the other two MAs. This is the biggest shortcoming of the simple MA, highlighted by many authors. EMA also highlights the importance of new data, but far less than the simple MA because it emphasizes the importance of the first data in the series (which

are also the oldest of the data) and reacts more quickly to changes. This is why these two indicators of moving averages have such different results.

- *Triangular Moving Average* attaches particular importance to the middle of the observed series. This method can be described as a simple moving average which is double aligned. Periods used in the MA vary depending on whether an odd or even number of time periods is being observed (Figure 3).

Figure 3: *Triangular, centered and triple moving average of the Microsoft Corporation in the period from June-November 2011*



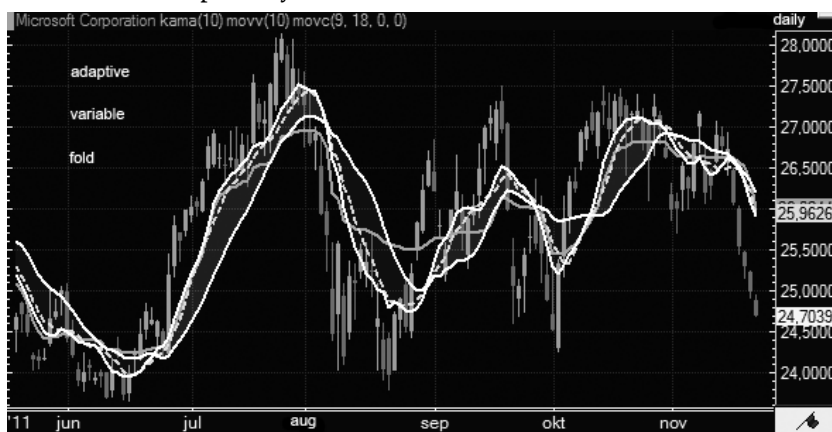
Source: Programme TeleTrader Professional, 22/11/2011

- *Centered Moving Average* is similar to the simple moving average, but differs in the first shown point. The MA always takes the middle of the observed period as the first point. For example, if you watch three periods, a centered MA would define the starting point from the second period. If an even number of periods is analyzed, then the MA starts from the first point to the right of the middle of the period (Figure 3).
- *Triple Moving Average* is an indicator that calculates and displays three simple arithmetic averages of the same price (closing prices), from each of the newest bars of a parameter period. These three averages can help determine strengths or weaknesses of a trend and is also used to determine the upward (upward) and descending (downward) trends (Figure 3).
- *The Adapting Moving Average* automatically adjusts to market volatility, using the level of market fluctuations to calculate the length of the trend (Figure 4). That is, in order to determine the MA, it uses sensitivity of the market to calculate the length of the trend.¹⁵

¹⁵ P. J. Kaufman, *Trading Systems and Methods*, John Wiley & Sons, Inc., 1998.

- *The Moving Average Variable* is the exponential MA that automatically adjusts the trend to volatility of the observed data. To measure the volatility the MA uses VHF (vertical-horizontal filter). The sensitivity is achieved by giving greater importance to the current-time data (Figure 4).
- *The Moving Average Cross* is an indicator using the cross of two moving averages of different time periods (Figure 4).

Figure 4: Adapting, Variable and Cross moving averages the Microsoft Corporation shares in the period from June-November 2011



Source: Programme TeleTrader Professional, 22/11/2011

Moving averages are subject to the dynamic needs of analysts and that is why they are often combined or new ones created. The aforementioned MAs are those that are commonly used in the analyses. However, their number is not final and they include: *The Adapting Moving Average*, *The Four Moving Averages*, *The Fractal Adaptive Moving Average (FRAMA)*, *The Hull Moving Average (HMA)*, *The Moving Average Momentum*, *The Moving Average Oscillator*, *The Smoothed Moving Average*, *The Variable Index Dynamic Average (VIDYA)*.

5. Range and limitations of technical analysis and moving averages

Technical analysis is a method for evaluation of securities, which analyzes statistics of market activities, such as prices and trading volume. It does not analyze the substantial value of securities, but identifies price patterns that may indicate future activities through charts, indicators and other tools. By analyzing the supply and demand in the market, technical analysis aims to determine direction of the future trend. It is based on the idea that the market is not fully effective and that changes will not be included in prices immediately. These are

only the greatest advantages of technical analysis, which can be decomposed by the following facts.

- Trends in financial markets can be long and are often influenced by subjective and psychological factors. Given that technical analysis is based on intuitive trend prediction, it can identify them at an early stage and provide great assistance in investment decisions.
- Changes in supply and demand do not happen instantly, but gradually. This time interval justifies the use of technical analysis, because the changes will not immediately affect prices. An ability to detect changes in the market before other participants provides investors the opportunity to earn more.
- Technical analysis uses publicly available information and represents a simpler method compared to fundamental analysis.
- Charts provide noticeable information about price movements and trends, which makes investment decision a lot easier.
- Finally, technical analysis is often used in conjunction with fundamental analysis, which makes decision making more secure.
- The biggest limitation of technical analysis is using intuition to predict future trends, which has caused great controversy and criticism among many authors.¹⁶ Many even believe that its use is meaningless to give false signals, justifying its claim the following facts:
 - most technical analysts can not credibly explain the efficiency of its methodology and tools;
 - efficiency hypothesis may not be entirely (or even at all) rejected, because many empirical data indicate its accuracy, on the other hand, there are studies that show that technical analysis failed, giving false signals to buy and sell;
 - the interval change in the trend may not always be sufficient to predict future prices, this change can happen in a short period of time and be covered by the new price, which supports the theory of market efficiency;
 - data used by technical analysis create “self-destructive” price patterns, because once the form is discovered, the change will be included in the new price.

Bearing in mind the achievements and limitations of technical analysis, it can be concluded that it is a useful method in making investment decisions. Due to its limitations it is often used as an additional technique to fundamental analysis. A number of studies¹⁷ have shown greater efficiency in the common use

¹⁶ B. Malkiel, *A Random Walk down Wallstreet*, Fifth ed., Norton, New York, 1990.

¹⁷ C. Chiarella, X. Z. He, M. Zheng, “An analysis of the effect of noise in a heterogeneous agent financial market model”, *Journal of Economic Dynamics and Control*, 35 (1), 2011, p. 148-162.

of technical and fundamental analysis. Many trends and indicators, which are useful tools in analyzing and presenting data, should not be the final arbiters in making decisions, but should try to help analyze complex financial assets.

Numerous indicators are used in technical analysis. However, the most reliable and most frequently used are moving averages. There are a lot of explanations for this:

- considering that these are “averages”, the main advantage of this indicator is the neutralization of frequent price fluctuations and the fact that in the point of intersection with the current trends, they provide signals to buy or sell;
- moving averages do not try to discover new trends, but they use existing trends and on the basis of these signals they provide information about the purchase and sales, support and resistance lines;
- a number of investors use them as a primary analytical tool, because they give the most accurate market signals in relation to all other technical indicators.

Limitations of the moving averages result from the limitations of technical analysis. Intuitive prediction can create false signals for buying and selling. Apart from it, compared to the charters technique or other analytical tools:

- moving averages are not a suitable indicator of limited-growth markets;
- there is a danger that some observations are seen as average, although their variability is significant.

6. Conclusion

This paper explains the theoretical concept of technical analysis and moving averages. With practical use of this indicator differences in the application of some basic moving averages are shown the example of the Microsoft Corporation. The analysis had the following limitations:

- 1) analysis has been performed only for academic purposes;
- 2) the sample is small, but sufficient to demonstrate differences in the calculation of moving averages;
- 3) obtained results do not perfectly predict the movement of stock prices of the Microsoft Corporation, because of limitations of technical analysis (moving average).

This paper explains the theoretical concept of technical analysis and moving averages. Through the practical use of this indicator, differences in the application of some basic moving averages are shown using the example of the Microsoft Corporation. The analysis had the following limitations:

- 1) the analysis has been performed only for academic purposes;
- 2) the sample is small, but sufficient to demonstrate differences in the calculation of moving averages;
- 3) obtained results do not have to perfectly predict the movement of stock prices of the Microsoft Corporation, because of the limitations of technical analysis (moving averages).

Finally, it can be concluded that technical analysis is an excellent tool for evaluation of price patterns, but that the possibility of its use is limited to subjective way of forecasting future price movement of securities. Given the subjectivity, signals for purchase or sales may differ from the actual (future), which affects wrong investment decisions. Therefore, it is often used as an additional technique with the use of fundamental analysis. Moving averages are used primarily within the methods of technical analysis, because the analysis of existing trends provides the most accurate signals to buy or sell.

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DINKO PRIMORAC, MSc*

Libertas Bussines School, Zagreb, Croatia

MIRKO SMOLJIĆ, MSc

Ministry of Science, Education and Sport, The Republic of Croatia, Zagreb

MARTINA BOGOMOLEC

Valamar hotels and resorts

INTERNET USE AS A PART OF BUSINESS STRATEGY IN SMALL HOTELS IN THE REPUBLIC OF CROATIA

Summary

In this paper a survey was conducted on how much owners/managers of small hotels in Croatia know about the strategic use of the Internet for marketing purposes and whether they are satisfied with the benefits of Internet use in their business. This study helps analyze the situation in the Croatian tourist market of small hotels, which skills and knowledge owners/managers of small hotels have, so that they can use the Internet as a strategic marketing tool and successfully implement it through Internet marketing. Additionally, the survey included the following potential sources of competitive advantage by using Internet tools in small hotels that are important to Internet marketing: improving the services that small hotels offer, the transfer of necessary information to guests, advertising and promotion, small hotel image, loyalty, marketing and Internet knowledge, business partners, associations - "National association of family and small hotels" and informal networks. Namely, in order to create sustainable competitive advantage, high level of involvement of owners/managers in Internet implementation in the business strategy of small hotels is essential. Therefore, this study examines the benefits that owners/managers believe to have by using the Internet for marketing purposes, i.e. how much the Internet can influence the improvement of running of small hotels.

Key words: *business strategy, the Internet, marketing, small hotels*

JEL classification: L1, M30

* E-mail: dinkoprimorac@yahoo.com

1. Introduction

Small hotels are one of the most important and most vital parts of tourist offer of Croatia. They present Croatian tourism in a new way and unite all the qualities of Croatian tourism. It is known that there is no substitution for the warmth of personal approach, and small family hotels provide this kind of approach to their guests.

The size of small hotels is their most important advantage and greatest disadvantage at the same time. The advantage is excellent business flexibility, faster and more efficient meeting of demands, and very close and direct contact with customers. Ironically, the drawback is their size as well. It is the cause of many problems that exist in business: limited financial resources, inadequate management, lack of qualified and trained personnel, undeveloped marketing, poor application of modern communication and information technology, and lack of knowledge about internet marketing.

In this paper we analyze the strategy of using the Internet to improve business in small hotels in Croatia. Since this area has not been sufficiently explored, an empirical research has been conducted to understand the situation of the Croatian tourist market of small hotels. It is important to show how internet marketing strategy and its clearly defined strategic activities can help to improve running of small hotels. The paper will mostly deal with strategic issues of internet marketing in running small hotels.

In order to find answers to these problems, the paper will try to give answers to the following questions:

- What is the position and role of small and medium-sized hotels in modern Croatian tourist market, and the features of their business?
- How can marketing tools be applied in running small and medium-sized hotels?
- How can the use of internet marketing improve running of small and medium-sized hotels?

In order to obtain the necessary answers to the abovementioned questions, this paper will use the following methodology: in-depth interviews with marketing and sales managers of the hotels "Pula" in Pula and "Holiday" in Zagreb, and a questionnaire which has been conducted in the Republic of Croatia.

2. Features of small hotels

In the last few years in Croatia, there has been the trend of increasing importance of small and medium-sized enterprises, and many experts have been examining the features of those companies. Based on the statistics we know that small

and medium-sized enterprises account for the largest number of companies in Croatia, and they employ more than half of the total workforce.¹

In Croatia, in accordance with the Accounting Act a small business is defined as the one that meets the following criteria: the sum of the balance, after deducting the loss reported in the balance of assets, amounts to €1 million, the income of 12 months before composing the balance sheet is € 2 million, with an annual average of 50 employees. Due to their specific activities, the size can be determined otherwise. Thus, in the hotel industry the above criteria are used relatively rarely. Commonly, the criterion of the number of rooms or beds that are available in hotels is used, which often varies from country to country. The upper limit of the capacity for small hotels ranges from 40 to 70 rooms, medium-sized have 70 to 200 rooms and the big ones have 200 or more rooms.²

The nature of hotel business is providing services, which small hotels can use as their advantage. Namely, one of their main advantages compared to large hotels and hotel chains is called personal touch or the ability to provide individualized service. To put it in another way, the owner/manager of a small hotel can run the hotel based on creating relationship with its guests, and thus increase the number of repeated visits of the guests and create their loyalty. In addition, s/he is able to operate the hotel independently, thus increase employee loyalty.³

The advantages of small hotels are numerous. Such hotels are less complicated to build, capital costs are lower and they need less equipment. Due to relatively small capital investment they are attractive to small entrepreneurs. The staff consists usually of the owner and his family (immediate and distant), and professionals. In addition, there is flexible working hour system. Since the work style is simpler, it is easier to train the staff and ensure efficient operation. These factors present the flexibility of small hotels, because the hotels are able to adapt to changing demands much faster than larger facilities. The manager/owner is not burdened with meetings and reports as in big hotels, therefore, s/he can fully devote to planning, organizing, monitoring and guests. Quality is ensured in such conditions because the staff is in constant contact with the guests, the service is personalized, and the staff tries to pay maximum attention to the guests and satisfy their needs and requirements. Small hotel are in a way unique since the guests and the staff are not anonymous - everyone has their own name. It creates a friendly atmosphere, confidence and satisfaction, that is, family atmosphere. An additional advantage is that small hotels usually have regular, loyal visitors. All this provide enough information on what a customer wants without large investments in market research. On the other hand, there are many draw-

¹ <http://www.dzs.hr/>

² S. Pivčević, *Primjena umrežavanja u poslovanju malih hotela*, magistarski rad, Zagreb, 2006.

³ S. Pivčević, 'Strategic networks of small hotels', *Tourism and Hospitality Management*, vol. 15, no. 2, 2009.

backs. Their size is the main cause of difficulties. The growth potential of small hotels is limited for financial reasons. Likewise, they also limited when it comes to promotional and marketing activities. Therefore, sales and service must rely on individual customers, not groups. A small hotel is a small customer in the market, therefore, there is no wholesale to achieve more favorable purchase price. Business volume is too small to provide a high degree of operation efficiency. Small hotel management in many cases is insufficiently and inadequately trained, and the funds available are insufficient for recruitment of experts in specific fields such as marketing. The organizational structure of a family hotel is very simple, so the connection between management and employees is intensive. Entrepreneurial and managerial functions are integrated. Therefore, creativity and innovation related to the formation of flexible products for guests are possible. As workers perform more functions, and are permanently connected to the product and the hotel service and guests, they can much better meet their needs. For the development of a family hotel business culture is important, which is influenced by extremely high work motivation, since it is a private project of an owner/manager. Consequently, there is teamwork with the aim to achieve client satisfaction.

3. Analysis of small hotels in Croatia

3.1. Explanation of a chosen sample for research

Primary data have been collected for the study. As it was stated in the introduction, this is a relatively unexplored area in Croatian tourism, so it was not possible to obtain data from secondary sources. In fact, similar research has been conducted in Africa, and the questions have been taken from foreign literature, while in Croatia there are few published studies of high quality about the issue. Thus, to understand what the owners/managers know about the application and benefits of internet marketing, and whether they are satisfied with it, the research was taken and adapted to Croatian market, that is, the issues important to running small hotel in Croatia were taken into account. Based on the results of the research the conclusions are drawn on the attitudes of owners/managers of small hotels in Croatia regarding the use of internet marketing in the strategic operations of their hotels. The research will help to explain how the owners/managers see their business with the help of internet marketing, and what significant benefits of the Internet are regarding improvement of managing their hotels. The research will also attempt to assess:

- how many owners/managers of small hotels in Croatia have positive opinion on the use of internet marketing when running their own hotels;
- what the owners/managers of small hotels believe that internet marketing can do to their hotel;

- how many owners/managers of small hotels are satisfied with using the Internet, and
- if the owners/managers get help when using marketing tools on the Internet.

3.2. The way how the research methods have been used

The data used in this study were collected from the questionnaire taken from foreign literature and adapted to the Croatian tourist market. The questionnaire was designed on the web page: www.surveymonkey.com.

Since the questioned owners/managers of small hotels perform different functions at their hotel and were very busy, the questionnaire was shortened to the most basic questions that are needed to make solid arguments. All the hotels who are members of the “National Association of family and small hotels” were contacted by phone. We talked to the owner/manager of a small hotel and asked him/her to complete a questionnaire on the website, which was sent by e-mail link. Out of 105 hotels in the association, a positive response (completed survey) was received from 54 hotels (51.43%).

The survey consisted of the following types of questions:

- Multiple-choice questions - question about the number of employees in the hotel (Question 1), the region of the hotel (Question 2). Respondents were offered a limited number of responses to the questions. These were the questions on demographic indicators. They are required to gain insight into the specific situation in the Croatian tourist market.
- Issues which measure the participants’ attitudes - Likert scale on which the whole research was based, because the researchers’ intention was to obtain insight into the level of using and knowledge about internet marketing in the Croatian tourist market of small hotels. We measured the attitudes, that is, the level of agreement with the given statement of the owner/manager of a small hotel.

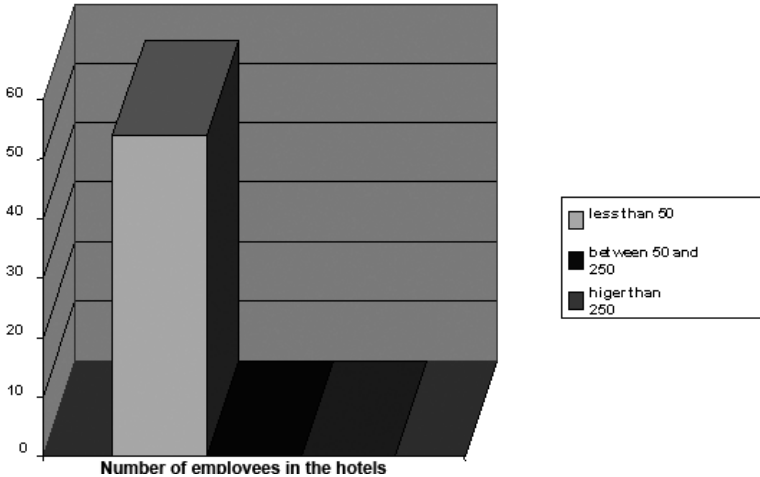
3.3. The results of the research

Empirical research in the study consisted of three questions. The third question, which is taken from the foreign studies present the core of the research. It shows what proportion of owners/managers have positive opinion on the use of internet marketing, how many are satisfied with the benefits of using the Internet for marketing purposes; how much it can help them in running the hotel, and if they are satisfied with the help received when using the internet marketing. The responses received in this study are displayed, and their graphic presentations as well in order to present the structure of the responses.

1. Question: How many employees does your hotel have?

This question was asked in order to eliminate possible hotels that do not belong to the category of small hotels. Classification of hotels is based on the number of employees at the hotel. In such categorization, hotels with up to 50 employees belong to the category of small hotels. All hotels responded that they have up to 50 employees

Figure 1: Number of employees in the hotels

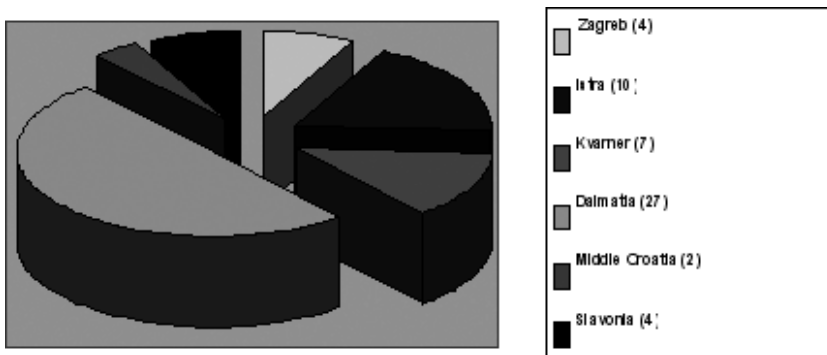


Source: Produced by the author

2. Question: Which region of Croatia does your hotel belong to?

This question was asked to analyze further the proportion of hotels according to the regions and obtain insight in the structure of small hotels according to the regions in Croatia. The largest number of responses was collected from the hotel owners/managers in Dalmatia, as much as 50%, while responses from hotel owners/managers in Istra and Kvarner constitute 31.5%. Below is a graphical display.

Figure 2: Number of the hotels according to the region they belong to



Source: Produced by the author

3. Question: State the degree of your agreement with the statements regarding the application of the Internet when running your hotel.

Table 1: Likert scale of the attitudes of the owners/managers of small hotels

	I could not disagree more	I do not agree	I neither agree nor disagree	I agree	I agree completely	Total number of responses
I am pleased that the Internet can improve the service of a hotel.	3.7% (2)	0% (0)	0% (0)	24.1% (13)	72.2% (39)	100% 54
I am pleased that the Internet helps to transfer information about a hotel to guests.	3.7% (2)	0% (0)	0% (0)	42.6% (23)	53.7% (29)	100% 54
I am pleased that the Internet improves the effectiveness of advertising and promotion of a hotel.	3.7% (2)	0% (0)	0% (0)	44.4% (24)	51.9% (28)	100% 54
I am pleased that the Internet enhances the image of a hotel.	3.3% (2)	3.3% (2)	7.5% (4)	50.7% (27)	35.2% (19)	100% 54
I am pleased that the use of the Internet improves marketing and influences the re-visit of guests.	3.7% (2)	0% (0)	1.8% (1)	55.6% (30)	38.9% (21)	100% 54
I am pleased that the Internet helps maintain relationship with the existing guests.	3.7% (2)	0% (0)	9.3% (5)	27.7% (15)	59.3% (32)	100% 54
I am pleased that the Internet improves the ability to obtain information about customers, competition and travel industry.	3.7% (2)	27.7% (15)	1.9% (1)	31.5% (17)	35.2% (19)	100% 54
I understand enough about internet marketing to make business decisions.	3.7% (2)	29.6% (16)	11.1% (6)	35.2% (19)	20.4% (11)	100% 54
We know to use the Internet for marketing purposes.	3.7% (2)	33.3% (18)	7.4% (4)	35.2% (19)	20.4% (11)	100% 54
I understand the problems when using the Internet for marketing purposes.	3.7% (2)	35.2% (19)	20.4% (11)	27.7% (15)	13.0% (7)	100% 54
I know what is necessary to make the Internet effective for marketing purposes.	3.7% (2)	32.8% (18)	13.2% (7)	35.2% (19)	15.1% (8)	100% 54

I appreciate all that the Internet can do to marketing of a hotel.	5.5% (3)	0% (0)	0% (0)	35.2% (19)	59.3% (32)	100% 54
I believe that the Internet can add value to the business.	3.7% (2)	1.9% (1)	1.9% (1)	25.8% (14)	66.7% (36)	100% 54
Our business partners help us in business over the Internet.	3.7% (2)	31.5% (17)	11.1% (6)	33.3% (18)	20.4% (11)	100% 54
Tips from our business partners influence the business of our hotel on the Internet.	6.2% (4)	37.7% (20)	17.0% (9)	27.8% (15)	11.3% (6)	100% 54
We have strong links with the people who advise us about internet marketing.	5.6% (3)	50.0% (27)	24.1% (13)	18.4% (10)	1.9% (1)	100% 54
Informal networks are the source of information about internet marketing.	3.7% (2)	37.0% (20)	31.5% (17)	24.1% (13)	3.7% (2)	100% 54

Source: Produced by the author

This table shows the attitudes of owners/managers of small hotels on the strategic factors of internet marketing conducted in this study. It is about the perceived success of internet marketing (statements 1-7), knowledge of the owners/managers about the use of the Internet for marketing purposes (questions 8-11), if the owners managers think that the use of the Internet for marketing purposes can get their hotel to the leading position (questions 12 and 13), and the benefits that they may get from the alliances/associations related to use of internet marketing (questions 14-17). Based on the results we can conclude that the highest percentage of the owners/managers responded positively (agree or agree completely) on the current success of the Internet for marketing purposes. 96.3% of them believe that they are satisfied (agree or agree completely with the statement) because the Internet improves the service of their hotel, it helps to transfer information to their guests, and improve effectiveness of advertising and the promotion of their hotels. Furthermore, 85.9% of the owners/managers of the small hotels have expressed their agreement with the fact that the Internet enhances the image of their hotel. Most of the respondents believe that internet marketing helps to create and maintain loyalty of the existing guests, proved by 94.5% of the satisfied owners/managers due to improved marketing and re-visits of guests, and 87. 1% of the owners/managers are satisfied with maintaining relationships with the existing guests due to internet marketing. High percentage (66.7%) shows that the majority of the owners/managers are familiar with the benefits that they can derive from using the Internet to develop CRM (Customer Relationship Management) in their hotel. They stated that the Internet improves their ability to obtain information about customers, competition and

travel industry. As a high percentage of owners/manager (31.4%) have still not seen the benefit of using internet marketing for these purposes, more should be done on the education of owners/managers to learn all the benefits and areas of the Internet use for strategic marketing purposes.

The next investigated factor refers to the knowledge of the owners/managers about the use of the Internet for strategic marketing purposes. The results of the study also showed that the owners/managers know about internet marketing, although not to the extent they could really be satisfied with the benefits of internet marketing. Just over half of the owners/managers disagreed with the statements. Furthermore, they are not sufficiently familiar with the problems of internet marketing. Consequently, these are the results: 55.6% of the owners/managers understand internet marketing enough to make business decisions, and can use the Internet for marketing purposes, 50.3% of the owners/managers know what they need to make the use of internet marketing more effective. Of all of the owners/managers, 40.8% of them understand the problems when using internet marketing, and 38.9% do not understand or recognize these problems. To run a small hotel and to make it a leader in the tourist market, most of the owners/managers responded that internet marketing can help greatly. Namely, 94.5% of them appreciate how much internet marketing can help their hotel, and 92.5% agreed that the use of the Internet for marketing purposes can create added value to their hotel product. The owners/managers do not believe that the association can really help them related to internet marketing. Despite relatively strong association "National association of family and small hotels", the owners/managers believe that they have no use of them in doing business over the Internet. Only 53.7% of the owners believe that their business partners can help them to use internet marketing, but 43.9% of them consider that the tips of business partners do not influence the operation of their hotel on the Internet, and 39.1% think they do. On the other hand, 55.6% of the owners/managers believe that the association that exists in this line of business does not provide enough information on using the Internet for strategic marketing purposes, while only 20.4% believe that there is benefit of the associations. In addition, most respondents disagree that informal social networks can be a source of information about using of the Internet for strategic marketing purposes, because only 27.8% of the owners/managers believe that they are a good source of information, while 40.7% disagree with the above statement.

4. Conclusion

In tourism, hotel industry is a fundamental part of tourist offer and in the tourist market there are accommodation services, food and beverages, and facilities for holiday and relaxation. Hotel is considered the basic representative of tour-

ist offer. It must fully meet the expectations of guests along with the hotel product of basic and additional services. It presents the added value to hotel products and thus creates loyal guests. This paper researched small hotels in Croatia. The organizational structure of small hotels is very simple – the functions of owner and manager are integrated and the link between workers and owners/managers is very close. Creative thinking regarding the ways of finding guests and forming marketing mix are vital. Employees are flexible and creative in their business, marketing task is to find the tourist market that they will serve, attract visitors and offer them a hotel product in accordance with their expectations.

In tourist market, supply and demand are spatially separated. The offer is a constant, static and can be delivered in a given time and space, while demand is characterized by needs of the guests that constantly change. The basic business orientation of small hotels should be marketing, which reveals the needs of tourist market and consequently meet the demands. The role of marketing in small hotels is to find the best way to serve clients and achieve their satisfaction. Segmentation, targeting and positioning (STP) are the starting points for the selection of marketing strategies in the hotel business. Marketing strategy based on establishing relationships with guests is very suitable for running small hotels because it is cheaper to serve existing clients and make them loyal.

The most important advantages of using online marketing tools in running small hotels are primarily the possibility of precise determination of the desired target market groups, online hotel reservation and purchase of hotel products. Its interactivity allows obtaining feedback from existing guests. The Internet offers the possibility of rapid expanding and the transfer of information and flexibility as well - for significantly less financial resources than any other media. Thus, brand awareness of small hotels can expand, while advertising on television or print media is too expensive. Web sites of hotels are a starting point of marketing activities on the Internet, and allow true insight into the marketing mix of hotels.

The most important results of this study are perceived success of using internet marketing in the strategic operations of small hotels in Croatia, the need for additional education of owners/managers of small hotels about the use of internet marketing, and the fact that the association that exists in this line of business does not help sufficiently to small hotels in the use of marketing tools on the Internet. Also, there is a need for better cooperation in this area, for example: workshops, seminars, instructions on the website of the association etc. Based on the statements, it can be concluded that more than 80% of the respondents expressed their agreement with the benefits when using the Internet for marketing purposes which consequently help them in the strategic operations of their hotels. The highest percentage of the owners/managers responded positively, they agreed or agreed completely on the current success of the Internet for marketing purposes. The owners/managers expressed their agreement with the following advantages of internet marketing, which helped their business: improving hotel

services, successful transfer of necessary information to hotel guests, improving promotion and advertising, improving the image of a small hotel, creating loyalty and CRM development. The majority of the owners/managers stated that they have enough knowledge about internet marketing to implement it successfully in their business, although not as much as they would be like. However, despite the fact that the majority possesses certain knowledge, more should be done on the education of owners/managers of small hotels in Croatia. Based on the knowledge which the respondents have about internet marketing, most owners/managers expressed their agreement with the fact that their internet marketing can help greatly in running of small hotels and place them to the leading position in their business. Namely, 94.5% of them agreed with the benefits of internet marketing, and 92.5% with the fact that using the Internet for marketing purposes could create added value to their hotel product. The owners/managers do not think the association can help them regarding internet marketing, because - despite the relatively strong association „National association of family and small hotels” - the owners/managers believe that they have no use of them in business over the Internet. Based on this knowledge further research can be conducted regarding ‘National association of family and small hotels’ and how it can assist more to owners/managers of small hotels in their business and help them gain knowledge on the use of marketing tools on the Internet to improve their business.

The survey also gives an indication to other areas that could be explored more deeply in the Croatian tourist market of small hotels, with the purpose to raise the knowledge of marketing tools to on the Internet a higher level and help owners/managers to improve running of small hotels. The survey also showed that the owners/ managers assess positively internet marketing for running small hotels and that their enthusiasm creates positive results.

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MIHAILO JOVANOVIĆ, MSc*
PTT "Srbija"

PROFESSOR SINIŠA RANKOV, PhD
Graduate School of Business Studies, Megatrend University, Belgrade

COST OPTIMIZATION MODEL AND ECONOMIC EFFECTS OF THE INTEGRATION OF REGISTERED ELECTRONIC AND HYBRID MAIL SYSTEMS

Summary

The paper analyzes and confirms economic and technical justifiability of the integration of registered electronic and hybrid mail systems (standard as well as distributed). The analysis of the system optimization model underlines some comparative advantages of the integration and effects provided for public postal operators, but also for consumers of such specific integrated services. In order to qualitatively prove economic justifiability and integration advantage of individual systems, by applying the method of M/M/1 service system (operations research model) modelling, the system's performances are analyzed (the function of waiting time distribution in the system's waiting room and the function of customers queueing time in the system) contingent on different values of the system's parameters λ (arrival rate) and μ (service rate) as well as the corresponding integration coefficient.

The paper shows economic and financial advantages of REM and HM systems integration in the applied model of the operator's business costs optimization which implies using integrated electronic access channels.

Key words: *electronic business, registered electronic mail, hybrid mail, service systems modelling, integration coefficient*

JEL classification: C60, L87

1. Introduction

Global volume of letterpost services that imply manipulation of mail in physical form constantly decreases. Explosive development of information and communications technologies, most recognizable in the global expansion of the Internet and mobile telephony, has led public postal operators, which are often

* E-mail: mihailo.jovanovic@ptt.rs

too traditionally oriented, to decide on development of their basic activity in the scope of integrated technological and informatics solutions. Regarding specific demands of customers, who have ceased to use traditional written communication thanks to the electronic access channels –the Internet and mobile communication, i.e. electronic mail and SMS messages, postal operators can only provide electronic communication in order to maintain letterpost services within their systems, i.e. protect their revenue. Two systems that provide electronic data transmission are **registered electronic mail and hybrid mail**.

Registered electronic mail (REM) is an electronic service that provides complete electronic exchange of information between end users according to the principles of exchange of registered mail in physical form. The main characteristics of this service are the fact it is completely electronic and it provides reliable and certified data exchange between mail sender, service provider and mail receiver. By comparison with traditional service of electronic mail exchange, REM system provides service of confidential electronic communication that contains record of sent and received mail between previously authenticated users. In every part of REM system, during transmission or exchange of electronic mail, recording and filing of all events and operations are performed and thus faithful tracing of mail status is provided. Therefore, it can be said that REM system, the electronic version of traditional registered mail in physical form, has been significantly improved with strict authentication procedures and high level of integrity protection and mail confidentiality, which provides undeniable record of all the events and operations within the system by applying contemporary cryptographic technologies.

Hybrid mail (HM) is a kind of partially electronic mail exchange where, unlike traditional mailing, the content of mail is sent and shipped in electronic form, printed and packed on the location nearby delivery point and in the end delivered to the receiver in physical form. Thus the combined electronic and physical ways of mail delivery encompasses technological phases of receiving, processing and preparing electronic data, printing mail, putting mail into envelopes or packages, addressing and delivering mail. Although exploitation of the first system of the hybrid mail began in the 1980's, it was only with the expansion of the Internet that brought about its intensive development. This development was led by the simplicity of sending hybrid mail via the Internet, but also by considerable reduction in transportation and processing costs. However, without integrative approach to providing services, postal operators cannot reach full potential of the hybrid mail, and thus their success on the market is limited. Integration with delivery network means that a postal operator produces mail in the way that it is optimized for transport, processing and delivery. It means that the system determines where, when and how the mail will be printed. Using the possibility of where the mail will be printed implies the implementation of distributed hybrid mail (DHM), i.e. using several distribution centers for printing

and packing mail, as well as a possibility of choosing one center because of its equipment or address data [1], [2], [3], [4]¹

2. The effects of the integration of registered electronic and hybrid mail systems

The integration of the public postal operator's REM and HM systems provides customers, who previously used individual, unintegrated systems, with the following, significant advantages:

- 1) Possibility to choose at integrated level these two systems, either if they want to conduct completely electronic communication, i.e. to send registered electronic mail to the receiver or if they want to have electronically sent mail delivered in physical form through the hybrid mail system. In this way, customers of these systems get **additional value**, because thanks to the integration they can simply choose a way of the delivery and characteristics of their mail.
- 2) Possibility to choose delivery speed and mail attributes. REM system has the fastest delivery speed, then DHM system, while HM system has the slowest one. It is understandable as communication in REM system is completely electronic, in DHM system it is mostly electronic and partly based on physical mail delivery, while in HM system electronic communication and physical delivery are equally present. On the other hand, HM system has the broadest range of managing mail attributes, mostly reflected in additional personalization, selection of envelope type and the way of putting a mail into an envelope, using colour print, as well as additional attachments and information. The range is smaller in DHM system and the smallest in REM system.
- 3) **Cutting costs** of mail delivery using delivery channels of REM system, while retaining the technology of delivering mail in physical form through HM system to the customers who cannot receive mail electronically. This option is quite important to big customers ("*billing*") of the integrated REM and HM systems (DHM) who can simply choose a format of mail delivery – electronically or traditionally. Those customers are most often huge telecommunication companies, electric power distributors, public

¹ Universal postal union: "Postal registred e-mail (PREM) functional specifications draft", 2009; Jacob Johnsen-Senior Consultant, "Hybrid Mail", World Mail Review, Nov. 2008; M. Jovanović, S. Rankov, Z. Mišić, "Upravljanje sistemom distribuirane hibridne pošte JP PTT saobraćaja Srbije, XVII telekomunikacioni forum – Telfor 2009, Beograd; M. Jovanović, V. Petrović, S. Rankov, P. Milošević, Z. Mišić, "Distribuirana hibridna pošta – integrisana usluga Pošte Srbije", XXVII simpozijum o novim tehnologijama u poštanskom i telekomunikacionom saobraćaju – PosTel 2009, Beograd.

utilities, commercial banks, insurance companies or local tax administration offices, which monthly generate hefty amount of mail.

- 4) Faster mail delivery using delivery channels of REM system, thus faster and bigger **economic, i.e. financial effects** of the mail: faster payment of bills, reducing time for marketing markets or more efficient informing. At the same time, using the potential of HM or DHM systems for personalizing mail and inserting advertising flyers, customers of the system are given a chance to manage marketing campaigns efficiently and realize additional profit (**special financial effects**).
- 5) Possibility to file mail. This option provides customers of the system with two advantages. First, through REM system a customer can afterwards access digital files, which are electronically signed and have time seal. Second, through HM or DHM systems a customer can in an easy and accessible way issue and deliver mail duplicate. These facilities are value added services for customers of the integrated systems.
- 6) Environmental protection by using REM system due to the reduction in paper forms exploitation and greenhouse gases emission that arise from transportation of physical mail, and on the other hand prevention of digital divisions and human rights protection of those receivers who do not use electronic communication and still receive mail in physical form only through HM or DHM systems. These advantages are additional motives for big users of the integrated REM and HM (DHM) systems to get involved in environmental protection, and at the same time to retain unchanged, traditional way of delivering mail to their clients.
- 7) Possibility for a customer to trace the mail, sent through the access channels of REM system in order to get prepared and delivered through HM and DHM systems, first through REM system, then through the subsystem for receiving, processing and preparing data in HM (DHM) system, and then through *track&trace* system of the public postal operator. Thus customers, regardless of the selected way of mail delivery, retain a very important feature of tracing the status of their mail, which is important for strengthening confidence between the service provider and user.

On the other hand, the integration of REM and HM systems brings numerous advantages to public postal operators, and some of them are:²

² The project team of JP PTT "Srbija": "Projekat sistema hibridne pošte", 2002; mr D. Spasić, *Profil kvalifikovanog elektronskog sertifikata*, Centar za elektronsko poslovanje pošte, JP PTT saobraćaja "Srbija", Telfor, 2008; B. R. Smith et al., *iSeries e-business handbook*, IBM, 2001; M. Singh, *A primer on developing an e-business strategy*, Western Illinois Univeristy, USA, 2002; M. G. Shields, *E-business and ERP*, John Wiley & Sons, 2001; J. Dyshe, *The CRM handbook: a business guide to customer relationship management*, Addison Wesley, 2001; M. Warkentin, *Business to business electronic commerce: challenges and solutions*, Idea Group Publishing, Mississippi University, USA, 2002; "E-business strategy", Department of enterprise, trade and employment, 2004.

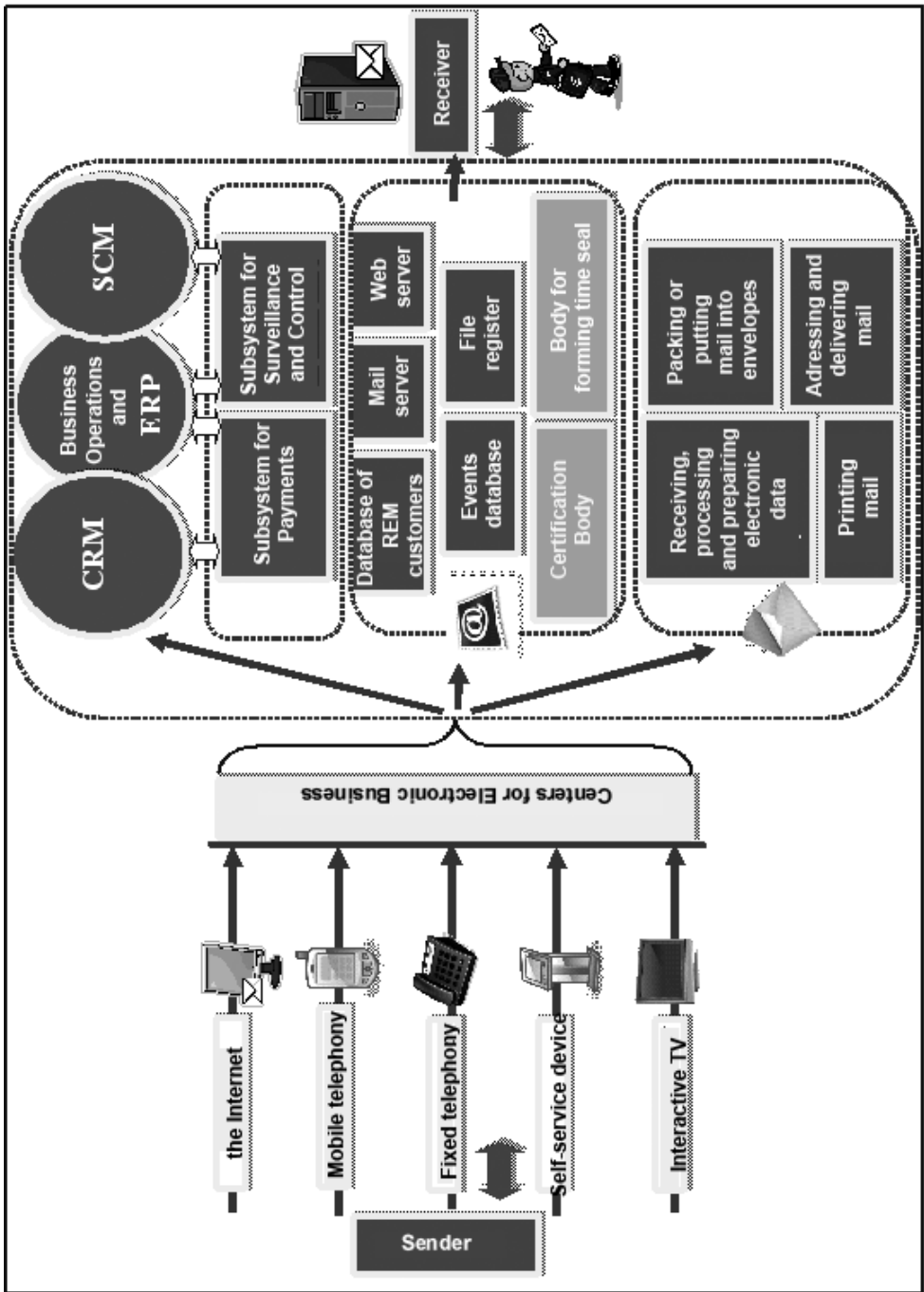
- 1) Simple receiving of mail of big customers (“*billing*” type) as well as of physical persons (“*mailing*” type) through **integrated electronic access channels**. The existing customers of REM and HM services in this way have a feeling that they still use their “old” systems for sending mail, while new customers quite easily accept integrated access, since they can choose a way of delivering mail, along with tracing the status and monitoring performances of both systems at the same time.
- 2) Possibility of different processing and keeping data, i.e. mail: preparation of mail in different formats in HM system, i.e. filing and keeping mail in REM system. For the public postal operator it is very important to offer all the additional services of filing, keeping, processing, search, afterwards access, resending, formatting and mail personalization, which are significantly facilitated by the integration of additional services that are characteristic of individual REM and HM (DHM) systems.
- 3) Considerable increase of operation and simplification and **lower costs of integrated systems exploitation** through using the following opportunities: simultaneous data processing and generating mails of different customers, either in electronic or physical form; easy mail processing (*electronic data processing, sorting, grouping, inserting barcodes and OCR, addressing, filing*); automatic mail transportation (*to various printers and packing machines in different distribution centers of hybrid mail, in different formats for printing*); managing mail delivery (*possibility to deliver mail in electronic or physical form, in desired time span, in various physical formats, automatically marking out dead mail, i.e. generating the status of undelivered or returned registered electronic mail, analysis of the address of the undelivered physical mail and a possibility of another delivery*); possibility of filing documents and issuing mail duplicates; possibility of organizing various marketing campaigns through different direct mail services, providing an option to choose a way of delivery.
- 4) Significantly **reduced costs** of planning, projecting, development, exploitation, maintaining and running electronic access channels and information systems, i.e. considerable **economic justifiability**, thanks to the **integration of REM and HM systems (DHM)** by using universal electronic access channels and parts of the information system, which can be used in both systems (*for example the subsystem for surveillance and control and subsystem for payments*).
- 5) Possibility of integrating the subsystem for surveillance and control and subsystem for payments of the integrated REM and HM systems into a single information system of the public postal operator, which provides control of all technological and information resources, **process optimization and costs cutting**, i.e. increases **economic profitability**. The integration of the system’s management and control elements with the operator’s

information system (the model application and electronic business strategy) embracing the software for Enterprise Resource Planning- **ERP**, Customer Relationship Management – **CRM** and Supply Chain Management – **SCM**, represents a strong information integration which results in easier and more efficient management of the integrated system, reliability grow, **profitability and productivity, cost cutting** of development, exploitation, and maintainment, but also it provides control of all technological and information resources as well as **process and costs optimization**.

- 6) Noticable **growth of profitability, competitiveness, efficacy** and better market positioning of the modern public postal operator, thanks to the application of the universal electronic access channels model and the integration of REM and HM systems.

The integrated model of REM and HM systems, shown in Picture 1, provides one subsystem for surveillance and control and a subsystem for payments, i.e. unique management and control elements. This means that it makes managing integrated systems easier and **optimizes operation costs**. Another significant advantage of the integration is the existence of universal **integrated electronic access channels** of two systems. Unlike the Internet that supports almost all models of electronic business thus representing universal infrastructure (**C2C, C2B, C2G, B2C, B2B, B2E, G2C**), mobile and fixed telephony, self-service device and interactive television are electronic access channels for individual customers – citizens, who in this way access integrated services of REM and HM systems, communicating with other customers, legal entities or public administration, local self-government and administration (**C2C, C2B, C2G**).

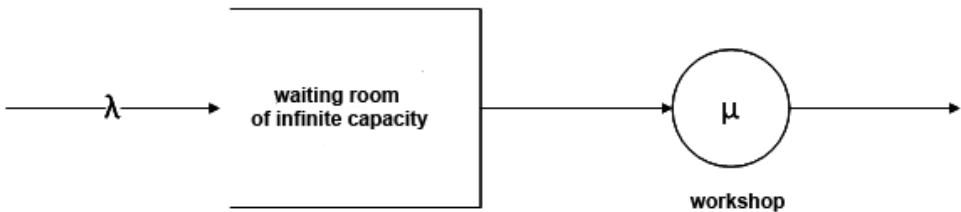
Picture 1: Universal electronic access channels of the integrated REM and HM systems



3. M/M/1 type of service system modelling of individual REM, HM and DHM systems

In order to analyse and quantify integration advantages, we model REM and HM (DHM) systems with the corresponding service system models. This paper considers a kind of modelling conducted with the elementary model of queueing system, which bears **M/M/1**³ name according to Kendall's notation. M/M/1 means that the process of customers arrival to the waiting room of the service system is according to the Poisson distribution (M-Markov process), that the process of servicing customers by the system's workshop is according to the exponential distribution (also M-Markov process), and the number of identical servers in the workshop that process customers equals 1. M/M/1 system is symbolically represented in Picture 2, where λ is arrival rate, and μ is service rate in the service system. M/M/1 system is considered to have infinite capacity, i.e. infinite number of positions in the waiting room and workshop.

Picture 2: M/M/1 type of service system with characteristic parameters λ and μ



When it comes to the Poisson process, the probability $P_k(t)$ that in the system in the time interval t there is k customers equals:

$$P_k(t) = \frac{(\lambda t)^k}{k!} e^{-\lambda t}, \quad t \geq 0$$

The main characteristics of the Poisson process are: the average number of customers $m(t)$ and variance $\sigma^2(t)$ have the same value, which is λt . With the exponential distribution, the probability that a customer queues in the workshop equals:

$$W(t) = \mu e^{-\mu t}, \quad t \geq 0.$$

³ L. Kleinrock, *Queueing systems, volum 1: theory*, Birth-Death Queueing Systems in Equilibrium, M/M/1: The Classical Queueing System, John Wiley & Sons, 1975, стр. 94-98; D. A. Menasce, V. A. F. Almeida, *Scaling for e-bussines*, Performance Modeling Concepts, Prentice Hall, 2000; R. B. Cooper, *Introduction to queueing theory*, Birth-End-Death Queueing Models, Elsevier North Holland, 1981, pp. 73-122.

The characteristic of the exponential distribution is that the average queueing time of customers in the system's workshop $m(t)$ equals standard deviation $\sigma(t)$ and it is $1/\mu$. Some of the main characteristics of M/M/1 service system is the waiting time distribution in the system's waiting room, i.e. queueing time in the whole system.⁴ It comes out that the function of the waiting time distribution in M/M/1 system's waiting room, i.e. the probability $\Pr\{tq \leq t\}$ that customers waiting time in the system's waiting room is less than t , equals:⁵

$$Wtg = \Pr\{tq \leq t\} = 1 - \frac{\lambda}{\mu} e^{-(\mu-\lambda)t}, \tau \geq 0.$$

Herefrom it is easy to get the function of customers waiting time in the waiting room:

$$wtq(t) = \begin{cases} \left(1 - \frac{\lambda}{\mu}\right) o(t), & t = 0 \\ \lambda \left(1 - \frac{\lambda}{\mu}\right) e^{-(\mu-\lambda)t}, & t > 0 \end{cases}$$

When it comes to the function of customers queueing time distribution in the system $Wtz(t)$, it proves to be equal:⁶

$$Wtz(t) = 1 - e^{-(\mu-\lambda)t}, \tau \geq 0.$$

Hence it is easy to get the function of queueing time in the system:⁷

$$Wtz(t) = (\mu-\lambda) e^{-(\mu-\lambda)t}, t \geq 0.$$

Based on the function of customers queueing time in M/M/1 system, we get mean queueing time of customers in the system T , which equals:

$$T = 1/(\mu-\lambda).$$

One of the main features of the Poisson process is that by merging two independent Poisson processes with the traffics λ_1 and λ_2 , we get also the Poisson process with the traffic $\lambda = \lambda_1 + \lambda_2$. Another important feature is by splitting the Poisson process with the traffic λ into two new, also independent processes and the probability of the rate of one new process α and another $(1-\alpha)$, we also get the Poisson processes with the traffics $\alpha \lambda$ and $(1-\alpha) \lambda$.

⁴ L. Kleinrock, *Queueing systems, volum 1: theory*, John Wiley & Sons, 1975; D. A. Menasce, V. A. F. Almeida, *Scaling for e-bussines*, Prentice Hall, 2000; R. B. Cooper, *Introduction to queueing theory*, Elsevier North Holland, 1981.

⁵ L. Kleinrock, *Queueing systems, volum 1: theory*, John Wiley & Sons, 1975.

⁶ L. Kleinrock, *Queueing systems, volum 1: theory*, John Wiley & Sons, 1975.

⁷ Ibidem

⁸ Ibid.

Applying M/M/1 model of service system to the systems of registered electronic, hybrid and distributed hybrid mail, we observe the systems' performances contingent on different values of the parameters λ and μ , and the value of their quotient. In that respect Picture 3 shows the function of waiting time distribution, i.e. the probability that customers waiting time in the system is less than t , $Pr(t)$, in case of hybrid mail and different models of distributed hybrid mail according to the values of the parameters given in Table 1, and Picture 4 shows the function of customers queueing time in the same systems, $wqz(t)$. The analysis implies that the customers arrival at the HM system is according to the Poisson distribution with the traffic λ , as well as that customers arrival at the DHM 1, DHM 2 and DHM 3 systems, i.e. DHM 4 and DHM 5 systems also, in accordance with the characteristics of the Poisson process, is following the Poisson distribution with the traffics $\lambda/5$, i.e. $\lambda/20$, which means that the analysis implies there are 5, i.e. 20 identical and evenly loaded centers of the distributed hybrid mail.

Here is the interpretation of the characteristics of the observed HM and DHM systems contingent on the values of the proposed parameters λ and μ and the derived charts of the function of customers waiting time distribution and the function of customers queueing time in the system:

1. The hybrid mail system modelled with M/M/1 service system whose $\lambda = \mu/2$ (*the system has relatively low arrival rate*) is compared with five systems of distributed hybrid mail. In the DHM 1 system the arrival rate of every center is $\lambda/5$, which means we model this system with M/M/1 system that has 5 times lower arrival rate, i.e. we split the Poisson process of customers arrival at the HM system into five identical Poisson arrivals at the DHM system, while maintaining the same service rate in the workshops of every DHM system. It should be mentioned this type of system is seldom in practice, because it implies 5 times bigger investment for the implementation of the DHM system than for the implementation of the HM system. Therefore, in practice it is more realistic to implement the DHM 2 system, as this system is assumed to be modelled with M/M/1 system whose arrival rate is 5 times lower, but whose service rate in the workshops of every DHM system is also three times smaller. Unlike the DHM 2 system, the DHM 3 system has even smaller service rate in the workshops of every system and it is $1/5$ comparing to the service rate in the workshop of the HM system. Finally, we have observed the DHM 4 system with 20 distributed centers whose arrival rate of every distributed center is 20 times lower, and service rate five times smaller comparing to the HM system, and the DHM 5 system, which unlike the DHM 4 system, has even smaller service rate in the system's workshop and it is $1/20$ of the service rate in the workshop of the HM system.

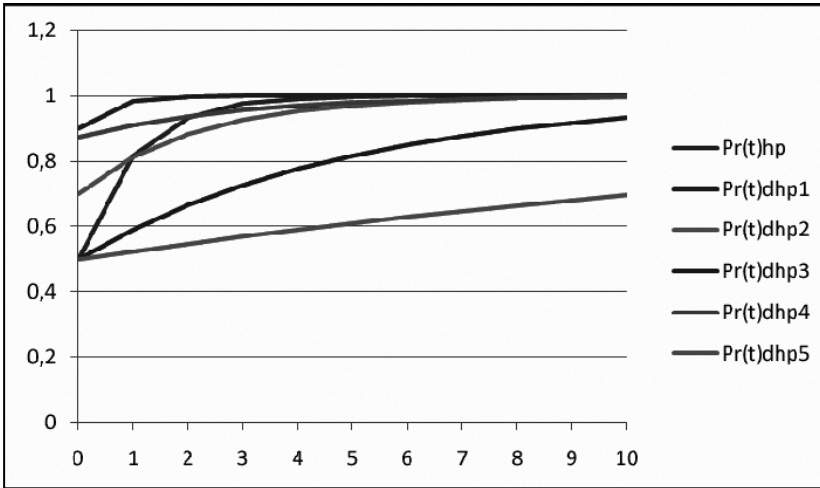
Table 1: Parameters λ and μ for the observed HM and DHM systems

Description of the system	Characteristics of the system	λ	μ	$\rho = \lambda/\mu$	$\mu - \lambda$
HM	Relatively low traffic intensity of the system $\lambda = \mu/2$	1	2	0,5	1
DHM 1: 5 centers	HM with 5 centers, arrival rate of every center is $\lambda hp/5$, and service rate is unchanged and is μhp .	0,2	2	0,1	1,8
DHM 2: 5 centers	DHM with 5 centers, arrival rate of every center is $\lambda hp/5$, and service rate is $\mu hp/3$	0,2	0,66	0,3	0,44
DHM 3: 5 centers	DHM with 5 centers, arrival rate of every center is $\lambda hp/5$, and service rate is $\mu hp/5$	0,2	0,4	0,5	0,2
DHM 4: 20 centers	DHM with 20 centers, arrival rate of every center is $\lambda hp/20$, and service rate is $\mu hp/5$	0,05	0,4	0,125	0,35
DHM 5: 20 centers	DHM with 20 centers, arrival rate of every center is $\lambda hp/20$, and service rate is $\mu hp/20$	0,05	0,1	0,5	0,05

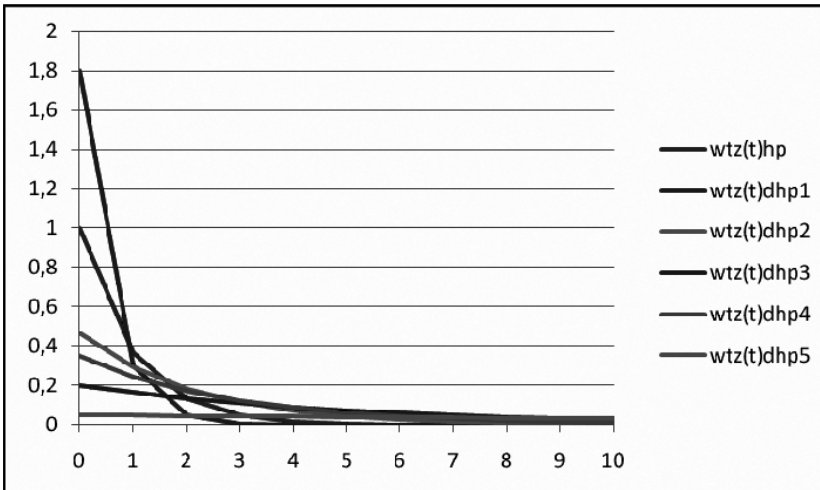
2. From the charts in Pictures 3 and 4 we conclude that in the moment $t = 0$ the DHM 1 system has the best performances, then the DHM 4 and DHM 2 systems, and finally the HM, DHM 3 and DHM 5 systems. Namely, the chart in Picture 3 shows the probability that a customer will not have to wait (moment $t = 0$) is the highest in the DHM1 system, which is very expensive and thus not quite realistic, in which every distributed center has service rate in the workshop like initially observed the HM system, and whose quotient of the parameters λ and μ is the smallest ($\rho = 0,1$). It is followed by the DHM 4 and DHM 2 systems, which has 20, i.e. 5 distributed centers and whose quotient of the parameters λ and μ is 0,125 i 0,3 respectively. The HM, DHM 3 and DHM 5 systems have the same probability that a customer will not have to wait (moment $t = 0$), which is understandable since every of these systems has the same quotient of the parameters λ and μ and it is $\rho = 0,5$. We come to the same conclusion observing the chart in Picture 4, which shows that for sufficiently small time interval t ($t \leq 1$) fastest reduction of queuing time is in the DHM 1 system, then in DHM 4 and DHM 2 systems, and finally in the HM, DHM 3 and DHM 5 systems. As the time passes (time interval $1 \leq t \leq 2$), the performances of the HM system improve, so it overtakes DHM 4 and DHM 2 systems! This is explained by absolute difference between the parameters μ and λ , because – as the time passes – this dif-

ference becomes more and more important for the system's performances, i.e. as the time passes in the system workshop much more customers are processed than the number of new customers arriving at the system.

Picture 3: The function of waiting time distribution in the waiting room in the HM and DHM systems contingent on the value of the parameters λ and μ and the number of DHM centers (HM system has relatively low traffic intensity $\lambda=\mu/2$).



Picture 4: The function of customers queueing time in the HM and DHM systems contingent on the value of the parameters λ and μ and the number of DHM centers (HM system has relatively low traffic intensity $\lambda=\mu/2$).



3. Following the charts in Pictures 3 and 4 we conclude that, from the aspect of system performances (*the smallest amount of time possible that a customer will have to spend waiting to be processed in the system workshop, i.e. the fastest reduction of queueing time in the system as the time passes*), it is best to implement a DHM system with as many distributed centers as possible whose service rate is as high as possible. Naturally, this logical conclusion is in contradiction to the amount of resources necessary for such an investment, so in terms of **optimization of system performance ratio and investment price** it is necessary to find an optimal value through the optimization of the number of distributed centers and the value of the service rate in the workshops of the distributed hybrid mail centers.

We conduct further modelling of the HM and DHM systems by applying M/M/1 model of service system when the values of the parameters λ and μ are approximately same (with, of course, a necessary condition that $\lambda < \mu$ so that a system can be in equilibrium⁹). In that respect Picture 5 shows the function of waiting time distribution, i.e. the probability that customers waiting time in the system is less than t , $Pr(t)$, in the case of the hybrid mail and different models of the distributed hybrid mail according to the values of the parameters given in Table 2, while Picture 6 shows the function of customers queueing time distribution, $w_tz(t)$, in the same systems.

Table 2: The parameters λ and μ for the observed HM and DHM systems

Description of the system	Characteristics of the system	λ	μ	$P = \lambda/\mu$	$\mu - \lambda$
HM	Occupied system $\lambda = 0,9\mu$.	1,8	2	0,9	0,2
DHM 1: 5 centers	DHM with 5 centers, arrival rate of every center is $\lambda hp/5$, and service rate is unchanged and is μhp .	0,36	2	0,18	1,8
DHM 2: 5 centers	DHM with 5 centers, arrival rate of every center is $\lambda hp/5$, and service rate is $\mu hp/3$	0,36	0,66	0,3	1,64
DHM 3: 5 centers	DHM with 5 centers, arrival rate of every center is $\lambda hp/5$, and service rate is $\mu hp/5$	0,36	0,4	0,9	0,04
DHM 4: 20 centers	DHM with 20 centers, arrival rate of every center is $\lambda hp/20$, and service rate is $\mu hp/5$	0,09	0,4	0,225	0,31
DHM 5: 20 centers	DHM with 20 centers, arrival rate of every center is $\lambda hp/20$, and service rate is $\mu hp/20$	0,09	0,1	0,9	0,01

Here is the interpretation of the characteristics of the observed HM and DHM systems determined by the values of the proposed parameters λ and μ and

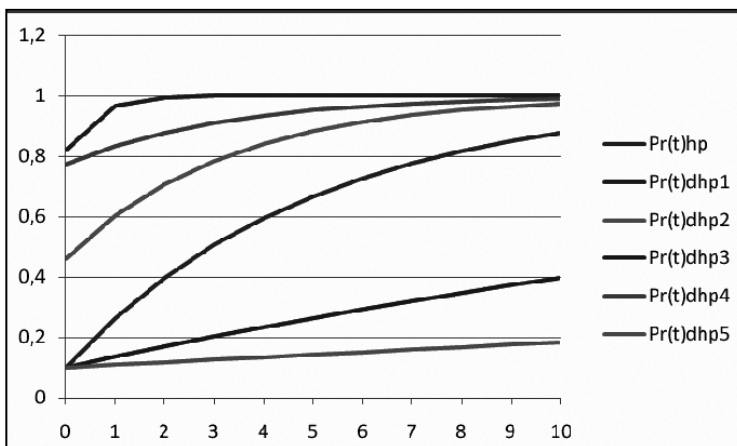
⁹ L. Kleinrock, *Queueing systems, volum 1: theory*, John Wiley & Sons, 1975.

derived charts of the probability that the time a customer has to spend waiting in the system is less than time t and the function of customers queueing time in the system, for the new conditions when the HM system is relatively loaded and $\lambda = 0,9\mu$ ($\rho = 0,9$):

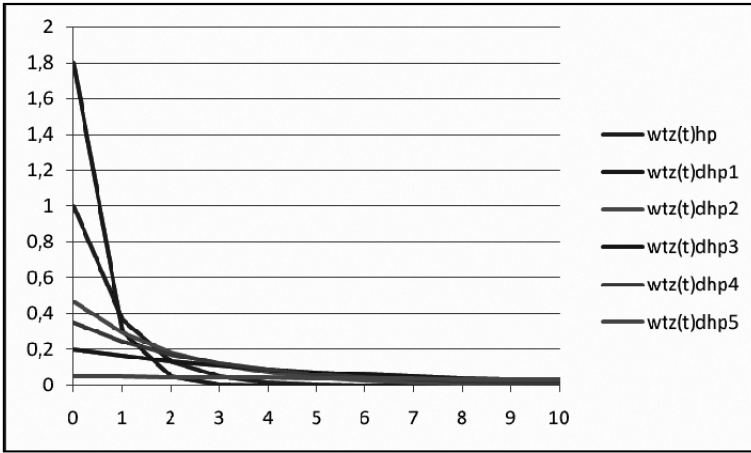
1. The systems behave similarly as in the situation when the HM system is not much loaded ($\lambda = \mu/2$). The difference is in generally worse performances of all the systems in comparison with the previous analysis. Namely, the probability that a customer will not have to wait in the system workshop (moment $t = 0$), is this time quite smaller, which is normal since the systems are more occupied, i.e. the quotient of the values λ and μ is bigger than in the previous analysis (the parameters ρ in Table 2 are higher comparing to the parameters ρ in Table 1 for the same systems). Also, the probability that the time a customer has to spend waiting in the system less than t , for all the samples of the systems in this analysis, approaches slower the value 1 as the time passes on, which is understandable since the systems are more occupied, i.e. the number of customers arriving at the system is just a bit smaller than the number of customers processed in the workshop of the system.

2. As the time passes, unlike the previous model, the performances of the HM system fail to excel the performances of the DHM 4 and DHM 2 systems. This is explained by the absolute difference of the parameters μ and λ , which, as the time passes, becomes more and more important for the system performances, i.e. as the time passes in the system workshop much more customers are processed than the number of new customers arriving at the system. In this analysis the difference between the parameters μ and λ of the HM system is not bigger than the difference between the same parameters of the DHM 4 and DHM 2 systems, thus as the time passes the performances of the HM system do not excel the performances of the DHM 4 and DHM 2 systems.

Picture 5: *The function of waiting time distribution in the waiting room in the HM and DHM systems contingent on the value of the parameters λ and μ and the number of DHM centers (HM system is relatively occupied $\lambda=0,9\mu$).*



Picture 6: The function of customers' queueing time in the HM and DHM systems contingent on the value of the parameters λ and μ and the number of DHM centers (HM system is relatively occupied $\lambda=0,9\mu$).



4. M/M/1 type of service system modelling of the integrated REM, HM and DHM systems

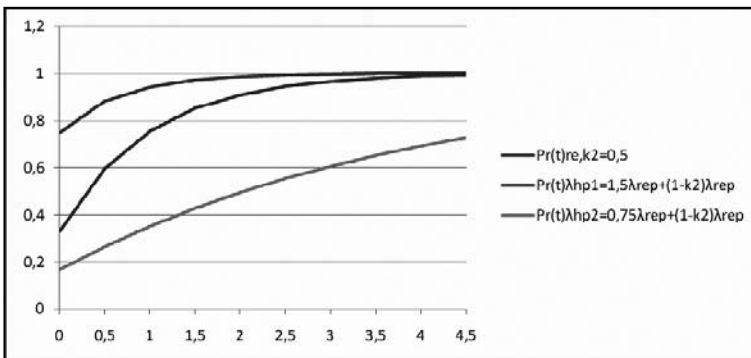
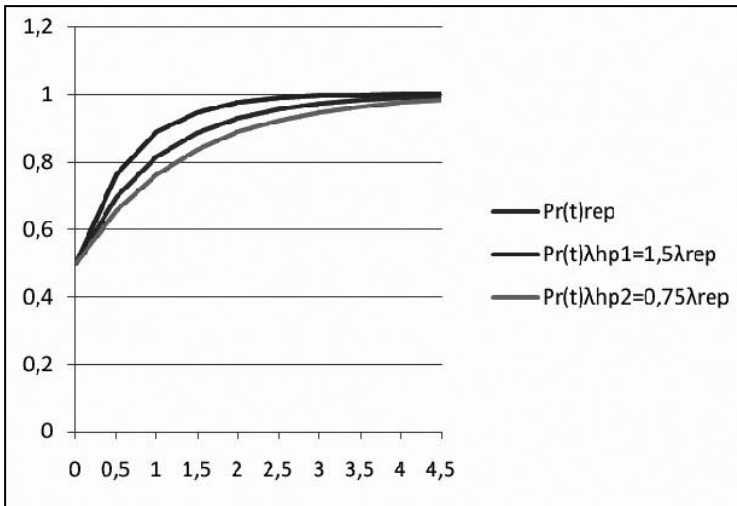
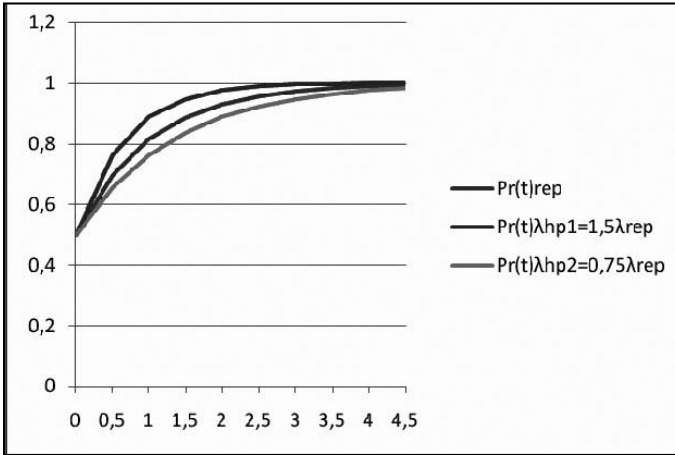
In order to analyze the integration of the registered electronic and hybrid mail systems by modelling with M/M/1 type of service system, let us observe three systems: the REM system with the parameters λ and μ , the HM 1 system whose parameters λ and μ are 50% higher than in the REM system and the HM 2 system whose parameters λ and μ are 25% lower than in the REM system. After that let us model the integration of the REM system and the HM 1 and HM 2 systems with the integration coefficient $k_2 = 0,5$. The integration coefficient shows how much customers flow is reduced, who, thanks to the integration, continue to use mail delivery through the REM system. The overview of the parameters λ , μ , k_1 and k_2 for the observed systems is given in Table 3.

Table 3: The parameters λ , μ , k_1 and k_2 for the observed REM, HM 1 and HM 2 systems

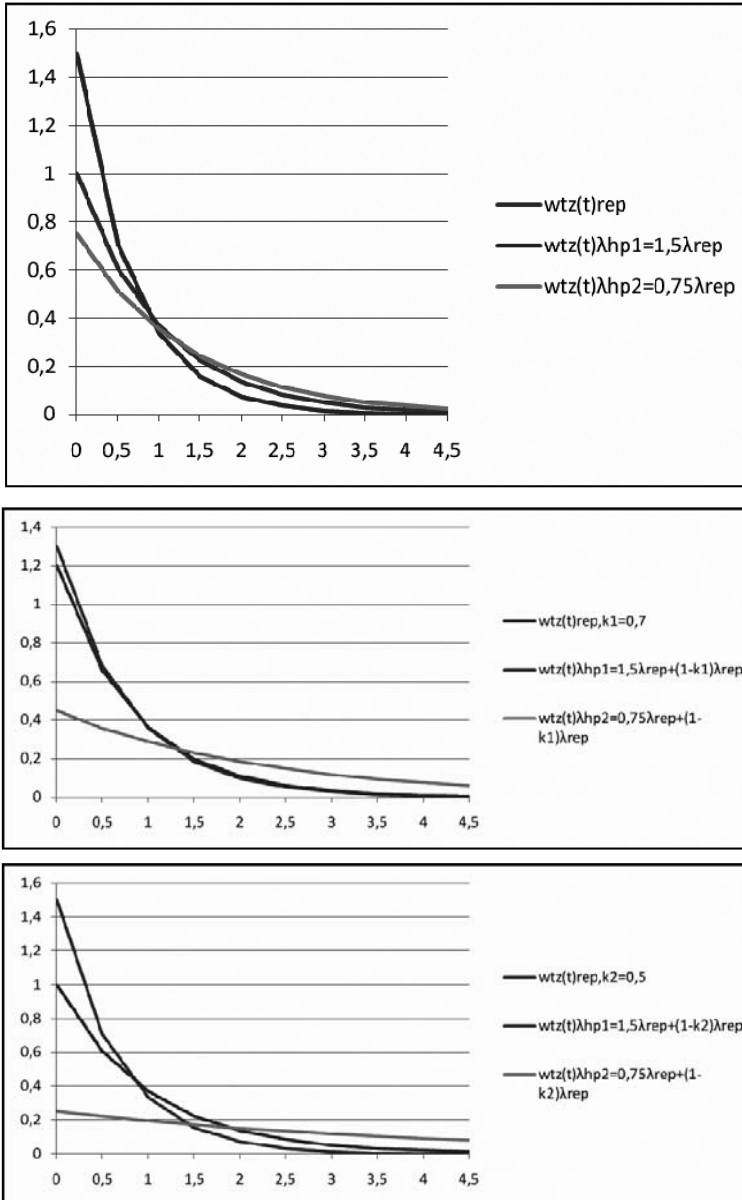
Description of the system	Characteristics of the system	λ	μ	$\rho = \lambda/\mu$	$\mu-\lambda$
REM	Relatively low traffic intensity of the system $\lambda = \mu/2$	1	2	0,5	1
HM 1	HM 1 with the parameters λ and μ 50% higher than in the REM	1,5	3	0,5	1,5
HM 2	HM 2 with the parameters λ and μ 25% lower than in the REM	0,75	1,5	0,5	0,75
REM after integration $k_1 = 0,7$	REM with a new customers flow which is due to the integration $k_1*\lambda$.	0,7	2	0,35	1,3
HM 1 after integration $k_1 = 0,7$	HM 1 with the parameters λ and μ 50% higher than in the REM and additionally increased by $(1-k_1)$ times due to the integration	1,8	3	0,6	1,2
HM 2 after integration $k_1 = 0,7$	HM 2 with the parameters λ and μ 25% lower than in the REM and additionally increased by $(1-k_1)$ times due to the integration	1,05	1,5	0,7	0,45
REM after integration $k_2=0,5$	REP with a new customers flow which is due to the integration $k_2*\lambda$	0,5	2	0,25	1,5
HM 1 after integration $k_2=0,5$	HM 1 with the parameters λ and μ 50% higher than in the REM and additionally increased by $(1-k_2)$ times due to the integration	2	3	0,66	1
HM 2 after integration $k_2=0,5$	HM 2 with the parameters λ and μ 25% lower than in the REM and additionally increased by $(1-k_2)$ times due to the integration	1,25	1,5	0,83	0,25

Picture 7 shows the function of waiting time distribution, i.e. the probability that customers waiting time in the system is less than t , $\Pr(t)$, in the case of the REM, HM 1 and HM 2 systems, as well as in the case of the system integration models with the integration coefficients k_1 and k_2 according to the parameters given in Table 3, while Picture 8 shows the corresponding function of customers queueing time $w_{qt}(t)$ in the same systems.

Picture 7: The function of waiting time distribution in the waiting room in the REM, HM 1 and HM 2 systems contingent on the value of the parameters λ and μ and integration coefficient k_1 and k_2



Picture 8: The function of customers queueing time in the REM, HM 1 and HM 2 systems contingent on the value of the parameters λ and μ and integration coefficient k_1 and k_2



Here is the interpretation of the performances of the observed REM, HM 1 and HM 2 systems determined by the values of the proposed parameters λ and μ , integration coefficient $k_1(0,7)$ and $k_2(0,5)$, and derived charts of the probability

that the time a customer has to spend waiting in the system is less than time t and the function of customers queueing time in the system:

- 1) The probability that a customer will not have to wait in the moment $t = 0$ is the same in all three individually observed systems REM, HM 1 and HM 2. This is understandable since the quotient of the parameters λ and μ is identical in all three systems and it is $\rho = 0,5$ (the first chart in Picture 7). However, as the time passes, the HM 1 system conducts the best performances, then the REM system, and in the end the HM 2 system. The probability that a customer will not have to wait in the system as the time passes is the biggest in the HM 1 system and it can be explained by the difference between the parameters λ and μ , which is exactly the biggest in the HM 1 system. Namely, since in the HM 1 system the service rate μ is bigger than the arrival rate λ unlike in other two systems, this system shows the best performances as the time passes, i.e. much more customers are processed in the system workshop than the number of customers arriving at the system.
- 2) Having the system integrated with the integration coefficient $k1(0,7)$ and $k2(0,5)$, the picture of the system changes in every aspect. The probability that a customer will not have to wait in the moment $t = 0$ is the biggest in the REM, then HM 1 and in the end HM 2 system, in proportion with the quotient of the parameters λ and μ . The system behaves relatively similarly in the case of the integration either with the coefficient $k1$ or $k2$, because in both cases relative relation of the quotients of the parameters λ and μ (ρ), remains approximate. Finally, as the time passes, the HM 2 system shows the worst performances, which anyway before the integration had the smallest difference between the parameters λ and μ , thus by the integration it has become most occupied by additional traffic of customers from the REM system.
- 3) The chart in Picture 8 confirms that before the integration the HM 1 system had the fastest reduction of customers queueing time, for the same reasons mentioned in the point 1, while the integration of the system improves most the performances of the REM system, in which the flow of arriving customers decreases because customers choose to use the HM 1, i.e. HM 2 system.

Experimenting with the service model and modelling of the processes with M/M/1 type of service system provide possibility to analyze the integrations of the registered mail and distributed hybrid mail systems and their effects. In order to model and analyze the system, let us observe the REM system and already analyzed DHM 2 and DHM 4 systems and let us apply integration coefficient $k1 = 0,7$. Picture 9 shows the function of waiting time distribution, i.e. the probability that customers waiting time in the system is less than t , $Pr(t)$, and the corresponding function of customers queueing time $wtz(t)$ for the REM, DHM 2 and DHM 4 systems, as well as for the system integration model with integration coefficient $k1$ according to the values of the parameters given in the Table 4. Here is the interpre-

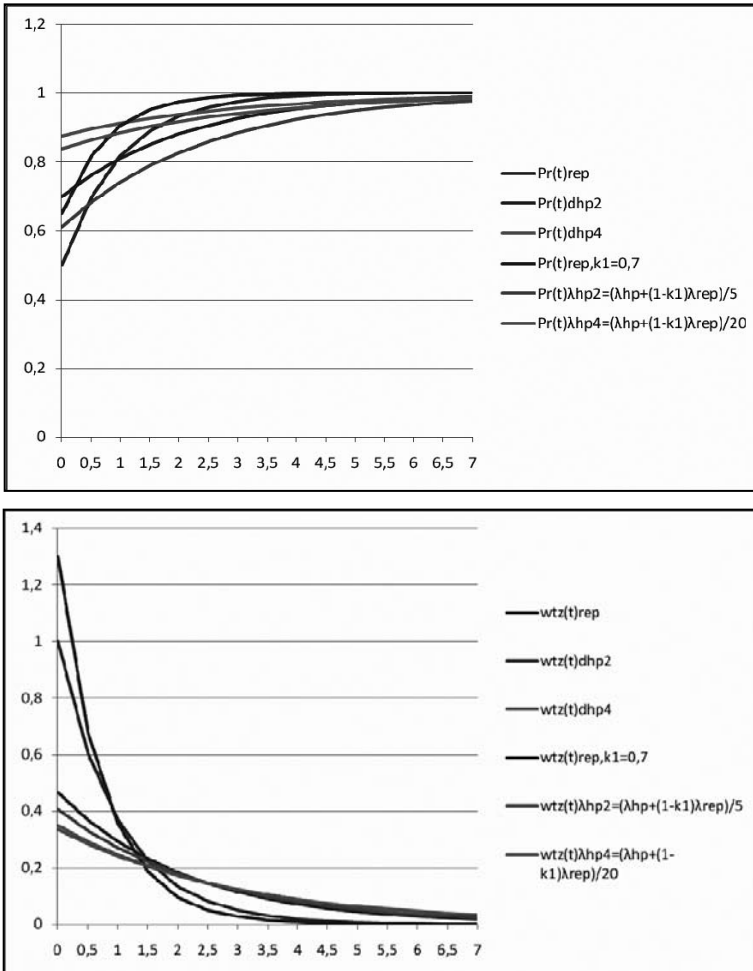
tation of the observed REM, DHM 2 and DHM 4 systems determined by the values of the proposed parameters λ and μ , integration coefficient k_1 and k_2 , and derived charts of the probability that the time a customer has to spend waiting in the system is less than time t and the function of customers queueing time in the system:

- 1) Similarly to the previous analyses, the probability that a customer will not have to wait in the moment $t = 0$ is the biggest in the DHM 4, then DHM 2 and finally REM system, in accordance with the values of the quotients of the parameters λ i μ . System integration results in improving the characteristics of the REM system and degrading the characteristics of the DHM 4 and DHM 2 systems, which is understandable since the traffic overflows from the REM system into the DHM 4 and DHM 2 systems. An interesting thing in this modelling is the fact that after the integration the performances of the DHM 4 system are dropping less than the performances of the DHM 2, which is explained by the fact that the system with more distributed centers is less affected by the increase in customer flow!
- 2) However, as the time passes, the performances of the REM system become more and more significant, so as they used to be before the integration. The explanation lies in the difference between the parameters λ and μ , which is exactly the biggest in the REM system. It means that as the time passes customers queueing time is less in these systems than in DHM systems.

Table 4: The parameters λ , μ , and k_1 for the observed REM, DHM 2 and DHM 4 systems

Description of the system	Characteristics of the system	λ	μ	$\rho = \lambda/\mu$	$\mu-\lambda$
REM	Relatively low traffic intensity of the system $\lambda = \mu/2$	1	2	0,5	1
DHM 2: 5 centers	DHM with 5 centers, arrival rate of every center is $\lambda h p/5$, and service rate is $\mu h p/3$	0,2	0,66	0,3	0,44
DHM 4: 20 centers	DHM with 20 centers, arrival rate of every center is $\lambda h p/20$, and service rate is $\mu h p/5$	0,05	0,4	0,125	0,35
REM after integration $k_1 = 0,7$	REM with a new customers flow which is due to the integration $k_1 \cdot \lambda$.	0,7	2	0,35	1,3
DHM 2: 5 centers after integration $k_1 = 0,7$	DHP with 5 centers arrival rate of every center is $\lambda h p/5$, additionally increased by $(1-k_1)/5$ times due to the integration	0,26	0,66	0,39	0,42
DHM 4: 20 centers after integration $k_1 = 0,7$	DHP with 20 centers arrival rate of every center is $\lambda h p/20$, additionally increased by $(1-k_1)/20$ times due to the integration	0,065	0,6	0,11	0,535

Picture 9: The function of waiting time distribution in the waiting room – above and the function of customers queuing time – beneath, in the REM, DHM 2 and DHM 4 systems contingent on the value of the parameters λ and μ and system integration coefficient $k1$



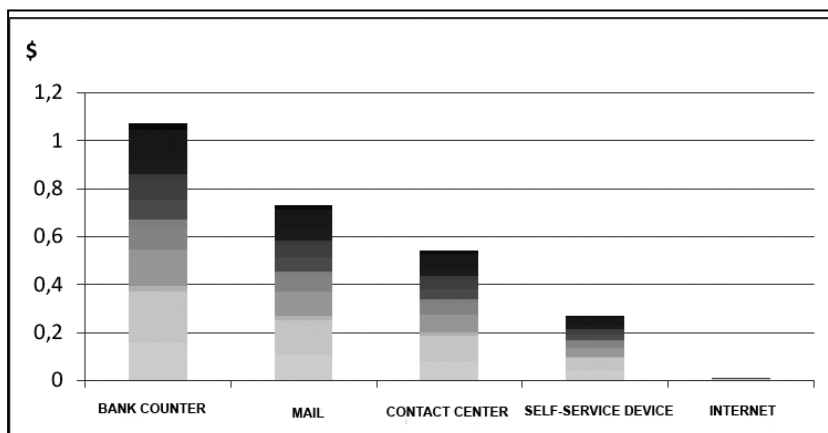
1. Finally, it can be concluded that according to the performances and characteristics of the systems, i.e. the results of the integration of the registered electronic and hybrid, that is distributed hybrid mail systems, the best integration is the one of the REM system with the DHM system that has as many distributed centers as possible. Clearly, with this integration additional inflow of customers arriving at an individual distributed center is smaller if there are more distributed centers. Furthermore, the performances of the DHM system are better after the integration if the quotient of the parameters λ and μ of an individual distributed center is bigger, i.e. if the service rate in the workshop of the distributed center is higher. Certainly,

this condition is opposite to the size of investment necessary to be implemented by the postal operator in order to develop the DHM system, thus an optimum is to be found between the number of distributed centers and their capacities of processing customer on one hand, and investment amount on the other hand.

5. Optimizing the costs of using REM and HM integrated electronic access channels

All the reasons for implementing the integrated electronic access channels of REM and HM systems are secondary to the price after the conducted transaction (**economic aspect of optimization**). For the cost optimization analysis we use the chart in Picture 10 that shows the price of one transaction (*a banking one in the given example*) that is done via the Internet or WAP service of mobile telephony, is even 97% cheaper than the transaction done in a bank subsidiary!¹⁰ This is understandable because in the case of accessing via the Internet or mobile telephony a customer is one's own liquidator, who buys and maintains his equipment (*a computer or mobile telephone*) and pays all the costs of establishing connection with a bank (*advantages of electronic business, i.e. using electronic access channels*).

Picture 10: The chart of banking transaction costs contingent on the type of electronic access channel¹¹



The relation between transaction costs done on a bank counter and via an electronic access channel, shown on the chart in Picture 10 is applied on the cost optimization of the public postal operator's operations, which accrue when using

¹⁰ V. Vasković, *Sistemi plaćanja u elektronskom poslovanju*, Fakultet organizacionih nauka, Beograd, 2007.

¹¹ V. Vasković, *Sistemi plaćanja u elektronskom poslovanju*, Fakultet organizacionih nauka, Beograd, 2007.

the integrated electronic access channels of the REM and HM systems. It has been determined that the number of letterpost mail processed (*received, processed, transported and delivered*) by JP PTT Srbija in physical, i.e. traditional form in 2010 was approximately 290 000 000, and the cost of processing one letter was approximately 25 RSD.¹² This company plans in 2011 to develop integrated REM and HM systems with conjoint electronic access channels, primarily contact center, self-service device (*ATM*) and the Internet. In order to forecast cost cutting of this operator's operations in the next five years, it is possible to assume the percentage, i.e. the number of mail that will be realized via some of the electronic access channels instead of physical form. Table 5 shows the parameters taken for this analysis of three different cases i.e. forecasts (*moderate, pessimistic and optimistic*), grounded on the data of JP PTT Srbija from 2010 (*statistically base year is 2010*).

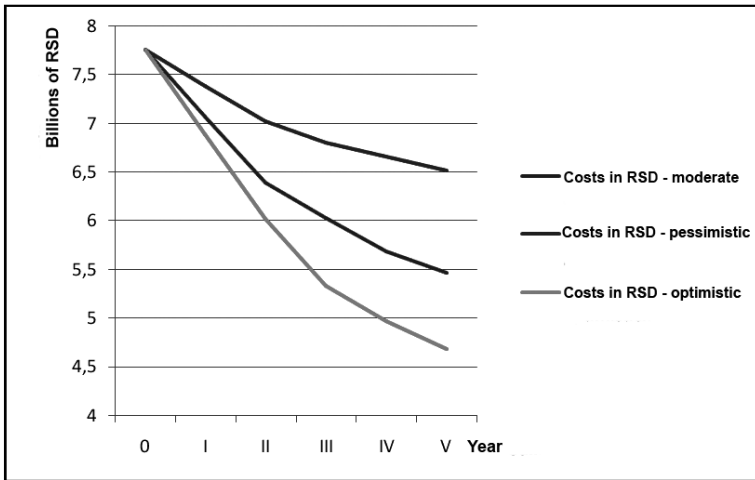
Table 5: *The percentage and number of transactions realized via integrated electronic access channels in a period of five years*

Year	I	II	III	IV	V	
Moderate forecast						
The Internet:	%	6	12	15	18	20
	Number	17 400 000	34 800 000	43 500 000	52 200 000	58 000 000
Self-service device	%	1,5	3	4	4,5	5
	Number	4 350 000	8 700 000	11 600 000	13 050 000	14 500 000
Contact center	%	3,5	7	9	11	12
	Number	10 150 000	20 300 000	26 100 000	31 900 000	34 800 000
Pessimistic forecast						
The Internet:	%	3	6	8	9	10
	Number	8 700 000	17 400 000	23 200 000	26 100 000	29 000 000
Self-service device	%	1	2	2,5	3	3,5
	Number	2 900 000	5 800 000	7 250 000	8 700 000	10 150 000
Contact center	%	2	4	5	6	7
	Number	5 800 000	11 600 000	14 500 000	17 400 000	10 300 000
Optimistic forecast						
The Internet:	%	7	14	20	23	25
	Number	20 300 000	40 600 000	58 000 000	66 700 000	72 500 000
Self-service device;	%	3	6	8	9	10
	Number	8 700 000	17 400 000	23 200 000	26 100 000	29 000 000
Contact center	%	4	8	11	13	15
	Number	11 600 000	23 200 000	31 900 000	37 700 000	43 500 000

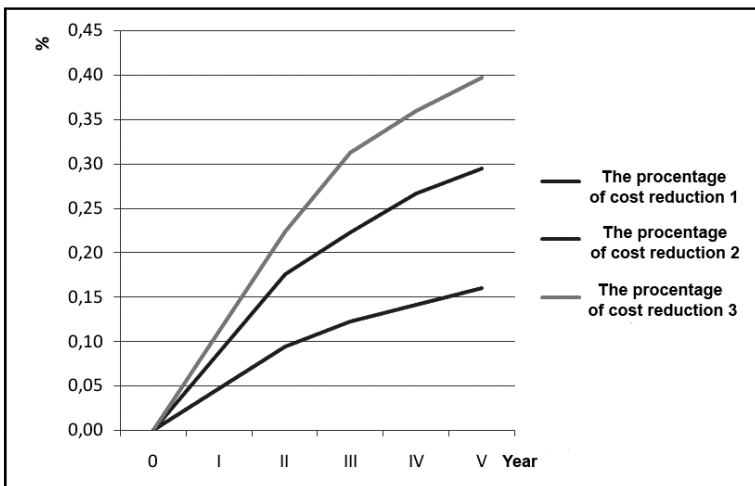
¹² Godišnji izveštaj JP PTT saobraćaja "Srbija" za 2010. godinu.

The chart in Picture 11 shows that the reduction of costs of JP PTT Srbija operations in a period of five years, depending on the forecast, goes from 1.5 to even 3.2 billion RSD. The chart in Picture 12 shows that the assumed model in a period of five years results in reduction of costs in the range from 1.5% to even 40%. Namely, according to the pessimistic forecast the percentage of transactions realized via the integrated electronic access channels results in 15 % reduction of costs, according to the optimistic forecast it results even in 40%, while the moderate forecast shows approximately 30% reduction of the operator's business costs.

Picture 11: Reduction of costs of JP PTT Srbija operations due to the usage of the integrated electronic access channels of the REM and HM systems



Picture 12: The percentage of cost reduction of the public postal operator's business due to the usage of the integrated electronic access channels of the REM and HM systems



6. Conclusion

Following the analyses given in this paper it can be concluded that for the public postal operator the integration of the registered electronic and hybrid mail system is **economically justified**. On one hand, the advantage of the hybrid mail is determined by print quality inserted into mail. On the other hand, the future of the hybrid mail is determined by growing desire of customers to receive their mail in electronic form. In that respect postal operators have to provide the integration of hybrid mail systems, so that they can offer electronic delivery through the system of registered electronic mail. **Additional savings and improvement of the characteristics** of the hybrid mail system are achieved by exploiting the distributed hybrid mail system. Developing as many distributed centers as possible a postal operator **reduces costs** of physical mail transport and time required for the mail delivery to the end user. **The best option**, in terms of the systems response, their characteristics and performances, is the **integration of the registered electronic mail system and distributed hybrid mail system**. Such an integration enables the postal operator to **increase** manyfoldly its **range of services**, and thus its **revenue**: the system integration provides simple mail reception of big customers (*“billing” type*) and physical persons (*“mailing” type*) via the integrated electronic access channels, there is a possibility of various ways of processing and keeping data i.e. mail, there is a significant **cost reduction** of planning, projecting, development, exploitation, maintaining and running universal electronic access channels and parts of the information system (subsystem for surveillance and control, and subsystem for payments). Finally, with the integration of the registered electronic and distributed hybrid mail systems, the integrated systems performances (*the function of waiting time distribution in the system waiting room and the function of customers queueing time in the system*) enable the best system response and the shortest queueing time of customers in the system, which is proved in the paper by modelling of the individual and integrated REM, HM and DHM systems with the elementary model of service system named **M/M/1** according to Kendall’s notation. **Cost optimization model** due to the usage of the integrated electronic access channels (*the Internet, self-service device and contact center*) of the REM and HM systems, applied on the range of services of JP PTT Srbija in a period of five years generates such **economic effects** that result in cost reduction of the public postal operator’s business from 15% to 40%.

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ASSISTANT PROFESSOR VLADIMIR RISTANOVIĆ, PhD
Graduate School of International Economics, Megatrend University, Belgrade

TO WHAT EXTENT DO THE CHALLENGES OF CRISIS INDICATE THE EXISTANCE OF ITS STRATEGY

An essay on the Monograph:
“The world Financial Crisis – challenges and strategies”,
by the authors Rajko Bukvic, Oskar Kovac (the editor), Branislav Pelević,
Branko Urošević and Boško Živković,
Serbian Scientific Society, Belgrade, 2011.

The monograph on current issues of the world crisis afflicting the modern world and leaving economic theory virtually powerless to offer an adequate solution represents a major step forward and a valuable contribution of our science. Having that in mind, it is a great responsibility to present the book in order not to reduce the concepts represented by the authors themselves. Even greater is the charm of being engaged in the analysis and the proposed solution to the crisis, which the authors introduce both from theoretical and practical point of view.

This book is a guide to the crisis, since it enables the reader a clearer understanding of the causes, effects and consequences of the crisis. It can be used as a guide to universal comprehension of the economic crisis phenomenon, and as such, it is intended for scientists, researchers, and even students who study international economics. It can find its purpose in the field of international business and consulting, but it may also serve as a useful reference for the economic policy makers of any economy. Clarity and ease of interpretation of such complex issues make the book accessible and easy to understand for an ordinary reader who is out of the economic discipline.

The book provides answers to key questions about where and how to recognize the impending crisis, the ways in which the crisis effects are reflected on the economy, as well as the feedback of the state on the crisis. The positions of the relevant international institutions are also emphasized, as well as their role in encouraging and rehabilitating the crisis processes. Besides theoretical analyses,

* E-mail: privrednis@privsav.rs

the book contains a plenty of real life examples that enable economies to prepare in time for the coming crisis, and to benefit from the earlier ones.

The five authors of the book have tackled the problems of the world economy, which fell into economic and financial crisis in the mid 2007, and the effects of which are manifested today. Different approaches to the same problem - the global crisis, have prompted the authors of the book to present key elements of the crisis and their focus through four parts, and point out the potential mitigation of the crisis effects, if not their removal. The book clearly points to the persistent imposition of global, i.e. universal solutions (to the majority by minority), the ever smaller scope of economic theory, the absence of perfect competition and the irrational behaviour of market participants, then the existence of asymmetry in information and moral hazard, as well as anomalies in international trade. The authors are professors of domestic universities, while some also of foreign scientific institutions, with a very prominent role in the fields of international economics and finance.

Professor Oskar Kovac's work entitled *The Causes and Alternative Methods of the Rehabilitation of the World Financial Crisis Consequences* begins with a clear positioning of the crisis problems, and then offers a solution to the rehabilitation of the crisis consequences, following the crisis effects on different markets - the EU, U.S., Asia and China. The absence of perfect markets and the irrational behaviour of market participants, as Kovac emphasizes, with a long lasting legislative procedures and rigid regulatory bodies, only deepen the crisis agony, especially in some large parts of the world economy, and then in the rest of the world. The cause of that, according to the author, lies in various pronounced interests of the key countries, especially in a situation when the centre of the world economic growth and exchange has been moved to the east. Therefore he points to the importance of the Asian countries' experience in the world crisis as a foundation in solving global economic problems.

This paper underlines the neoclassical school postulate according to which a crisis cannot occur under conditions of rational behaviour of economic entities and the perfect functioning of the market, because such imbalance is automatically removed without the need for economic policy intervention. It is obvious that the functioning of perfect market is undermined and that dominance of big monopoly capital has changed the role of the state and diminished the importance of national development strategy. The dominance of transnational companies and the segmented labour market do not make an environment in which the neoclassical model can function. Therefore, it is not surprising that there is no proper response of the neoclassical direction in economics to the global crisis.

The new business operations conditions, those of imperfect competition, according to Kovac, are convenient for big capital and oligopolies, as actors of innovation, which additionally create asymmetric information and monopolistic position in the market. Such a business environment disturbs the position

of common institutions that would make decisions in the interests of all (the majority, and not minority) and that would form political and common regulatory measures.

The author thoroughly examines the global issues and reminds us of the earlier works of Dixit and Stiglitz, while sharing the same opinion on the crisis causes with a number of contemporaries, such as Krugman and Felps. They all confirm the acceptance of a global model that is based on a non-existent economy - irrational behaviour and perfect competition. There they find the causes of the crisis for the real and financial sectors of the economy. Surprisingly, even though these crises spill over from one country to another at high speed, with enormous consequences, few lessons have been learnt so far, or almost none¹.

Past experience has confirmed the rule that the global crisis first appears in the financial market, and then spills over to the real sector of economy. Still active, the crisis started in mid 2007 in the U.S. mortgage market, but was accompanied by a series of bad decisions of the U.S. government, which believed that saving the big players in the market could help overcome the problem in the short run. However, as Kovac points out, rescuing large insolvent companies only deepened the problem in the financial market and returned like a boomerang - the systemic risk was increased. The size of these companies increased to the U.S. GDP, what only increased their level of indebtedness in relation to their assets. Problems escalated in the mortgage market so that every effort of the U.S. government in the form of bank recapitalization and fiscal stimuli of the real sector of the economy were not successful, but rather harmful - the budget deficit grew as well as the U.S. indebtedness. The state funds alone were not sufficient, while banks were reluctant to come out with an offer of favourable assets to the economy, although until recently they managed to take advantage of low interest rates and invest huge sums of money in risky assets. The strongest systems adopted a similar game and achieved secure placements in securities through the process of securitization. However, the desire to catch up with fast-growing economies (double digit growth in the east) did not allow an adequate pricing policy of financial assets from fear of slowing down the growing economic activity in the developed part of the world. This exacerbated the capital adequacy of the financial market because the ratio between costs and the approved loans (even to the companies with a low credit rating) soon led to the growth of prices of financial assets. Such trends in the financial market left no space for growth of the real sector of the economy, so that the economic activity was reduced while unemployment increased. What followed was the recession of the world economy, and we have obviously become victims of the imposed financial conditions!

¹ This is particularly pronounced in the imbalance in the real sector, where there is the opinion that the problems are accumulated in the relations of macroeconomic aggregates. In the financial sector there are more precise explanations, but not sufficiently clear or acceptable to painlessly overcome the next wave of the crisis.

The first targets of the financial crisis were international trade and FDI flows. Reduced capital flows in the world market have hit emerging market economies most. Decline in the volume of foreign direct investment in the world does not harm the developed countries (among which about 70% of FDI are exchanged), which introduce discriminatory measures while they require other countries to apply the rules of liberal economy. However, all countries are affected by the slowdown in economic activity (except for Asian countries). In the large, developed countries the growth of fiscal stimuli are expected, and consequently, the increase of public debt. On the other hand, less developed countries too face the problem of increasing public debt, the additional fiscal burden, fall of revenues, but also the pressure of short-term capital due to unbalanced exchange rate. Contrary to the application of the same recipe of the Western world – the protection of the financial sector, in Asia (primarily China) the commercial banks have stepped up lending to the economy and population, with the support of the state in financing of infrastructure investments and with the notable social benefits (improved health care, various transfer payments). The main objective was to encourage the generation of domestic demand without inflationary pressures brought on the economy. The final result is that China is still recording high economic growth rates, low corporate and individual debt, while banks have sound money on their disposal.

The consequences of such policies of developed countries - the fall in prices of financial assets, then the low yields on corporate sector bonds, short-term capital outflows from money market, investments mainly in the risk-free assets (government securities and placements in banks with high guarantees), postponing major investments, etc. , soon spilled over to developing countries. But the consequences were far less favourable - the value of financial assets abroad declined, the access to loanable funds in financial markets became more difficult and unfavourable, the inflow of FDI was reduced, exports prices fell, and there was pressure of protectionist measures in developed countries, which restricted the exporting from developing countries.

The author finds the basic causes of the global crisis in completely altered basic objectives of the relevant international institutions, the strong growth of world economy (global growth in the period 2003-2007 was 5%), unstable financial system (loose monetary policy, inadequate regulation and weak control) and cancellation of the markets functioning, but also in inadequate system of management and control of the corporate sector. Further in the text Kovac introduces us with the necessary changes in the global economy before giving possible solutions for eliminating the causes of the crisis by putting in the same the plane many key factors in the global financial market. First of all, he urges the relevant international institutions to return to their initial goals and abandon the overestimated method of quotas and the number of votes, where minorities make decisions on behalf of the majority, and according to the principle 'in one's favour,

and at the expense of others'. He also puts forward the unambiguous question whether it is possible for the concept of inter-state model of the United Nations that would go to the overall benefit to come to life - taking short-term measures to revive the real sector of the economy, stopping the growth of unemployment and poverty and long-term measures to prevent recurrence of financial and economic crisis². Thereby Kovac does not diminish the importance of the existing international institutions (such as the Bank for International Settlements or the Financial Stability Forum or the UN). Yet he suggests a change in management and decision-making, emphasizing transparency and responsibility of these and similar institutions. In order to complement the above mentioned views, Kovac adds that it is necessary to adjust the national regulatory systems in at least a minimum of common provisions, extend the scope of activities of central banks (from price stability and hypertrophied role of creditors of the final instance to the preservation of financial stability of the capital flows and the appropriate exchange rate policy), avoid the existing banking regulatory system in which large financial systems are protected like endangered species (although in the first place they present the risk, and then the burden for the global economy). And finally, he points to the necessity of adopting an overall debt restructuring mechanism for countries and harmonization of national regulations, because the existing financial deregulation, leading to globalization architecture, leaves the author in doubt that something will change in perspective.

Therefore he gives us a probable outcome, before the final proposition for crisis resolution, in which he points to the repeated practice in behaviour of large financial systems that are reluctant to approach the uncollectible liabilities of the real sector of the economy, but are willing to enter risky financial transactions with a high rate of profit, expecting the recapitalization funds of taxpayers in the event bankruptcy or liquidation. At this point, the author expresses doubt about quick resolution, primarily because of the degree of complexity of the necessary reforms and the inefficient operation of international institutions, but also because of the fact that necessary measures are not in compliance with the legitimate interests of the strongest countries in the world economy.

Kovac links the exit strategy to the immediate coordination and harmonization of economic policies of all countries, with setting appropriate regulation, as well as the supervision of financial institutions and financial markets, especially in a situation when the global crisis has opened an additional problem of control and management of the guaranteed debt (which is most prominent in the EU). Therefore he insists on the necessary acceptance of the specifics of certain regions, their characteristics and peculiarities, and accordingly on undertak-

² From this perspective, the author gives an advantage to interstate over humanitarian method of problem solving the crisis (for example the EU), emphasizing national development strategies and intergovernmental agreements. Only with the equal participation of all countries in solving global problems it is possible to found the right and proper decision.

ing adequate measures and instruments of economic policy before the universal solutions of supranational institutions.

The range of the regions through which the author tries to show the true effects of the crisis he starts from the USA, where the experts are divided when it comes to the continuation of the old or adoption of a new strategy to fight the crisis. The proponents of the strategy of further incentives, regardless of the existing debt burden, fear of the crisis deepening and a new recession, and they see the incentives of monetary policy as a solution, which would stimulate economic activity, increase tax revenues and reduce the debt burden. On the other hand, partial scientific papers and several international institutions are in favour of the exit strategy, where the emphasis is on abandoning the incentives and the normalization of monetary and fiscal policy. For the time being the dominating position is that of continuation of incentives as a justification of the current loss of GDP, rising capital costs, high unemployment rate, a fall in investment and fierce efforts to preserve the major players from collapse. The existence of megabanks in the U.S. financial system, as their product, damages the rest of the economy, because they made huge profits through high-risk investments. And to make matters even worse, with someone else's money. The illusion of high liquidity in the market without any real cover has led the U.S. to a situation that is impossible to control the financial sector, as well as manage it. By volume, the financial sector exceeds both the volume of trade and national wealth. Therefore, Kovac proposes the necessary application of Basel II regarding the harmonization of regulations among countries in order to ensure the most favourable conditions of business operations at the global level³.

According to Kovac, the focus of the global crisis is in the U.S. rather than Europe, because the network of financial institutions and the size of financial markets in Europe are far below those in America. Therefore, the EU countries, unlike other developed countries, did not rush to protect their financial sector by strong, monetary and fiscal stimuli, letting the currency downstream (towards the loss of value). On the contrary, they relied on restrictive fiscal and monetary policy, the policy of targeted inflation and control of exchange rate movements. Also, the EU was the first of all to begin the process of financial system reform - new regulatory institutions were created, as well as supervisory bodies, rating agencies, and a number of programs. The problem of initiating stimulating measures insisted on excessive approvals of loan for liquidity, which has doubled deficits in a number of EU countries in the short run. Similarly, the consequences of excessive borrowing, according to Kovac, lie in the comfortable position of many countries from the period of the beginning of European monetary union functioning, when favourable borrowing conditions appeared. Attractive borrowing terms were transferred both to the bank and the popu-

³ However the U.S. insists on the improvement of the presented Basel II regulations, which may be the cause of the extended preparation of these regulations.

lation, which according to the author, disturbed the *bank - intermediary* position due to irregular loan payment. Within the EU, Greece has the least favourable position, and is unable to service its foreign debt obligations without debt rescheduling. At the same time, the author clearly points to the problem of a lack of a unified fiscal system within the EU, but also the fact that the debt of each member country expressed in euros represents a problem of monetary union and the ECB. As there is no interest to help countries with a similar problem, and at the expense of fiscal sovereignty of other Union countries, those countries are forced to accept precisely defined obligations regarding budget planning and execution, with possible exposure to penalties in case of non-compliance with the set criteria. Kovac finds an important step towards a permanent systematic solution in the newly established Mechanism for European Financial Stability (EFSF – European Financial Stability Facility), which due to the absence of a common fiscal policy within the EU, may grow into a European Monetary Fund. At the same time, a system of economic management is being built which will examine the budgets of the member states, take into account the competitiveness of the economies and the EU as a whole, as well as guarantee discipline in the fiscal and monetary system.

On a completely different pole, a positive one, despite a strong impact of the crisis, there are countries of Asia, led in huge steps by China and India. Although the Western world has recognized the contribution of Asian countries in solving global imbalances, it tends to criticize every move of their governments. On the example of large capital investments in the infrastructure of China, the author explains the suggestive policy of the West that large investments may threaten the budgets of local authorities and prevent the regular return of loans, forgetting (intentionally or accidentally) that the positive effects of such investments on economic activity will provide not only higher budgetary income and compensation for the use of that infrastructure, but also the means for smooth servicing of debt. India has also resisted the pressure of the crisis, achieving high rates of economic growth, and together with China, it represents the engine of economic development of the Asian region. This region is characterized by an increasing number of integrations, mutual investment funds, currency swaps, trade agreements, standards and institutions. With the expansion of such initiatives, and the potential elimination of tariffs between the countries of Asian region, the U.S. will face a loss of huge market due to lack of competitiveness of products (burdened by tariffs). Therefore there are frequent verbal clashes between the U.S. and China, which mainly end with pressure on China to make unilateral adjustments in its economic policy (the appreciation of national currency, reduction of surplus, increase of spending, and reduction of savings). As relations in the economy are generally two-way, when in theoretical analysis the model of two countries is presented, then, according to Kovac, the U.S. can be expected to commit to similar corrective measures with the opposite sign in their economic

policy (depreciation of dollar, reduction of deficit, consumption reduction, and increase in savings). And the world government would be necessary if this model were to be applied to the global economy, where all would equally bear the burden and responsibility for the adjustment.

Bosko Zivkovic and Branko Urosevic are the authors of the text entitled *Information Asymmetry, Moral Hazard and Financial Crisis*. This collaborative text is a guide to the theoretical and practical basis of imperfect market functioning. At the outset, the authors clearly state that a superficial approach to the real causes of the crisis is fatal and that therefore, the crisis still represents an unexpected occurrence for economic theory. They teach us that the Keynesian concept accepts a broader scope of the factors that drive crisis processes, which justifies extensive government intervention. On the other hand, the monetarists base their concept of the crisis on the banking sector panic, reduction of the money supply and liquidity deterioration in the real sector. However, the authors remind us that crisis processes are not fully predictable by means of traditional concepts, because there are numerous phenomena with special effects (flows, volume, the intensity of individual factors' effects) which make a crisis processes nonlinear. Triggering the crisis process involves a series of alternating disturbances in the financial and real sector which multiply, generating uncertainty and risk.

Today the most common factor that also plays an important role in the creation of rational behaviour of market participants is **information asymmetry** (alt. **asymmetry of information**). Asymmetry of information, as a rule, leads to a set of market disorders, typical of all activities (economy, education, health-care, public affairs, and unavoidable finance) and often difficult to understand, because they clash with the applicable regulation in certain areas. It is typical of the crisis process that this phenomenon is strongly expressed and that it is negatively related to the crisis (negative feedback).

Information asymmetry is most pronounced in finance and is expressed in the *debtor - creditor* relation, where, for example, the debtor is in a more favourable information position in credit relation than the creditor, whereby the differences regarding their information are reflected in the objective availability of information. In addition, various objective sources of information lead to a series of reactions that have the opposite direction of expression and which deepen the differences in decision making and behaviour of market participants. This is when errors in the selection occur as well as *negative selection*. But, even so, the advantage of this concept, according to the authors of the text, is that it recognizes the flow of the crisis process and the mechanism of the impact increase.

An additional set of disorders that the asymmetry of information causes is represented by *moral hazard*⁴. A feature of this type of problem is a tendency towards riskier investments and transactions. Namely, participants in the mar-

⁴ The authors underline that moral hazard represented the trigger of the global crisis - the case of incollectable second-rate mortgage bonds.

ket in such a situation increase the likelihood of the disconnection of relation between the two parties, threatening to cause a massive disruption in the financial sector - a borrower with a risky investment jeopardizes the continuation of the loan repayment (he is threatened by bankruptcy). According to the authors, the problem does not end here, but is deepened by the so-called banking panic in the primary credit relation. The authors illustrate the problem of the primary credit relation. If the borrower decides to increase the risk level of the credit taken, all costs of such activities fall on the lender. However, the authors emphasize that the problem does not end, but rather deepens here. For, if the lender makes the transformation of deposit by a loan given, these costs are spilled to the deposit owner and panic sets in throughout the sector. Here the banking panic is largely driven by the actions of banks themselves. According to their words, in modern business, banks are less financed from private savings and more on the capital market, so in terms of negative selection they are forced to sell assets⁵. Since the costs spill between market participants at high speed, the banking sector is in such position to expand the system of deposit protection. However, the state also faces a problem because the deposit insurance is covered from public sources, which further burdens the budget. Such circumstances deepen information asymmetry and rational decisions of market participants on the basis of objectively available information, leading to the conflict of interest. On the one hand, banks facing the problems of debt collection come to a situation to sell banking assets (illiquidity, insolvency, including bankruptcy), while, on the other hand, the deposit owners extract deposits from banks because they can not reliably assess whether a bank is in trouble or not. Such activities of the banking sector reduce credit activity, and indirectly the level of investment and economic activity of the real sector of the economy. Normally, according to the authors of the text, the presence of the *debt deflation mechanism* –the reduction of general level of prices occurs due to the reduction in aggregate demand. Falling prices increase real interest rates⁶ and the burden of the debtor, and in crisis conditions the value (price) of the company shares is also reduced. Stock market indices and the level of market capitalization are exacerbated, increasing the level of financial, but also the real sector indebtedness. In financial markets, deepening of information asymmetry distorts supply and demand for financial derivatives, the value of financial indices declines, and losses accumulate. However, according to the efficient market hypothesis, it is expected that competition in the financial market will set the prices of financial derivatives **within available information**.

⁵ They emphasize, that due to asymmetric information it was impossible to accurately evaluate which banks are in unfavourable position and which banks should be avoided. Furthermore, moral hazard has imposed the withdrawal of the investors not prone to risk from the market.

⁶ The Fisher effect

The authors further emphasize that the flows of crisis processes are further deepened by the impact increase and that the disturbances spread rapidly in space and time. The reader is introduced to the (numerically expressed) values of the crises trigger and losses which are then drastically multiplied⁷. The authors also retain the view that the crisis originated in developed centres of the global financial system and that from there it spilled over to the countries of the periphery. The crisis was caused by a high credit expansion exactly in the countries that financed credit lines, mainly through imported savings⁸. Like Kovac, Zivkovic and Urosevic find the basis for the crisis emergence in the high growth rates and low interest rates in the years preceding the bubble busts. Paraphrasing Mishkin, they emphasize causing of asymmetric information and encouragement of moral hazardous behaviour. That set in motion the wheel of uncertainty, the deterioration in the balance sheets of lenders and stock indexes, and influenced the interest rates growth⁹. The first hits caused huge damage to big financial institutions that managed to put regulatory measures in their favour. But as it turned out, that happened later, and to their detriment! Namely, they started financing their portfolios with less capital¹⁰, by transferring balance sheet assets into off-balance sheet assets, through the so-called structural funding. Reduction of the necessary capital adversely affected the investment activity in the real sector of the economy, slowing down the economic growth and reducing the level of GDP. This reduced the net equity of the corporate sector, increased credit risk and increased uncertainty. And again, as a response of the financial sector there was insolvency of financial institutions. The value of assets in the balance sheets of banks was reduced, leading to a decline in the value of their capital, which forced them to sell more assets. The world economy entered into a spiral that ended with the latest in a series of relations - the minimum value of capital adequacy ratio, below which there is a delay in funding due to the massive liquidation of assets at low prices.

The spark that caused the world economic crisis was initiated by several years of investment of foreign capital in the U.S.¹¹, in government securities, mortgage deeds and the companies of the real and financial sectors of the U.S. economy. The largest influx came from the countries that wanted to sell their surplus on

⁷ The loss in the financial market with the first hit of the crisis in October 2007 amounted to 250 billion dollars, in order to rise to 26 400 billion dollars in November 2009 due to the multiplication effect. When the loss of GDP of all countries that were affected by the first hit of the crisis is considered, in November 2008 it was 4700 billion dollars.

⁸ The Centre countries absorb most of the world's income due to low risk investments, because they are assumed to have a high quality of institutions and a high degree of regulation

⁹ The interest rate growth came only in 2004 after a trend of their decrease during several years.

¹⁰ Increasing the return on invested capital.

¹¹ Besides the U.S., a large capital surpluses were directed to the financial markets the Euro zone, Great Britain and Japan.

the developed financial market with less risky arrangements - the countries with high rates of economic growth (the BRIC countries and South Korea) and those rich in oil and gas. Globally connected financial markets, with a large number of new financial instruments, which were, according to the authors, introduced without understanding the real risks they carry, rapidly spilled from one to other financial markets.

However, the authors remind us that before and during the crisis, mainly a stable monetary policy was pursued without high inflation rates, despite the sharp fall in interest rates since mid-2008. Many countries have opted for a strategy of the targeted inflation strategy, and from the fear of deflation and fall of economic activity, they targeted the above zero inflation. However, the problem arose because the monetary authorities completely neglected the level of credit risk, taking into account only the quantum of the loans offered, assuming that the level of risk of the banks to the interest rate on the market is independent. And each new question of the movement (decrease) of interest rates in the banking sector makes room for moral hazard, because financial institutions, forced to substitute assets, search higher yields or care more about adjusting the level of indebtedness, are more prone to taking excessive risks. The authors remind us here that inclination to risk is determined by the period for which institution take loans. It is clear that in the long run there is more room for adjusting the level of capital with the amount of risk taken, while in the short run this is not possible, so the tendency of taking additional risk is greater.

In the rest of the text the authors take us back to the quantum of the approved loans, in fact, to the problem reflected in the culmination of granting mortgage loans and the growing risk of collectibility of receivables on that basis¹². The biggest problems of all U.S. economy, and as it turned out, the world economy, came from the agencies that dealt with the approval of these loans. The largest of these in the U.S., 'Fannie Mea' and 'Freddie Mac' abused the position of major players and started (as the newly privatized companies) to over-invest in securities issued by other parties, knowing that the state would come to the rescue in the event of unexpected and adverse events. The same occurred in the UK and the Euro zone. Lowering the standards of lending carried out by agencies and banks, deepening moral hazard, led to a crisis of global proportions, to which the authors of the text added the regulatory bodies and the political elite.

The effects were clearly demonstrated in the real estate market as well, where the growing trend of home prices was already present. Of course, investment in construction increased, but so did the wealth of the population at the same time.

¹² In the U.S. the culmination of mortgage loans is mainly linked to the approval of bad credit lines that were given in areas with high rates of migrants, and which were comfortably transferred to other securities (the so-called process of securitization of mortgage loans) and then through the commercial banks continued to spread throughout the world. Thus, the problem was transferred to investors because banks did keep them in their balance sheets. Large investors were faced with the drop in share value.

It was a good foundation for new loans of the retail banking. There was a speculative bubble which was followed by low borrowing conditions (low interest), high demand for housing and a growing supply of loans, but also by external effects in terms of inflows of foreign capital (opportunity for high investments).

However, the biggest problem was caused by sales in the credit derivatives market (the rate of default in obligations on the loan and the rate of secured obligations by debt). According to the authors, there was multiplied value of the contracts signed in the credit derivatives market¹³ due to the unregulated market, the existence of information asymmetry and a small number of institutions operating in that market. In such circumstances, the concentration of risk was high (instead of dispersion), market participants were taking large open positions, exposure to risk was huge and possible only for big banks, and the securitization process also spread¹⁴. The information asymmetry deepened and moral hazard increased. There were cases that once securitized papers re-entered the new emission flows, especially just before the outbreak of the crisis. The contribution to the distorted and bad image of this market was also given by rating agencies, whose interest was the search for clients who they would offer and approve new loans. It often happened that, owing to oligopoly, the rating houses were only interested in getting the commission from the applicant for the ratings issuance. How much rating score was important for investors (the level of capital adequacy of financial institutions is determined), shows the fact that many companies competed to win a more privileged position and a better assessment of rating agencies - an opportunity for the spread of moral hazard! In addition, with the delay or lack of the adequate regulatory measures in this market, the problems were piling up, confidence in the institutions was gradually lost, and this caused a liquidity crisis and led the global economy to a new economic and financial crisis.

The text of Professor Branislav Pelevic, entitled *The trade Aspects of the Global Economic Crisis*, shows that the imbalance in world trade influenced to a large extent the creation of global imbalances, and that they appeared simultaneously on both the export and import side. Therefore, Pelević points to a far greater decline in international trade than the reported decline in GDP, considered individually, but also in the world as a whole. It is interesting to note, according to the author, that the flow of world trade always goes ahead of GDP, regardless of whether the local economy or the global economy recovers, or falls into recession.

¹³ From June 2001 to the second quarter of 2007 the value of contracts of the signed credit derivatives was increased from 695 billion dollars to 58 000 billion.

¹⁴ Securitization involves combining various credit derivatives to reduce credit risk and come to securities carrying the highest ratings. Basically, the debt instruments are used that support the new issue of debt instruments to provide financial resources earlier, long before the final repayment is registered in the balance sheets.

Pelević finds a reason for the more rapid trend of world trade over GDP in the different treatment and the total and value added in the calculation of GDP and total goods trade. Namely, with the evaluation of trade the 'gross principle' is applicable under which the trade calculation takes into account each product or raw material after every crossing of the border, while the calculation of GDP includes only the value added within the manufacturing process or trade chain. So that open economies are more severely hit by the crisis due to the high volume of trade, i.e. products of higher levels of processing in particular. In these economies the changes in exports are more pronounced than changes in GDP if the imported components are highly represented in the production of exports¹⁵. The author shows on an example how the export growth rate exceeds the growth rate of domestic product in a reciprocal measure in which the added value of exports participates in the formation of the domestic product.

Pelević identifies another cause of rapid decline in international trade than the drop in GDP. According to him, the crisis hit harder the demand for the sector the products of which are intended for international trade (tradables), and far less the demand for the sector the products of which are not intended for international trade (non-tradables). Therefore in the economies that have a higher share of products from the international trade contingent a greater decline in exports and a relatively modest decline in GDP were recorded. The author uses a similar logic when he makes a distinction between the exchange of durable goods and consumer goods (non-durable goods). As in previous crises, the demand for durable (expendable and investment) goods is hit more heavily by the crisis than the demand for consumer goods. Citing a number of foreign authors, Pelević shows that the decline in trade of various products groups and from different sectors is much greater than the decline of global GDP. The drop in demand is affected by various factors. With the durable goods trade is mainly conditioned by changes in demand, while in the raw materials and energy the changes in price dominate as the key factor in trade. This is particularly evident in international supply chains, where the components are the subject of cross-border trade. So in the process of vertical integration, with an interruption of one link in the chain every other link is stopped and the supply chain disturbed. Therefore there is the view that the negative multiplicative effect on the trade is much bigger than the effects on GDP. However, as the author underlines, the correction of trade with the GDP deflator reduces the difference in the amount of decline in trade and GDP, and when the impact of the change (increase) of the price of energy is included, the decline of international trade and that of GDP is almost identical.

¹⁵ The author here analyzes the rate of export growth and GDP growth rate and shows that the decline in exports compared to the decline in GDP during the crisis is most prominent with the economies whose exports are largely based on imports of components and the so-called 'process industries'.

The causes of disturbed supply chains when vertical specialization is prominent are mostly associated with the volume of trade credit. The reduced credit activity due to the crisis brought about the disturbed international supply chains too. A large burden of this disorder falls to less developed countries since in the crisis they record a significant reduction in credit activity. However, there is the opinion that the supply chains are relatively resistant to the crisis processes because, on the one hand, they include the establishment of an organized structure that is hard to break and, on the other, they are generally organized within a multinational company that has no interest for the process to be interrupted anywhere, so they come to the rescue to the weakest participants. Therefore, the author of the text points out that international supply chains are rather the crisis companion than its cause, as well as that he expects a faster recovery in relation to traditional international trends.

The link between financial crisis and world trade is presented in terms of effects caused by the crisis itself and in terms of derived crisis effects. Therefore the author sees the most obvious effects of the financial crisis in the general loss of confidence, growth of business pessimism and reluctant investment (capital and long term). Such an environment deteriorates credit conditions, increases the risk premium, and leads to increased costs of lending. On the other hand, he observes the derived effects through foreign trade. The fall in domestic demand has greatly influenced the reduction of import, while the reduced export potential and high costs of export credits contributed to the fall in decline of imports¹⁶.

In the rest of the text the author deals with the issue of growing protectionism in the period of the crisis, which has considerably slowed down the recovery of the world economy. There is increased use of both conventional protective measures as well as those which have been increasingly applied recently. The majority of developed countries are characterized by the application of various measures of non-tariff protection, while developing countries apply all instruments, but tariffs in particular as well as other import duties. Therefore protectionism is seen as an important crisis companion, which generates negative trends if the wide application of protective measures deepens. Otherwise, protectionism occurs through legal instruments of the World Trade Organization (but at higher intensity), or it is used through the disguised forms (which are harder to identify and eliminate). As the author emphasizes, in the period between 2008 and May 2010, the world economy recorded almost 700 trade measures (500 of which were of discriminatory nature), the G-20 countries covering approximately two-thirds of these¹⁷.

¹⁶ The author reminds us of several more derived crisis factors - the alteration of the exchange rate, balance of payments imbalances and stimulating anti-crisis measures of the state.

¹⁷ There are numerous protection measures applied - from the classic anti-dumping, preferential treatment of domestic firms covered by government assistance programs, to various discriminatory procedures and protectionism in disguise in the form of tax relieves and exemptions.

The application of the enhanced protection in the time of crisis can be justified by positive expectations regarding employment, income and the condition of trade balance. However, the positive effects of such policies can only be expected in the short term. Problems spill over through aggregate demand, and are prominent especially in the situations when other countries answer the grown protectionism also by protectionism. Similar effects can be expected if the state chooses to implement direct assistance or incentives to domestic sector, which developed countries are particularly prone to. Problems arise in the absence of the expected results of export growth, and due to a decrease in export demand, or the effects of an unexpected drop in imports. Therefore, as a rule, it is easier to introduce protectionist measures than to abolish them.

Opening of the market and liberalization of world trade are key elements of the enhancement of the economy, not only in terms of trade growth, but also from the viewpoint of cost reduction, better allocation of resources, increase of employment¹⁸, transfer of technology... It cannot be achieved automatically and spontaneously, but with the help of appropriate measures of economic policy.

We should not lose sight of the imbalance in current balance of all countries, since it is obvious that the deficits in one group do not cover the surpluses from other countries. It is also important to consider the nature of such an imbalance, because numerous deficits have developmental character and are not the result of faulty economic policy. Also, it is important to note the real causes of the imbalance (deficit / surplus may be the result of foreign outflow / inflow of capital) and the consequences of imbalance (deficit / surplus leads to overheated / discouraged demand). It is therefore crucial for any economy to fight against the 'false' imbalance, because only such imbalances reflect wrong allocation of resources and create anomalies in the economy. In contrast to the 'false' imbalance, the 'good' one enables economic growth and development, regardless of the balancing of partial balances and particular macroeconomic relations. Hence, as Pelević emphasizes, (re)balancing must be carried out simultaneously at the global level, and in order to avoid a repetition of the crisis. The question of interests, as well as the starting point, will be crucial in creating the economic image of the world economy also in terms of (re)balancing. There are few individuals who give more importance to adequate distribution of load balancing, rather than to the global reduction of imbalance. Therefore, the quality of the global economy does not depend only on what is absolutely expressed (im)balance, but how this balance is distributed within the world economy.

Professor Branislav Pelević at the end points to the necessity of introducing different mechanisms of macroeconomic regulation both at the national and multilateral levels. He sees constantly present uncertainty, risk aversion, fear of

¹⁸ Here the author reminds us of the controversial issue of employment and liberalization. Recent studies question whether the achieved results of stimulating measures of specific sectors have surpassed the damage suffered by the competitive sectors.

investing and refraining from spending as a delay of recovery in all countries individually, but also in the world economy as a whole.

The latest in the series of works is the one by Professor Rajko Bukvić, entitled *Transformation Crisis and the Prospects of the Serbian Economy in the Era of Globalization and Financial Crisis*. This author also reminds the reader of the fact that the latest economic and financial crisis originated from the developed world and that it is the result of international transactions of the world's richest countries, as well as that the consequences of this crisis will be far stronger and more durable than the acute phases of the crisis. He also confirms the previously established view that the burden will fall more on the less developed countries (either through higher budget deficits and higher debt level) than on developed countries (where it will mostly fall on taxpayers). We are even witnessing the situation that the developed countries disregard the laws of economics (not to mention the moral codex) and consciously shift the burden to less developed countries, either indirectly with the help of relevant international institutions, or directly, through direct intervention and control.

The most striking example of imposing the only and universal solution, the author of the text finds in the Washington Consensus¹⁹, which was accepted by the neo-liberal approach as a solution for all countries in the process of ownership transformation and seeking a higher degree of integration into the global economy. However, as a result, almost all countries are faced with long-term economic decline and the negative consequences in other spheres of economy, which, according to the author, is a result of the proposed measures, and inconsistencies in the implementation of these imposed measures. Therefore he proposes the necessary reindustrialization of all countries that have resorted to reforms as a condition of economic regeneration and a prerequisite for less likely fall into long-term crises²⁰.

However, mere resorting to reforms is not a sufficient reason, nor a condition, for one to expect results. The last crisis points exactly to the fact that quick-fix implementation of universal solutions does not give good results, especially not in the long run. It turned out that these systems are highly vulnerable despite the fact that the 'mainstream' economists predicted milder and shorter effects of the crisis. Again, as in the story with a bad end, countries in transition represent the negative results of the consequences of the wrong application of the basic assumptions of the transition process, what was indicated only by a small

¹⁹ The work was originally formulated by John Williamson in 1989, which in its original form, provided proposals of economic recovery in Latin America after the changes in the global economy during the 1980s, (the rate of dollar, the level of interest rates, debt crisis).

²⁰ Professor Bukvić finds the analogy with the Morgenthau plan for West Germany after World War II, when there was the idea that after the war West Germany should be industrially disarmed, in order to become impoverished and turned into a raw material supplement to developed economies, with the disabling of survival of the then population. Luckily for West Germany, the Marshall Plan of industrial reconstruction was accepted.

number of economists. There are still a few who suggest serious reconsideration of the fundamentals of transition processes and new solutions for the progress of these countries.

However, the neoclassical market idea of 'natural harmony' is becoming the dominant trend in economic thought. The representatives of this movement have become the main experts who obediently share the recipes of particular international institutions spreading the transitional strategy around the world. According to the author of the text the recommendations arising from the strategy are the result of the Washington Consensus^{21,22}, and have been adopted throughout the world (in addition to Latin America, the former socialist countries and certain African countries). It is interesting that the actual recommendations of the conference at which Williamson's paper was presented (1989) were designed for the moment in which the countries in the region were. The author agrees that socialist or African countries were nowhere near that position twenty years later, and that they had to accept a program based on unchanged fundamentals. It is obvious that they believed the consultants that the economic transition would occur rapidly, with a low profile crisis at the start but also quick recovery, followed by ownership and institutional transformation.

At this point, the author points to the features of the new economic order - the goal of the reforms is competitive capitalism, the neoclassical economics being the methodology, while the ideological basis is one's own interest. In these settings the role of the state disappears or is substantially changed, and the specifics of the country remain aloof. Hence, the insistence on the use of shock therapy is not surprising, (rapid liberalization, privatization and stabilization) rather than the gradualist (gradual) approach to the transformation of the economy. In addition, the Consensus recommendations are not set in the same plane. In fact, they have completely different implications for the economy. According to the author, the plane of the foreign liberalization and / or openness to FDI is in contrast with the tax reform. Therefore, he directs more attention to the consideration of the set of recommendations rather than to determining the extent to which the Consensus is good or bad.

The appalling fact for most of the countries that have adopted this concept is that they were soon forced to renounce it. They fell into additional problems and the responses of the original Consensus members were generally given in terms

²¹ The original Washington Consensus covers a large range of references, where the following issues are dealt with: (1) fiscal discipline; (2) public expenditure change of priority; (4) tax reform; (5) unique and competitive exchange rate; (6) foreign trade liberalization; (7) liberalization of FDI; (8) privatization; (9) deregulation and securing property rights.

²² The above mentioned set of recommendations of the Washington Consensus represents a serious set of measures, which neither theorists or professional community underestimate, but many of them agree that some policies lack important moments (the author of the text singles out: social equity, and institutional development).

of additions to the existing recommendations, and, as a rule, were more difficult to implement.

Serbia is still undergoing a process of transformation of the economy. Although the shock therapy was applied at the start (price liberalization, foreign trade liberalization, free movement of capital, privatization, convertibility of currencies), so far market institutions have not been created in the expected level. A market economy can not function without sound institutions, so there is no renewed production and economic growth. Instead of the promised prosperity, Serbia, like other countries of a similar fate, the fate of the Washington Consensus, faces a long-term decline in GDP, industrial production and living standard. The real sector is significantly affected by the decline of industrial production (at a level of approximately 40% compared to 1989), which is why many industries are practically extinct, unemployment and poverty have increased, and the demographics of the population is negative. The state has begun to reduce the scope of its functions, leaving meeting numerous public needs to the population, so that there is a growth of intolerance, as well as the increase of inequality and corruption.

The greatest paradox of the countries that opted for the proposed transformation of their economies is the increased level of borrowing (originating from the international institutions created by the experts??) in spite of the implemented privatization. Revenues from privatization, in the case of Serbia, and from foreign remittances, have not been utilized productively, while much of them spilled over into consumption, and of course, into import. Therefore, Serbia faces external imbalance today. Competitiveness of Serbian economy and its products is low and very unfavourable. As the author points out, even foreign exchange corrections would not be of great help to increase the export position for two reasons. On the one hand, he underlines that only redistribution among manufacturers will be achieved so that those who export most will gain most, while on the other hand, the trends in exports are not affected by the nominal but real exchange rate, and in the long run. He even adds that the high degree of harmonization of domestic prices with the exchange rate trends is inherited and that it will not significantly improve the image of Serbian exports in the short term. The foreign exchange correction can rather be expected to cause macroeconomic instability.

The basic settings of the selected route of reforms are not put into question, but there are still no results. The whole engagement of the realization of the initiated work is put on hold over the technical issue of the reforms implementation. Therefore there is no serious discussion about the state of the economy and the real effect of the global crisis. It can be seen that the Consensus recommendations (tough financial discipline and privatization with deregulation) are not sufficient to enable the growth of these countries with the support of the neo-liberal free-market platform. In fact, the IMF also recognizes that the standard

implementation of the reform settings does not give long-lasting effects, and that the institutional conditions are not enough²³.

It is necessary to adequately review all the Consensus recommendations, analyze the specifics of the economy and initiate a discussion on the concept of the Serbian economy development. Earlier considerations (Antonio Serra, 17th century) emphasized the importance of industrial production for economic growth and development and poverty reduction, so that the country, in addition to producing food for its population, needs industry as well. And today, it seems as if the competition among industrial sectors disappeared, because the development of industries in poor countries is even directly prohibited.

Bukvić concludes that inconsistency of the neoclassical model is very prominent, what is indicated by the very results of its implementation - inflation, reduced production, unemployment, foreign trade imbalance, the destruction of the welfare system, corruption. These outcomes are seen by the representatives of the neoclassical economic concepts as necessary in the process of adjustment, although the transition countries are forced to search for new paths of development and reconstruction of their economies. Therefore, the author proposes the need for reindustrialization as necessary, which will help abandon the logic of the modern capitalism (quasi capitalism) through the industrial concept of development, what he himself considers a difficult task!

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²³ The extended Washington Consensus involves: (1) corporate management; (2) fighting against corruption; (3) flexible labour market; (4) joining the WTO; (5) financial standards; (6) careful liberalisation of capital balance; (7) completely fixed or flexible exchange rate; (8) the independence of the central bank / targeted inflation; (9) the system of social protection, and (10) targeted measures for poverty reduction.

NADA JEFTENIĆ, PHD CANDIDATE*
Faculty of Music Arts, University of Belgrade

THE STATE AND CULTURE – THE STUDY OF CONTEMPORARY CULTURAL POLICY

An essay on the book

“The state and culture - the study of contemporary cultural policy”

by Vesna Djukic, PhD,

*The Institute of Theater, Film, Radio and Television of Faculty of Drama Arts,
Belgrade, 2011.*

The book “The state and culture - the study of contemporary cultural policy” by dr Vesna Djukic represents a scholarly monograph, written as a final research paper within the research project¹ “The function of art and media in European integration: Serbia 2000-2010” carried out at the Institute of Theater, Film, Radio and Television of Faculty of Drama Arts, which is also the publisher of the book. It is an original scientific contribution to the study of contemporary cultural policy, but also a unique guide in the field of cultural policy and cultural management, with clear explanations of the majority of relevant concepts in this area, as well as explanations of methods, theories and ways of successful operation in the field of cultural management and cultural policy. The author specially emphasizes the culture of Serbia and the current problems in this region, describing and explaining cultural policy models current in the European countries and the world.

The book “The state and culture - the study of contemporary cultural policy” contains five chapters, each of them dealing with one important theoretical aspect of contemporary cultural policies in Serbia, Europe and the world over the last two decades in the field of theory, history and contemporary public practical policy in Europe, contemporary cultural policy in Serbia, and the methodology of research and analysis of public practical policy.

In the first part of the book entitled “The theory of cultural policy”, the author analyzes the relationship among public practical policy, cultural manage-

* E-mail: jeftenicn@fmu.bg.ac.rs

¹ A scientific research project “The function of art and media in European integration: Serbia 2000-2010” the Institute of Theater, Film, Radio and Television of Faculty of Drama Arts, is financed by Ministry of Science and Technology of the Republic of Serbia.

ment and cultural policy. This part also gives an overview of relevant theoretical sources, theoreticians, research centers and key concepts in the field of cultural policy, as well as the level of activity and cultural policy holders. Special sections are devoted to the analysis of the cultural policy models and instruments. The author presents in detail several models of cultural policies, which are present in most countries of the world, with clearly outlined advantages and disadvantages of each of these models. Besides the state, parastatal, and liberal models of cultural policy, the analysis of the cultural policy models of transition countries is given, since Serbia is at that stage at the moment. As the main feature of this model the author underlines “heavy dependence on the old models of cultural policy and the organization of the system of institutions, on the one hand, and the dependence on the expressed demands of the democratic-minded intellectuals, turned predominantly to the issues of the nation and national culture” on the other. Dr Djukic sees a danger of the absence of essential changes due to heavy dependence as the primary risk of this model. Another risk according to her comes from the situation in which the state, “occupied” with more important problems than changing cultural policy, sets this important change aside, at all levels of cultural development. As a solution the author offers a “long-term strategic vision, which is implemented in practice by short-term tactical measures, legislation and all other available instruments and strategies of cultural policy”. The cultural policy instruments that are used in achieving the set goals are presented and explained. Organizational, economic, legal, political, ideological and value instruments are broken down into more detailed models and relations, which enables a reader to gain a full insight into this aspect of cultural policy. It is specified which of these instruments is appropriate in which situation, and the interdependence of the cultural policy instruments is described.

In the second part of the book, the author presents a retrospective of historical phases and effects of cultural development in the region, explaining the cultural policies in Serbia since the period of emergence of the Serbian state in the 19th century, when the Obrenovic dynasty was the holder of the rebirth, renewal and construction of the Serbian state, and thus of culture as well. During this period all the national institutions of culture were created while a trend of investment in culture continued during the Karadjordjevic dynasty. This was also the period of the appearance of the first laws and regulations in the field of culture, which were to be in effect for decades later. Then the author moves on to “The cultural policy of the second Yugoslavia”, i.e. to the period after the Second World War, when the communism and a one-party rule set the scene, bringing the “AGIT-PROP” with them, the tool for agitation and propaganda, whose task was to control all events in the field of culture, education, and science in the name of the party. It is clear that this was a period of the renewal of the state in all fields, including cultural. However, despite the centralized approach and the use of state cultural policy model, this period is characterized by the creation

of a wider cultural scene, which may have been repressed by censorship, which prohibited anything that could be interpreted as criticism of the regime. It is undeniable that in this period a huge number of cultural centers were established which were primarily used for literacy and education of people. The author leads us to conclude that the result was not so great. In the early seventies we see a shift in cultural policy, and the establishment of a new model: self-management. That represented a transition to the quasi-governmental model of cultural policy, which also brought about a change in the decision making process. The development of amateurism was encouraged, with the aim of developing more active relationship of people towards culture; the tax system was reformed, and as one of the characteristics of self-management, the author points out the system of "cooperative planning" as a form of long-term planning of social development. The historical overview of the development of cultural policies continues with an analysis of the situation during the rule of Slobodan Milosevic, in a country that was burdened by a civil war, sanctions, external pressures and the subsequent bombing. All that reflected negatively on the overall situation in the country, including the culture. As the main feature of this period the author sees "a discontinuity in relation to the trends in cultural policies of previous regimes, as well as a discontinuity in relation to the dominant cultural trends in Europe ...". By the adoption of a new constitution in this period the existing system of self-managing cooperative planning was abolished and the funds for culture financing were established, which fundamentally changed the organization and financing of culture. This fund, like all other state institutions of the time, was established on the principle of etatisation and state centralization, whereby the Minister of Culture was awarded a large and exclusive right to decide. This period ended with a change of regime, which began the process of transition changes from a totalitarian to a democratic society.

The third part of the book, "The innovative tools and strategies", offers theoretical explanations and practical solutions in the field of cultural management and cultural policy, like the strategy of connectivity, partnerships, decentralization and inter-governmental cooperation, inter-sectoral cooperation, cultural cooperation with the EU and their funds, as well as strategy of sustainability. The part entitled "The program and organizational competitive strategies" provides insight into the possibilities of expanding cultural market, a strategy of diversification of programs and services as well as diversification of resources. In this section the author gives an excellent overview of international organizations, conventions and recommendations, with the clarification of functioning of these organizations.

In the fourth section, "The development possibilities of contemporary cultural policy in Serbia", the author puts forward her concrete solutions and direct advice on successful action in the field of culture. After showing the development and the possibilities of movement of inter-sectoral fields of culture, the

diagnosis of the conditions and problems of cultural policy in Serbia is given. Then the author proposes recommendations for raising turbulent capacities and new system solutions in the form of detailed preparation of contemporary strategies and instruments of cultural policy. The significance of the conceptualization of long-term development of culture is clearly presented.

The last part of the book titled "The methodology of writing recommendations for cultural policy" explains how to formulate solutions to real problems of public practical policy, and how to rely on a particular system of values and put forward value arguments based on data analysis through the well-established and comprehensive analysis of the available data. The author divides the science of practical policy in two areas: the study of practical policy and the analysis of practical policy, explaining the difference between the two. In this part dr Djukic takes us through the process of creating cultural policy, citing the five stages in this process: defining the problem, i.e. setting priorities, defining objectives to be achieved, the most appropriate choice of practical policy, making a conception, implementation and monitoring of practical policy. Here we can also find an explanation of how to write effective proposals for practical policy, as well as what such a proposal should contain.

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