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BUSINESS OPPORTUNITIES IN SERBIA

The Case of the Italian Business Sector and the Role of Management Education

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Part I.

CONFERENCE ADDRESSES AND SPEECHES

Prof. Hasan HANIĆ
Dean, Belgrade Banking Academy

Your Excellency, Vice-Prime Minister, distinguished colleagues, ladies and gentlemen, it is my honor and great pleasure to welcome you on behalf of the Belgrade Banking Academy, which is one of the organizers of today's international conference "Business Opportunities in Serbia: The Case of Italian Business Sector and the Role of Management Education". Also, I would like to thank you all for accepting our invitation to participate in the Conference.

The Conference is organized as to mark the successful completion of the *Tempus* Program, which was organized by the Belgrade Banking Academy – Union University, the University of Turin Business School and the Seville University Law School. I would particularly like to greet the Vice-Prime Minister of the Republic of Serbia, Mr. Mladjan Dinkic, who, as the Minister of Economy and Regional Development, has contributed substantially to attracting foreign investments to Serbia; Prof. Dukiandijev, the International Coordinator of the *Tempus* Program; Prof. Cantino, the Dean of the Faculty of Management (SAA), University of Turin; Prof. Dutto from the Faculty of Management (SAA), University of Turin and *Tempus* Program Coordinator; Prof. Adame from the Seville University Law School; Prof. Besim Culahovic from the Sarajevo Faculty of Economy, who was one of the consultants in this Program; Dr. Botzios, the First Secretary of the Italian Embassy in Belgrade; Dr. Corsi, Director of the Italian Institute for Foreign Trade in Belgrade; Ing. De Filippis, CEO Fiat Group Automobiles, (FGA) Serbia; Dr. Miranda, Deputy President of the Executive Board, COO Banca Intesa ad Beograd; Dr. Neu, Deputy General Manager of the Fondiaria - SAI group; Mr. Rossi, CEO of *Progetti*; Dr. Canteri, Global Marketing Manager, Piemonte Agency: Centro Estero Internazionalizzazione Piemonte. I would also like to greet the media representatives.

One of the main results of the project "Business University of the New Age in Serbia: the BBA" is the development of master and MBA programs of the Belgrade Banking Academy, banking, financial and business management programs, which were devised by the Belgrade Banking Academy and the Faculty of Management (SAA), University of Turin. I am sure that the initiation of this mutual master program represents a good example of a successful cooperation between Serbian and Italian organizations, and that the implementation of this program, that is, the education of young professionals according to the highest EU standards, will contribute to further strengthening of this cooperation, as well as result in Serbia being even more attractive to foreign investors.

Prof. Dutto will present our *Tempus* Program in more details. Right now, I would like to ask Minister Dinkic to open the Conference officially.

MSc Mlađan DINKIĆ
Deputy Prime Minister and Minister of Economy and Regional Development

Dear Mr. Hanic, ladies and gentlemen, I would like to thank you for giving me the honor to open the Conference and thanks to the Belgrade Banking Academy for this extraordinary meeting. Why is this meeting so important? It is important because the practice proved that foreign direct investments make significant contribution to economic development of small countries, such as Serbia, and especially of countries that are dependent both on import and export. Practice proved that $1.0 of foreign direct investment generates on average $3.0 of economic growth, while one new job in foreign company generates 1.5 to 2 new jobs in supplier companies and services, that is, in domestic companies supplying these foreign companies. Additionally, foreign direct investments are the biggest generator of export as evidenced by the present situation. You know that financial crises has also hit Serbia and the export dropped the most in multinational foreign companies leading to drop of Serbia's total export.

In terms of Serbia's attractiveness for foreign investments, we can talk about three different periods: period before the crises, present period and forecasts on what will happen after the present crisis is over. As regards to the Government's strategy of foreign direct investment attraction before the crises broke out, we have focused ourselves on several segments. We have realized that we are a small country, with only 8 million inhabitants, that we are a small market and not many people will come here with major investments just because of the 8 million population market. We have identified our chance in being the only country in Europe with numerous free trade agreements i.e. customs free export to other markets. Therefore, we have concluded the agreements with the European Union, then, with the Russian Federation, and we are the only country in Europe which has signed the free trade agreement with both the European Union and the Russian Federation. Companies producing in Serbia can execute custom free export of their products to these markets. Another very important agreement is the regional agreement CEFTA, also on free trade, that allowed production and customs free export to all countries of the region. Serbia has signed another two free trade agreements, with Byelorussia, in this April, and with Turkey in May. We are now the country with open relations with all these countries, and companies having production in Serbia can execute custom free export to all of these markets. That is one of the strength we believe will be the mid-term strength of Serbia in regard to attraction of foreign investments.

The second, naturally, is related to improvement of the business environment. In 2005, significant tax reforms were carried out. We have realized that the previous tax system was based on high tax rates which were not paid because nobody wanted to pay taxes. Then, we decided to reverse the logic, and to lower the tax rates on production, on one side, and to generate key revenues from taxing the sales. This is how we have created the current system. We have reduced the profit tax rate to only 10%, we have exempted all investors that create more that 100 new jobs and invest more than 10 million Euros from profit tax for a period of ten years and we have taken a direction of wage tax reduction. As regards to other measures, many new laws were adopted. However, I think that there is a lot to do in that sphere in order to improve the business environment. We have established four customs free zones: Pirot, Zrenjanin, Subotica and Novi Sad. We have planned for the coming period to establish customs free zones in Kragujevac and Nis, and later in some other cities, too. It turned out that Serbia was not using the strengths of customs free zones in the best way. However, the fact that Fiat indicated that one of the strengths of coming to Serbia is the ability to work from the customs free zone in Kragujevac, is significant for the coming period. Why? If you work from the customs free zone, you do not pay VAT for imported goods, you do not pay customs fee for imported goods and that way you improve significantly the solvency of your company. Of course, this is related to export oriented companies. Also, in order to encourage foreign direct investments, we have adopted relevant decrees to establish the Serbian Investment and Export Promotion Agency and encourage foreign direct investments by providing 2,000 to 10,000 Euros incentives for each new job. We have intentionally focused ourselves in this development stage on labor intensive industries; we have intentionally set the number of new jobs as the basic criterion because, as in all transition countries, Serbia has initially had unemployment rate growth. Unemployment rate reached its peak in 2006. Afterwards, the unemployment rate in Serbia started to drop, because in 2006 we had 28.1% unemployment rate, and the end last year rate was 14.7%. That has happened in all transition countries. All transition countries had unemployment rate growth during the first 5 or 6 years as a consequence of the privatization, and then, as a consequence of foreign direct investments, before all greenfield investments, the rate started to drop. In some countries, such as Poland, rate drop was very fast. In Poland unemployment rate was halved in five years comparing to the inherited situation.

In regard to Italian investors, they will speak about the plans for the crises and the plans for after the crises. We are very satisfied with the investments and companies. According to data I have, total 800 million Euros of Italian investments have been implemented in Serbia so far. Italy is among first five investors in Serbia, and the good thing about it is that we have the trend of growth one year through another. Initially, Italian investments were mostly focused on the financial sector. You all know that we have Banca Intesa on our market, than, UniCredit and finally, Findomestic. Meanwhile, Sao Paolo merged with Banca Intesa. Share of Italian banks on Serbian market currently is 25%. In present crises, Banca Intesa proved to be, let’s say, the most solvent as within the Serbian Government’s loan subsidy program for economic activity improvement, Banca Intesa only has disbursed in the last three and a half months around 160 million of loans to businesses out of total 410 million given to all banks in Serbia. The second, in this sense, is our domestic bank, Komercijalna Banka, with 70 million Euros of disbursed loans. However, Banca Intesa demonstrated that it intends to expand on the Serbian market. These years are the years of repositioning. In the time of crises, some go down, some go up. In the end, those who were ready for the crises, manage to improve their position. I was not surprised by Banca Intesa’s decision to go aggressively now on the market by improving its placements. This world crisis is actually the banking crises. Banks which were oriented on investment banking in the previous period are having major losses now. Those banks, which were on the classis retail side and which were focused on the wide sphere of small and medium enterprises, are in much better position. Take a look. Both Intesa and Societe General, all those banks not involved in investment banking and which were not investing in “toxic” assets, are essentially driving the development in these years of crises and increase their share of the market. In the insurance sector, we have two biggest Italian insurance companies, Generali and Fondiaria. Actually, Italian insurance companies’ share of the market is 44%.

As regards to industry sector, before the arrival of Fiat, we have had mainly small and medium enterprises. This is not surprising, because the Italian economy saw development actually thanks to the small and medium enterprises. Exceptions are big companies such as Fiat and big companies in the energy sector. But, generally speaking, Italian development was based on small and medium enterprises development. Present in Serbia today are all Italian and, at the same time, European leaders in the sector of clothing production such as: Caledonia, Golden Lady with two factories in Valjevo and Loznica, Pompea, also with two factories in Brus and Zrenjanin. Also, the biggest Italian producer of child footwear, Faul Kids, has two factories. Also, Pakerson, one of the renowned Italian brands in footwear production. We also have companies from the construction material sector such Tegola Canadese which privatized our company from Kanjiza, as well as company Falconi which privatized PIK Ivanjica.

Of course, everything got a faster pace in terms of Italian investors when Fiat showed up. Now, we come to the topic of this Conference, which is the role of management in production process improvement. I will use this opportunity to present you with an example. What did we do to attract Fiat? Firstly, we have decided to support additionally three sectors we believe are the biggest sources of import presently. We have decided to support those who invest more than 200 million Euros and create more than 1000 new jobs. Then, we have decided to cover up to 25% of investment cost from the Serbian budget if the investment is the automotive sector, information technology, telecommunications and electronics. Why did we select those sectors? Because, the products of these sectors are imported to Serbia. We produce almost nothing these sectors producing except for car parts and electronic components. This is the reason why we were ready to use this to attract major investments. Fiat opted for Serbia although they were thinking about Romania. Why? Because Serbia has educated labor, technical knowledge and the operational cost comparing to other countries are competitive. Firstly, improvement of production of Punto started. When Fiat came to Zastava production capacity for Punto was 40 cars per day, i.e. available domestic knowledge in terms of car production organization was 40 cars per day. Thanks to staff training and operational processes improvement, business environment improvement, they have managed to increase that capacity to present 120 cars per day, and by September the capacity fill further grow to 200 cars per day. Therefore, quite a modest capacity will become a rather solid one. As of September, Punto production capacity in Kragujevac will be 50,000 cars per year. For the sake of example, with 3800 workers Zastava produced 9800 cars last year. This year, in only eight months it will produce at least 20,000 cars thanks to improvement of the process organization. For the first time, car producer started to earn money. Fiat-Zastava has earned 2 million Euros from Punto in the last two months. This is a profit after all wages are paid, all cost covered and everything else. For the first time, Serbian Government was in position to reduce subsidies to Zastava after 15 years having in mind the profit generated in the previous period. Naturally, primary goal of Fiat's arrival to Serbia is the launching of the new model. Last week, we have discussed this issue with the Vice President of Fiat, Mr. Altavil, and the investment will start soon and definitely in 2011 we will have a new model produced in Kragujevac. As you probably know, Fiat is one of rare car companies which will be profitable this year. Together with Porsche, Fiat will be the only profitable company. Fiat's factory in Poland produces cars in three shifts six days a week. So, it is quite clear that Kragujevac factory will be even more competitive than the one in Poland. Half a million of cars are produced in Poland in the crisis time. I am talking about the results in the year of crisis, not about normal years of operation but about the crises years. Hence, it is quite clear that with even lower production cost there are chances of to have success.

On the other hand, Fiat's arrival means arrival of suppliers. As soon as Fiat announced its arrival, some 15 or 20 suppliers, components producers have decided to find sites in Kragujevac and in the vicinity to build their component production factories. Also, Fiat is currently negotiating with and licensing around 15 domestic suppliers which will produce components firstly for Punto and later for the new model. Therefore, these are all very clear strengths of the arrival of a big investment. Chance was that this was an Italian investor.

Let me say few words on the consequences of the crises in regard to investments and what is going to happen after the crisis is gone. We have here all economists. It is not a secret anymore. If it was a surprise when the crises showed up, now it is clear that this is a banking crises that led to demand drop in the real sector. Bad placements that some banks made in the past, bankruptcy of certain banks led to creation fear among banks to issue loans. With the drop of granted loans, global world demand dropped. Global demand drop led to foreign trade drop, domestic production drop, drop of gross domestic product in all countries. Demand drop today is the main reason of the crises in the real sector. However, since the crisis started in the financial sector it will end there. Currently, developed countries are working on capital stock increase, i.e. they are clearing the bad balances of those banks which have caused the crises. When this process comes to its final stages, new loans will resume.

Of course, there is another factor adding on to the depth of this crisis. It is the fear and psychological factors- fear from uncertainty, which is natural for us humans. When there is a fear among consumers, they buy less. When there is a fear among investors, they invest less. Less investments result in even lower production and drop of the gross domestic product, and lower consumption additionally reduces demand. Remedy for this crises lies in two segments. More loans mean that banks have to start to work to raise the level of demand as much as they can. On the other hand, both consumers and investors have to be freed from this unrealistic fear. Naturally, it is understandable to have rational fear and be cautious. But, irrational fear makes the crises even more profound. American great depression was so long and profound exactly due to that irrational fear from uncertainty. When the fear disappeared, recovery started.

We have applied several measures here in Serbia. I think that they were the only applicable short-term measure as our country that was not the cause or crises but the one that was hit by it. Since we have seen that the drop in bank credits was the key of economy's insolvency, we have decided to subsidize bank credits. We wanted to simulate normal situation as much as we can. We have seen the banks raising their margins. We have seen that business can not endure that, and we have decided to subside 5% of all bank credits to reach the annual interest rate for business sector of 3%. That measure has had first positive results as the solvency started to improve. Secondly, we have seen the situation in the first quarter where the state began to default its liabilities. We have realized that the state will generate additional insolvency. Then, we have decided that the state has to service its liabilities on regular basis and by the end of the previous month we have paid all debts from previous period. This week we are paying even the old debt of around 200 million Euros to road companies created in the previous years. Naturally, these measures improve the solvency. The second measure we have undertaken was to try to exert impact on those things we can. We can not impact demand growth in Germany or Italy, but we can exert impact on certain domestic sectors. You will probably ask yourselves whether Serbia has any domestic sector. Yes, it has. They are food industry, agriculture, and civil engineering. Road construction is not dependant upon the crisis. If you give money for road construction, that is not going to have any connections with demand in Italy or demand in Germany. It has to do only with domestic economic policy. Hence, we have designed a program that will accelerate construction of domestic transportation infrastructure and just now we are finalizing the program that will start-up the high-rise construction business though demand encouragement. We will restore the subsidized bank loans for apartments, before all, for new constructions, and that way we will try to improve the demand.

We have also undertaken certain active measures on the labor market. We have seen that in this crisis and created fear employers are thinking what to do with the existing workforce let alone to think about new jobs. This is the reason why we have decided to pay the one year training period of employment for those people who just got their degrees and are jobless, and we have decided to allocate more money for public works to employ people who can not find the job. This is how we try to exert impact on employment. Finally, we have realized that the only thing of essential value we can do in crisis time, which will be beneficial for business environment improvement and for businesses, is to reduce administration and effectuate the legislative "guillotine", i.e. to eliminate unnecessary bureaucratic procedures and improve the business environment. There is no other additional measure our Government can undertake except to reduce administration firstly in the sphere of state administration (state, provincial and local levels), and to design a serious plan of rationalization of all public services, including the health care and education system. Problem here is that we have a single budget for those people, and then that money is disbursed without control, especially outside Belgrade. So, we have a lack of discipline and we have to make things organized in this sector.

Also, procedures have to be streamlined. We have streamlined the business registration process. Today, all procedures are carried out with one civil servant. We have to streamline the process of registering and un-registering employees. Today, employer has to go to three different locations to record any change in workforce: to Health Care Fund, to the National Employment Bureau and to the Pension Insurance Fund. In the time of technology, this has to be effectuated in a single place. It will be so as of this fall.

And, now something that is not going to come to our minds at all. We are not going to increase taxes, and we are not going to reduce wages and pensions, regardless of what other people say, what different professors, annalists, journalist and opposition talk about. Again, reduction of wages and pensions will result only in further contraction of demand. This is a classical mistake that Letonia made, made also by Baltic States upon the IMF recommendation. However, that was a mistake. IMF does not provide good advice always. Most of their advice is good, bus some are not. Letonia cut wages in state administration by 33%. What was the result? The result was 18% drop of gross domestic product. Not only that their Government fell, but the gross domestic product fell, and that is much more important. There is nothing new Government can do because the demand dropped. In the environment of global crisis that actually led to demand drop, you can not decrease demand additionally. If you further decrease demand you will definitely have additional drop and further pressure on demand side. Another wrongful measure would be tax increases, VAT or any other having impact on production. Tax increases would result in nothing else but pumping solvency out of economy and drowning in even more profound problems. Hence, there is not room for maneuver there. Now, you ask yourselves where the room for maneuver is. In the time of crisis, room for maneuver is to increase budget deficit, take a bit more debt and reduce administration. So, do not reduce wages but reduce the number of staff, which is actually unnecessary, and accelerate the operational process. This is what Serbia is going to do regardless of the stories circling around. Hence, the crisis will not be worse as of fall comparing to present. Fortunately, we have a low level of public debt, only 25% relative to gross domestic product. Together to foreign debt of private entities that rate is 60%. That is a far lower rate comparing to Italy, whose rate is 110% for total debt or Germany with 100%. Average rate in the European Union for this year is 100% relative to the gross domestic product. Believe it or not, average the European Union will generate in budget deficits will be 6%. Hence, average European Union country will have 6% budget deficit in this year; twice higher comparing to Maastricht criteria. The United States of America will have budget deficit of 12%, Japan 11%, Great Britain 11%. It is quite clear that people there have realized that further demand contraction would lead to additional drop of the gross domestic product.

What will happen later? I have already said that I think that global crisis started to reach peak, i.e. the bottom has been touched in the late first quarter. What does that mean? Drop was very fast and very deep. It started in the last quarter of the last year. After this year’s first quarter, we have seen stabilization at much lower level. New macro economic balance was created at much lower level as of the first quarter. Of course, recovery will take time. More clearly visible recovery will start in the last quarter of this year, and will be much more visible in the next year. I think that will be the case not only in other countries but in Serbia as well. Consequence of the crises will be the bankruptcy of companies from real sector in the whole world. Weak will go bankrupt, strong will survive. You have witnessed the destiny of the Chrysler; you have witnessed the destiny of the General Motors. But, some other such as Fiat, remained. Fortunately for Serbia, these things will take place mainly in big developed countries. Also, another consequence of the crises will be moving of certain industries from developed countries to countries with lower operational expenses. This is an absolutely sure thing, because to rationalize future cost companies will consider moving part of their facilities from their domicile locations to countries with lower operational cost. In the coming years, I see this as a chance for Serbia to attract investors with our environment of lower production cost. This is the reason why this year we have to reduce bureaucratic procedures and preserve current encouraging tax system and, possibly to make it even more attractive to attract such investors in the coming period. We have been informed on certain announcements related to moving of factories, and I believe that this process will slowly start in the second half of this year, and it will be visible during the next year.

Therefore, I believe that Serbia will get through this crisis with no major damage. I am among the people who believe in good things, but if you make the right moves and avoid mistakes. I also believe that one part of investments will spill over to Serbia from the Western Europe in the coming years.

Thank you and I wish success to this Conference.

Prof. Stefan DUKIANDJIEV
International Coordinator, TEMPUS - Belgrade Office

Dear Mr. Minister, deans, ladies and gentlemen,

It is a great honor and pleasure for me to represent Serbia, Tempus project Serbia, at the final Conference of a project which shows what kind of possibilities can be used in the European program *TEMPUS* by Serbia and other beneficiaries.

It has been a great honor and pleasure to listen to Mr. Minister's speech because it explained the connection between education and industry. Minister Dinkic said that Serbia has a great advantage and that's a large number of educated people. And this is so, however education cannot be held in the same point, it needs to be constantly advanced forward and be invested in, so as to increase the number and quality of people to keep the country's appeal.

In that sense, I'd like to say a few words about the *Tempus* project in Serbia; the Tempus project has been initiated in Serbia right after the democratic changes in 2000 and until now, for these 8 years, with the help of EU finances we succeeded to do more than 120 projects similar to the one of interest for this event.

When you hear professor Dutto's presentation of the project you will see what has been accomplished in the project and easily extrapolate from that what benefits Serbia had from the Tempus project and what were the activities similar to those undertaken in more than 120 projects.

I can only say that evaluation of the European Commission in charge of the Tempus project in Serbia has been a very positive one. The first and only criteria, as Minister Dinkic mentioned in terms of attracting investments, is strengthening the Tempus budget. Serbia is the only country which succeeded to strengthen its budget. And the reason for it is a large interest of the academic community of Serbia and successful results. The current budget for Serbia is seven million Euros per year. This gives us the opportunity to fund 15 to 20 projects every year and the amount for these projects, since we are now in the faze 3 and faze 4 - tempus 4 projects go from 500 thousand to up to million and a half.

This is information for you to understand the framework of the project, and I want to say couple of words about this particular project which has being implemented by the Belgrade Banking Academy

When our colleagues from the BBA applied for funding we have decided to support them. Why? We wanted to show to the public that private universities are esteemed as highly as public ones. That's the policy of the European Commission, the European Commission thinks that education can never get enough finances, the state cannot provide for all their needs. That's why it is important to recruit all possible resources to support development of education, science and similar fields.

We wanted to show that private universities may be successful participants of *Tempus*. But what happened was that the results went far beyond all our expectations. For instance when professor Hanic and professor Dutto come to our office, and it is normal for projects like this for people to come to talk about problems, because projects get to be demanding, involving many partners of different cultures and goals. And when professor Dutto and professor Hanic come, they talked about new projects and new ideas for working with industry with other institutions and that was really pleasant.

That's why I am saying openly that this project is a good example as to how we can use Tempus program resources for specific, concrete goals in this case for the banking program, and even more so for strengthening connection between industry and education, for serving civil society as every university may and should do.

I don't want to talk about this any longer because many interesting presentations are to follow and I'd like to extend my thanks to the colleagues who were involved in the project and I wish success to all of you.

Prof. Giuseppe DUTTO
SAA Professor and BUONA Project Coordinator

I . THE BACKGROUND OF THE PROJECT

The Economic Framework

At the time the application for a Tempus grant, one of the most important factors that was affecting the Serbian economic scene was perhaps the fact that the country embarked on transition with a ten years delay, due to the political and international situation in the 1990s. What might have looked like a severe disadvantage, however, could as well has proven to be an opportunity. The experience gained during those years by the other countries on various aspects of the process could be effectively used by Serbia, but most of all provide the opportunity to avoid the mistakes made by other countries.

Nonetheless the process towards transition in Serbia appeared to have been in a sense wavering. Transition began in Serbia in 2000 and started off at a fast pace. By the end of its first year considerable results had been achieved. However, it turned out that such a pace simply could not be sustained. Probably as a result of the "self-management" attitude the country had developed after the conflict between the domestic and the Soviet Union communism, it was difficult to detect an original, internal driving force for transition since there was no consensus among political forces on whether transition was a desirable outcome. Transition in Serbia was thus mostly unfolding under the influence of the international community, with the European Union in the forefront.

Some positive results had been achieved in the public sector. Much needed to be done in the private one. Experience has proved that it is new private companies that can sparkle the economic growth, provided they can count on a renewed institutional scenario, and on fresh, updated personal competencies. This was exactly what Serbia lacked. It was at the same time what a modern education system that is up to international standards could offer.

The National Higher Education Context In The Partner Country And How This Relates to the Project Proposal

Until the beginning of nineties in Serbia there were only state owned higher education institutions. Only at that time private higher education institutions started to appear and the growth was especially intense in last two years, when 50 such institutions were registered. At that time in Serbia there were 6 state and 6 privately owned universities.

The new "Law of Higher Education" of September 2nd 2005, brought radical changes, mainly as a result of the adhesion to the Bologna Process. Three levels of higher education studies were defined: Basic studies or studies of the first degree with 180-240 ECTS; studies of the second degree – master studies with 60-120 ECTS (depending on the number of ECTS achieved on the first degree) and Specialist studies with 60 ECTS; and the studies of the third degree – Doctoral Studies with 180 ECTS.

Many faculties had made serious preparations in anticipation of the new law. Some were already launching the third year of restructured study programmes, but a good part of others had just started with the implementation of the reform.

State VS. Private Higher Education

At the time of the application, it was possible to detect a broadening difference between state and private education in Serbia. State Universities appeared to be increasingly leaning to the "traditional" academic cliché, extremely reluctant to adopt changes that were considered the result of a "capitalist pressure". To a large extent education was delivered by professors that were still hanging on to old models both in terms of content and of methodology. Efficiency was quite low. Average time for completing the studies was around 8 years, and only one in fifteen Master students completed studies on schedule. Student/professor ratio is over 100:1. Curriculum was often redundant and obsolete.

Private universities once used to be a comfortable shelter for "rich" people. In 2007 some of this still persisted, but it could be said that by and large private institutions were trying to achieve a competitive advantage in terms of studying efficiency and of more adequate programs. Unfortunately such an advantage could not be exploited as a result of an inadequate number of teaching staff and most of all of funds given that these institutions were financed only by tuition fees. The available opportunities therefore quite often could not be caught. For that reason, among many others, it was necessary that private universities, which are in their nature more flexible, faster in reacting, be provided support from competent Higher Education Institutions in Europe. This cooperation appeared to be mostly necessary in the area of master and specialist studies, where number of students was expected to grow fast as a result of the enrolment under the new "Law of Higher Education".

II. THE CONSORTIUM

The **Faculty for Banking, Insurance and Finances of the Belgrade Banking Academy (BBA**), was designated to be the partner country beneficiary institution. It was and still is an outstanding institution of the private sector, established on December 28th, 2004 by three prominent Serbian Institutions, the Atlas Bank, the Kopaonic Osiguranje and the Institute of Economic Sciences.

The Faculty is a co-founder and member of the Belgrade "Union" University (established in June 2005) one of the six accredited private universities in Serbia, comprising 8 faculties ranging from Industrial management to the law faculty, with approximately 1900 students and 112 teaching staff. BBA is recognised to be the one of the most prominent higher education institutions in Serbia and the most prestigious in the field of financial and banking related disciplines. This was the result of a highly competent and motivated staff and of the adoption of programs of the leading world universities for banking, insurance and finance, analytical skills development based on the highest academic standards that are supported by a Faculty Council.

Strong cooperation was already established at that time with a series of high ranking institutions such as NASD of USA, ERENET, the Oracle Academy and IBM Academic Initiative. This was an additional proof that the vision BBA had adopted from the very beginning was aimed at achieving high and updated standards of education in line with the market economy and clients' requirements.

As of the date of the application, BBA, as a private institution, was funded exclusively out of tuitions. The average acceptance rate for undergraduate studies was about 40%.

As a result of its adhesion to the Bologna process, two educational products were offered as of 2007, a three years undergraduate studies program of the first degree (240 ECTS), and a two years Master studies program of the second degree (120 ECTS). Given the early stages of the implementation of the University law, the first master that was launched was that on Investment banking

The **Scuola di Amministrazione Aziendale, (SAA), the School of Management of the University of Turin (Italy)**, was designated to be the contracting and co-ordinating institution of the project. It had matured a vast experience in MBA Curricular programmes in several similar projects (listed below). Assistance in the project implementation was expected to be provided by drawing on a vast and qualified reservoir of full, associate, assistant professors, a wide network of contacts with Italian and foreign financial institutions, a specialised library with hundreds of titles in English.

In particular, it is worth mentioning that SAA was one of the first Italian institutions to launch in 1978, a Master in Business Administration (MBA) through a program that integrates university methodologies with exposure to company's experience in line with the present needs of the stakeholders.

SAA acts in the international dimension, through the International Relations Department (IRD) that was created to manage the SAA participation in international projects. The IRD has been involved in several EU funded programmes, such as TACIS, TEMPUS, Alfa, EU-India Economic Cross Cultural Programme and by the European Social Fund. All projects mentioned below concern the development of curricula and/or the training of trainers in the beneficiary institutions. In all these projects, SAA played or is playing the role of the consortium leader.

- TACIS Civil Society Development Programme (CSDP) – Institutional Twinning Component – BELARUS: the Curriculum Development for MBA in Management.
- TEMPUS TACIS Multilevel Management Capacity Improvement" – Grodno (BELARUS),
- TACIS EDUK9603 - "Support to the Lviv Institute of Management (LIM)" – Lviv (Ukraine), to support sustainable economic development through the strengthening of business and management training and consultancy capacity.
- TEMPUS TACIS - Russian Federation "Restructuring the VSUES International Curriculum" – VLADIVOSTOK
- TEMPUS TACIS - Russian Federation "Establishing the ISU (Independent Siberian University) Business Department" – NOVOSIBIRSK
- TEMPUS Phare – Slovenia "Establishment of an International Division at GEA College of Entrepreneurship (GCE).
- TEMPUS CARDS – Bosnia-Herzegovina "Upgrading the University of Sarajevo MBA to International standards" SARAJEVO
- TEMPUS Meda - "Microfinance at the University)" - Arab countries

The **University of Seville Law School (UDS)** agreed to be the second European partner. SAA and UDS are tied by an excellent and fruitful experience of co-operation in Vladivostok (RF), Sarajevo and also in Ulan Bator (Mongolia) where UDS acted as project coordinator. UDS has a well rooted record of international co-operation, with staff ready to participate in cross-cultural programmes, and it is particularly strong in quality management, complementing SAA in the transfer of know how to the beneficiary partners.

Founded in 1502, it is today recognised as one of the best in the country. It has, among its faculty former Presidents of Government, Presidents of Parliament, Ministers, domestic Supreme and Constitutional Courts, alongside with internationally recognised experts in many fields, like civil law administrative law and agricultural law, real estate and commercial law. The University has a vast experience in international co-operation. It is currently managing several European Projects, and its European Centre has been recognised by the European Commission as a Centre of Excellence. It has also coordinated the Ener Iure Project, concerning the harmonisation of the European legislation related to renewable energies, whose contents will benefit the current proposal. The UDS Law School has been the EU partner of SAA in the TEMPUS-TACIS project "Restructuring the VSUE International Curriculum", and "Upgrading the University of Sarajevo MBA to International standards", which are very similar to the one considered.

III. THE PROJECT' OBJECTIVES

The project focused on the Business administration subject area, since it was aimed at Upgrading Serbian private sector MBA to EU standards through the Belgrade Banking Academy (BBA).

The wider objective was identified in the establishment and promotion of closer links among private sector Universities as a driver of a process aimed at achieving a «Centre of Excellence» in the higher education system of Serbia.

The specific objectives to be achieved within the duration of the project were identified to be:

- Upgrading the Belgrade Banking Academy's MBA to international standards;

- Fostering quality control procedures in order to enhance the ECTS system;

- Creating a network for dissemination of knowledge in the higher education system of the country

Such objectives stemmed from the needs analysis that highlighted a series of factors that were supportive not only of the needs of establishing a superior system of higher education in Serbia, but also of providing the cooperation that was necessary on the studies of the second degree (master and specialist studies), where fast growth of students was expected.

The needs analysis emphasized how Serbian State Universities were still biased by to the "traditional" academic cliché, and reluctant to adopt changes that were considered the result of a "capitalist pressure". To a large extent they still seemed to stick to the old paradigms of the past that were obviously unfit to meet the needs of an economy in transition. The perceived attitude was that of their being the depository of knowledge and truth, with negligible attention devoted to the changing needs of stakeholders.

On the other hand, private universities appeared eager and willing to undertake the new course, but were hampered by the lack of adequate staff and by limited resources. For that reason, among many others, it appeared necessary that private faculties/universities, which are in their nature more flexible, faster in reacting, be provided with the support from competent higher education institutions in Europe. This cooperation appeared mostly necessary in the area of master and specialist studies, where number of students was expected to grow fast as a result of the enrolment under the new "Law of Higher Education"

The support provided to BBA, a leading higher education institution, was expected to be a decisive step that would allow the target University not only to strengthen itself, but also to venture outside of its unchallenged niche in the area of finance and insurance. The acquisition of the competencies that are typical of an MBA program was expected to enable BBA to properly train a new generation of students capable of meeting the needs of this crucial stage of transition.

Such need, in order to be sustainable, requested the support of high standards of quality and control procedures and of a strong implementation of the new developments in the ECTS system as a means to further the process of international recognition and to support the commitment to the achievement of high standards of education.

More important, however, was the fact that BBA had committed itself to share the acquired skills and competencies with a number of Serbian higher education institutions. If this were to happen, as we had every reason to believe, we could have been entitled to say that a major contribution was to be achieved from the project, i.e. the upgrading of the standard of education in the higher education institutions of the private sector. We were confident that this would have positive effects on the entire education system of the country: competition from the private sector would exercise a positive impact in accelerating the much needed changes inside the public sector, as shown by the Central European experience of the last 15 years.

In summary great emphasis was attributed to the reorganisation of the structure, and of the courses content of the MBA of the Belgrade Banking Academy (BBA). This explained why great emphasis was placed on upgrading the MBA of BBA in terms of curriculum, courses, syllabi, and didactic material. Special attention was given to the development of courses that were particularly relevant for the contemporary Serbia.

Improvement of the quality control procedures and adhesion to the ECTS system was expected in order to ensure a better quality in the target institution and to facilitate the process of international recognition.

Having achieved these goals, the BBA could have been in the position of establishing itself as a reference point and a standard for the wide universe of private Universities that for the reasons explained above were just in the stage of establishing themselves and/or are offering an education that is below the standard.

We were aware that we were submitting a very ambitious project, but we were confident that about our determination to achieve positive results.

IV . THE IMPLEMENTATION OF THE PROJECT

The design that was supporting our proposal together with a very detailed work plan that contained the actions (organised in 11 outcomes) to be undertaken in order to guarantee its achievement was accepted.

Our attention at this point must turn to the implementation of the project that has been the faithful enforcement of the originally submitted work plan. The only significant and unforeseen event non included in the application will be analysed separately

Outcome N° 1: *CURRICULUM DEVELOPMENT*

The goal of the outcome has been to produce a curriculum for the MBA in line with international standards but also attentive to the specific needs emerging in the country.

This has been a very sensitive and important outcome, considering that it was meant to allow BBA to diversify its portfolio of products by venturing outside of its traditional home turf of banking and insurance. General management disciplines such as marketing, human resources management, managerial planning and control, leadership, decision processes strategic management were to be included in curriculum.

Great attention and care has been therefore devoted to the development of a curriculum capable of responding

a) to the requirement of the national legislation an that would allow the students to earn a Serbian diploma. In other words, a curriculum that could pass the test provided by the Ministry of Education for the release of the accreditation; and

b) to the needs of the national and international stakeholders. In other words a curriculum capable of responding to the needs of stakeholders, in order to guarantee the sustainability of the program.

At the initial stage, the task was carried out by the project coordinator, and by the contact persons of the partner country and of the 2° European University who reviewed the existing master curriculum, syllabi and courses, discussed the various alternatives through the Internet. In order to insure the responsiveness of the Curriculum to the country’s needs, research on the market of business education and business training was carried out

The draft of the findings and of the proposed curriculum was submitted the Steering Committee through the Editorial Board. The resulting curriculum was approved at the Steering Committee of June 2008. It is analysed in the report by Prof. Zvonko Brnjas.

Outcome N° 2: 12 UPDATED MANAGEMENT COURSES

The development of the teaching material (lecture notes and case studies) for the courses that were foreseen by the new curriculum have been carried out in a staged activity by 12 teams each made up by one Serbian and one Italian professor.

The relevance of this process has been considered central all along in the implementation of the programme, since it was believed that only through the delivery of a package of education that was at the same time comprehensive, consistent, up to the most recent pedagogical standards and capable of responding to the needs of the stakeholder it would be possible to provide BBA a competitive hedge capable of supporting the product's sustainability.

Each teams was requested to follow a process that started with the analysis of the textbooks to be used the respective courses. Attention had to be devoted to the quality of the proposed textbook, its availability in Serbia and the financial burden.

Each Serbian professor was to produce a tentative outline of the syllabus, to be discussed with the Italian mentor over the email.

Each Serbian professor would then travel to Turin for a visit to SAA in order to finalize with his/her mentor the syllabus and to complete the preparation of the teaching material for the courses. Two additional and important results were achieved with these visits. One was the possibility to familiarise with the presents western pedagogical approach, which is growingly drifting away from the traditional one way method of delivering education. The other was the opportunity of an exposure to a different social economic and cultural environment, that in par contributed to overcome the isolation factor.

Thanks to a cost effective process in the management of the project, one additional professor relative to what foreseen by the application was able to travel to Italy,

Outcome N° 3: QUALITY ASSURING PROCEDURES IMPLEMENTED AT BBA

The purpose of this outcome has been the designing a system of quality control aimed at insuring the maintenance of quality standards consistent with the scheme of DG XII at the BBA. This is an important step aimed at establishing teaching standards that would make the participation to the ECTS system possible.

The process foreseen for this outcome has envisaged the whole process from the acceptance of students into the MBA until their granting of the diploma. It has permanent for teachers.

The development of a system of teachers' assessment and students' evaluation has been first step in the establishment of the quality ensuring body at the MBA. One professors of the University of Seville drafted a methodology for teachers assessment taking into consideration assessment of teachers by students, implementation of a consistent system for grading students, assessment by peer groups, assessment by outside experts and assessment by the professional success of students (assessment by the market).

The draft has been intensively discussed by MBA professors and students. The results of the review have been reported to the European partner that will be in charge of the redrafting, and have been approved by the Quality Control Committee (QCC) that will be responsible for the implementation of the finalised method of assessment and evaluation procedures.

Finally a Quality Management Handbook has been developed and adopted paying specific attention to the specific needs and requirements of the Serbian environment.

Retraining of two professors in this field has be carried out at UDS.

Outcome N° 4: IMPLEMENTING ECTS AS A NEW METHODOLOGY

A full outcome of the project was devoted to the adaptation of the curriculum and the methodology of the new courses at the beneficiary institution to European Credit Transfer and Accumulation System (ECTS). Serbia is part of the European Higher Education Area that implements the Bologna process since 2003, when it joined the Berlin Conference, and therefore there is national commitment to fulfil the goals by 2010.

This commitment is two folded. On one hand, each country has to adopt legislation to reorganize its High Education System, and this was implemented on September 2nd 2005 when the new "Law of Higher Education" was enacted. On the other hand, each University has to prepare a convergence plan following the EU guidelines.

The project has provided support for the beneficiary institution in the preparation of the plan of convergence as a process. The first thing to has been the celebration of a Work-shop in place, to target the maximum amount of local professors possible at the smallest cost, in which the EU expert explained the details and technicalities of ECTS.

ECTS was set up initially for credit transfer. The system facilitated the recognition of periods of study abroad and thus enhanced the quality and volume of student mobility in Europe. Unfortunately many professors still identified ECTS only with this first idea. But the most important one is the second. In fact, ECTS is developing into an accumulation system to be implemented at institutional, regional, national and European level. This is one of the key objectives of the Bologna Declaration of June 1999 Student workload in ECTS consists of the time required to complete all planned learning activities such as attending lectures, seminars, independent and private study, preparation of projects and examinations.

All this things have to be carefully explained to professors, so that they realise the full implications of it. Credits in ECTS can only be obtained after successful completion of the work required and appropriate assessment of the learning outcomes achieved. Learning outcomes are sets of competences, expressing what the student will know, understand or be able to do after completion of a process of learning, long or short.

The proposal was also aimed at explaining some of the documents that are normally used in ECTS, like the learning agreement, the transcript of records, the diploma supplement.

Having shown the real idea of ECTS, the implementation has moved on to the preparation of a serious proposal of convergence, and to the general adaptation of the current situation, not only in number of hours, but also in broader methodological terms. This work has been done jointly by one UDS expert and by7 professors from the beneficiary institution.

The outcome provided for one BBA professor travelling to Seville to be exposed to best practices in western institutions.

Outcome N° 5: EXCHANGE WITH UNIVERSITIES

The purpose of this outcome has been that of providing the opportunity to professors of all consortium members and to students of the beneficiary institution to be exposed to different economic, social, and educational environments and to learn from that.

In the case of professors, this meant participation to lecturing, seminars and workshops at the partner Universities. Four professors were taken from the EU partners to Belgrade, and two professors from Belgrade to Seville and two to Turin respectively.

Three BBA students were provided with the opportunity to visit Italy for a three months study period to attend courses held in English at the MBA programme of SAA

These exchanges have proven to be most beneficial and satisfactory, and has contributed to in part alleviate the effects of the isolation syndrome.

The experience of the students deservers a special note. These young and smart people seem to be most eager to positively investigate different horizons. They usually emerge enthusiastic from the experience, and most often become the best ambassadors of the program with their peers and within the educational environment of their country.

Outcome N° 6: EQUIPMENT

The outcome was intended to provide the equipment required for the implementation of the project, namely Outcome N° 2 (12 updated management courses developed) and N° 7 (Project website and upgrading the BBA website). Finally it has provided resources for the purchase of equipment for the upgrading of the information and processing system supporting the postgraduate studies with the purchase of PCs and notebooks, laser printers monitors, servers and routers

Outcome N° 7: PROJECT WEBSITE AND UPGRADING BBA WEBSITE

The project website has been developed and has become a powerful tool to disseminate the results of the project and to strengthen the relationship among partners.

It has become a point of reference where all the material developed and all the information about the project itself has been made available for downloading, making it easier to have an higher international visibility (business community, public administration, other national and international universities) both for the project and for the institutions partner.

The web site is available under the web site of SAA at www.saa.unito.it .

Outcome N° 8: DISSEMINATION

As mentioned above, the project pursued the goal of providing support to BBA in upgrading its MBA, but also has the ambition to sustain the private higher education sector in Serbia in order to:

a) upgrade its profile that as a result of a dynamic and somewhat unmonitored growth is at present at a substandard level; and

b) introduce as a result a new element of competitiveness in the higher education sector, a shock therapy that could force the public sector universities to face the new features of a rapidly changing world.

These results have been pursued through dissemination, that as a result was designated from the beginning to play a fundamental role in the project. This is proven by the fact that BBA had already established working contacts at the time of the application with significant higher education institutions of Serbia that had manifested their interest in sharing the transfer of knowledge as acquired by BBA.

The dissemination partners have been contacted at the very early stages of the project in order to keep them informed of the goals of the dissemination activities and of the benefits they can gain as a result of them. These meetings have enabled the project experts to gain further in depth knowledge about the dissemination partners specific needs.

In the second project year, as material developed under outcome # 2 (12 updated management courses) # 3 (quality assuring procedures implemented at BBA), # 4 (ECTS system implemented) have become available, the process of redesigning such material has started.

The Project’s web site has proven to be an effective channel of communication to this purpose, and has contributed to a fruitful interaction among the parties involved.

An important element of the outcome has been a series of workshops in significant areas of Serbia to inform the education and the business community about the project’s aims and results. The final workshop that we are holding today as a final event of the project in conjunction with the outcome # 10 (Sustainability) is expected to produce considerable results for this purpose.

Outcome N° 9: SUSTAINABILITY

At the close of the project we can state our strong confidence that there are strong prospect of sustainability.

Support provided to BBA is in line with the established guidelines and the recognized mission of the MBA, a product that goes beyond the “academic” approach to respond to the concrete issues that managers of the business community and of the public administration must face.

EU funding has enabled the MBA of the BBA to reach out of the present elitist niche and to address a broader segment of the education market that in turn is addressing relevant needs for the contemporary Serbia. It is therefore believed that BBA has been able to develop a competitive edge in the sector of Management Training in the region, and that BBA can establish itself as a reference point not only for the private sector higher education institutions, but the whole sector of postgraduate studies in the country.

This is important, since students are showing great dissatisfaction with old fashioned, academically oriented education. A business oriented approach addressing the needs of the job market and delivered with updated teaching methodologies will undoubtedly increase enrolment, contributing to the financial sustainability of the program.

To overcome the risk of an education that is divorced from the real needs of the end-users, is imperative for BBA to continue its close monitoring of such needs, and to engage into image building, promotional process that will be relevant to support practical placements and projects as well as job opportunities.

This is what has been done during the life of the project with an ongoing analysis of the training needs of regional managers, the creation of image of the MBA in official and business circles by holding seminars, inviting local authorities and business community, and in agreements between the MBA and local administration and companies concerning education and training of managers and consulting.

The highlight of this "external" dissemination as mentioned before is today's Conference to facilitate a broad recognition on the achieved results by the country's stakeholders. I believe that we have been able to achieve what we had in mind when the project started.

It is important at this point that we at least spend a few words on an event that was not originally foreseen in the application and was brought to our attention by the Tempus people who correctly advised us to put into action a prototype of the MBA before the end of the programme as a proof of sustainability. We are grateful to the Tempus people for the challenge that we have accepted with a strong determination.

The result is the cooperation agreement signed by the Rectors of the Turin university and of the Union university of Belgrade on behalf of SAA and BBA respectively that will allow the students of the MBA who have completed their studies to earns a double diploma issued by each universities.

I know that Prof Brnjas will tell you the all story about the implementation of the double diploma that was launched on Nov 14, 2998.

I will limit my comment to underline the quality certification that such agreement implicitly contains, as well as the strong marketing appeal, two factors that are going to play a decisive role in support of sustainability.

Outcome N° 10: QUALITY CONTROL AND MONITORING

Quality has been addressed at two levels. The first was meant to define a system of quality assuring procedures, consistent with the scheme of DG XII, that would rule the MBA, the product resulting from the implementation of the programme, This was described under Outcome 3.

The second was intended to set up a system of quality control and monitoring procedures that would guarantee the e most effective and correct management of the programme itself.

For this reason a series of committees was established at the very inception of the project to insure monitoring and control.

The Steering Committee, consisting of the deans of SAA and BBA and by the deputy rector of UDS was set up to be the highest authority of the Project, responsible for the general monitoring and cross contacting with relevant projects bodies, operating as the entity of last resort for any eventual conflict that might arise.

The Editorial Board (EB), was attributed the responsibility of assuring the maintenance of a consistent and adequate academic level for all written material produced in the project. Special attention was also be devoted to the needs of establishing a system that would favour the participation of the partner country institutions to the ECTS system as a means of achieving academic recognition. The findings of the EB were submitted for approval to the Steering Committee.

The Quality Control Committee (QCC), lead by the Project Coordinator and by one representative each of the Partner country institution and of the second European partner was assigned the responsibility of overall monitoring of quality over the entire programme. QCC has reported its findings to the Steering Committee twice as year.

The Equipment Committee (EC) was established to undertaking an analysis of equipment needs required for an updated information and processing system, of submitting the needs assessment with the relevant financial breakdown and a detailed plan for procurement and installation of the equipment. It was also responsible for monitoring the proper use of equipment, for evaluating any advisable change over the original plan for procurement, and for submitting reports to the Steering Committee on a semester basis on the main areas of its responsibilities.

The Human Resources Committee (HRC) has operated to oversee the selection of teaching/ and administrative staff and of the students involved in mobility as well as to monitor their performance.

This has been done through a combination of interviews, of self-assessment, of assessment by peer groups, by students, by outside experts, and through the evaluation of the professional success of students (assessment by the market).

The selection criteria that have been taken into consideration have been: Motivation; Capability of interacting with the business environment; Capability to work as a team; Age; Potential with participating institution; Loyalty to the programme as shown for the teachers by the commitment to work for the Participating Institutions for at least three years after the completion of the programme; Foreign Language; Academic standing; Areas of specialisation.

The plan for the project's operations was agreed

Basic criteria for quality assessment

The following quality criteria have been implemented as parameters od monitoring for the outcomes de4scribed above:

1. Curriculum development: Report by the Editorial Board to the Steering Committee and assessment by the Steering Committee, students hired
2. 12 updated management courses: Report by the Editorial Board to the Steering Committee, Assessment by the mentors of the hosting institutions, project evaluation, activity report, assessment by students and peers
3. Quality assuring procedures implemented at BBA: Report by the Quality Control Committee to the Steering Committee
4. Implementing ECTS as a new methodology: Student's evaluation report, Contacts established with foreign Universities, report by the EU expert to the Steering Committee
5. Exchange with other Universities: Report by the host university for visiting professors, Assessment by teachers of the host Univ. for students
6. Equipment: Report by the Equipment Committee to the Steering Committee
7. Project website and upgrading BBA website: assessment by the Dissemination partners, Review by the Quality Control Committee, number of contact with dissemination partners
8. Dissemination: Number of visits made, N° of workshops held, N° of visits to the website, volume of utilization of developed material
9. Sustainability: Report of needs analysis for links with business environment, Exposure to the media of the final conference
10. Quality, control and monitoring: The reports issued by the various control committees conveyed to the Steering Committee through the Quality Control Committee.
11. Management of the project: Number of revisions of the Work-plan, Monitoring of the Work-plan Time required to implement directives and changes

Outcome N° 11: MANAGEMENT OF THE PROJECT

SAA has been the project co-ordinator. It has been involved in project management and control, and project reporting. It has had primary responsibility in curricula, courses and syllabi development, in the development of teaching material and related retraining of MBA professors. It has operated with primary responsibility through its designated expert in the implementation of dissemination activities and of measures aimed at assuring the project sustainability. It has finally been borne the responsibility for financial activity and quality control and monitoring in cooperation with the partners.

UDS has been the second European Partner, and has been responsible for the development of Outcome # 3 (Quality assuring practices) and of Outcome # 4 (Implementation of the new developments in the ECTS system). It has also provided support to all other activities (especially in the area curriculum development and of Dissemination) according to the plan jointly developed with the other partners.

BBA, the partner country University, has co-ordinated operations in Belgrade providing capacity according to the Work-plan; in particular it has been responsible for the adaptation of the teaching material developed with the European partners, it has engaged itself in the adoption of updated teaching methodologies, it has cooperated with UDS in implementation of the quality control procedures and in the adoption of the new developments in the ECTS system. It has ensured the development of links with the business community and will be actively involved in Dissemination of results.

Decision making procedures envisaged

The project has been implemented under the supervision of the Steering Committee and of other committees set up to assure the proper control over the activities carried out by the partner institutions.

The plan for the operations of each period stemmed from the review of the performance of the previous period and of the work plan submitted with the application. The very limited changes that became necessary were jointly agreed by the project coordinator and the coordinators of the partner country institution and of the second EU institution and implemented after the approval of the Steering Committee

The project co-ordinator has also been responsible for monitoring over the implementation of the project. He has reported twice a year to the Steering Committee about the progress achieved and has submitted modifications of or deviations from the original Work-plan. He has informed the consortium partner institutions about any changes approved by the Committee in order to assure their implementation.

The contact persons of partner institutions # 2 and 3 have be responsible for the implementation of the actions attributed to the respective institution

They have also co-operated with the project co-ordinator in the implementation of the Steering Committee decisions, as well as on the decisions of other Committee in charge of quality insurance.

Extensive use of electronic mail has occurred in order to insure a prompt and effective monitoring of and reaction to events that were unfolding

We have come to an end of the programme. Much gratitude must be given to the EU commission and to the Tempus officers in general and to those of the NTO of Belgrade in particular. They have always been very cooperative and available to provide to us sound advices.

The management of the project was smooth and characterized by a very cooperative attitude. Our partners have become our friends as well. Fortunately we will be able to continue a stretch of the way together with the implementation of the Dual Diploma.

Dr Thomas BOTZIOS
The First Secretary, Italian Embassy in Belgrade

Distinguished Professors, ladies and gentlemen, dear friends, I am very glad to have the opportunity to address this distinguished gathering.

First of all, I would like to underline that Serbia and Italy are having a very high level of relationships: not only in economy and trade, but also political, cultural and scientific relations.

Just a couple of days ago we welcomed in Novi Sad and Belgrade the President of the Republic of Italy; one week ago our Minister of Foreign Affairs was here, as well our Minister of Economy did one month ago. For the next months, I can anticipate that in the fall – September, October – our Minister for International Trade will pay a visit in Serbia with a huge mission of companies interested to invest here.

This is a tangible proof of how high is the level of the relations between our two countries.

Besides traditional sectors (banks, insurance, mechanic, textile, wood-processing) of Italian investments, we are looking new fields of investment. There is a strong commitment in the energy sector, especially that of renewable energies, and infrastructure. We are encouraging our firms to invest in those two crucial sectors, that can play an important role in terms of economic development of the country.

Italy has a wide range presence in Serbia: the economic and commercial section of the Embassy; ICE, that is the Foreign Trade Commission; credit agencies and other agencies for supporting exports, the technical cooperation unit. Each one of these actors is involved and engaged to do their best to further boost our commercial relations and to facilitate the inflow of Italian investments in Serbia.

The results, I think, are on the table: trade between Italy and Serbia more than doubled with respect to just few years ago; companies from my country are three times more numerous than three to four years ago; since the privatization process started in Serbia, Italy ranks as the second country whose companies bought Serbian social owned companies.

This is the best signal, I believe, on how performing our relations are. First of all it depends on how well are doing our firms but it is also due to the good relations established at all levels of the governmental institutions. At this purpose, I would like to thank H.E. Minister Mladjan Dinkic for what he said before about the Italian investments in the country and our deep and friendly relations.

I would like to make a last remark about the target of this process. A target that we should not forget. A target to which Italy and Serbia are jointly committed: the integration of this country in the EU, to let Serbia get the place where it belongs, in Europe. This is the major aim of stronger relations, we must not forget that.

I cannot end my speech without addressing you, students of the Tempus Project whose closing we are celebrating today. Many success stories of Italian investment are due to women and men working in our companies. The main asset of Italian companies is the human factor and without it no results would have been possible.

I really hope that in the near future other projects like the one we are concluding today will be implemented, since a good connection between universities and companies is the way to grant investors an increasing quality of human resources. I wish you the best for your professional careers and I thank you very much.

Dr. Fabio CORSI
Instituto Nazionale per li Commercio Estero Ufficio di Belgrado

Ladies and gentlemen, distinguished guests,

I am pleased to be here today, as the representative of the Italian Institute of Foreign Trade and the Italian Trade Commission in Belgrade. I was very happy when, one year ago, or maybe one and a half years ago, Professor Dutto came here and got in touch with our Office. The friendship between me and Professor Dutto it is long dated. It is very old and cold because it began in Siberia about 10 years ago. When we founded the Office there, we cooperated also in projects like this. So, I believe, and people believe in the possibilities that a project like this one has not only in the field of university, between training and management departments, but also for the effects this kind of project can have aiming to grow business opportunities for Italian enterprises.

Just a few words about my Institute. Its main aim is to promote exports, Italian exports and investments around the world, but we also have a responsibility in the field of training and retraining of enterprises and management. So, we are always interested in this kind of projects. In fact in Serbia we did something which is very close to this kind of project, because, one year ago we began cooperation with *Dante Alighieri* that is involved in training course for Serbian civil servants, coming from several administrative institutions – Ministry of Finance, Ministry of Economy and Agency for the Promotion of Investment (SIEPA) and so on. We also organize a one-year course on the Italian language in order to send nine employees from several ministries and institutions to our headquarters in Italy where they had the opportunity to be involved in courses in management, marketing, international marketing, business plan, and so on. I believe that this is a strong evidence of our interest in the area of business management.

I will now show some slides that I believe are relevant to highlight the business opportunities for Italian companies in Serbia. The full set of such slides will be available in the Conference proceedings.

Why Serbia? The geographical location is important, it is an ideal position for our companies, because they want to be established relatively close to their main market.

The level of services is relatively high, more efficiently from the European Union and the Middle East. As was mentioned before, Serbia benefits from some free trade agreements with important countries. Not only the free trade agreement with Russia, but also Serbia signed other agreements like this one with other countries very important like Belarus and Turkey. And so, for our enterprises the Serbian market is important not only for itself, but also for the opportunities it gives to us to go to other…to additional markets like Russia, for example, of 150 million.

All indicators of the Republic of Serbia registered a favorable trend. GDP registered growth of 5.5%, in line with the tendencies of the past seven years. So, all the macroeconomic indicators in Serbia currently are generally characterized by constant growth of GDP, decreased rate of inflation and a strong rise in foreign trade.

This strong rise in foreign trade is shown by growth that we that Serbia has registered last year with an increase of 15.4% in exports, equal of 7.5 billion euro, and a rise of 15.5% of the import. The balance trade is negative, but this is a structural phenomenon caused by the rise in foreign energy products and raw materials from Serbia.

We have some statistical data about Serbian imports from the main partners. The main partner of Serbian import is the Russian Federation, of course. After them, Germany and Italy more or less on the same level. And it registered growth in 2008 of about 14%.

What is interesting here is that for the first time there are some ex-Yugoslavian countries, like Bosnia and Montenegro, which became the main countries of import from Serbia. So, the condition of Italy, which was in the past second trade partner of Serbia, after Russia in 2008 Italy was the third trade partner of Serbia. The total exchange between the two countries amounted to 2.2 billion euro. And, of this, 1.4 billion euro Italian export to Serbia and 763 million euro of Italian import from Serbia.

What are the most notable sectors in foreign trade between Italy and Serbia? Serbian imports from Italy are above all metal – steel and iron, textile products, shoes, food products. Italian exports into Serbia are mainly vehicles, general industrial machinery, specialized industrial machinery, clothes.

As you can see in this figure we are showing the top ten commodities exported from Italy to Serbia that represent 90% of the total: the most notable is equipment for special purposes, clothes and other machines. So, these are the main commodities exported from Italy to Serbia.

For our enterprises, I think that the most interesting sectors in Serbia are food, metalworks, information and communication technologies, textiles, wood and furniture, construction and infrastructure.

Food sectors is one of the main sectors, together with logistics, transportation and together with energy sector in which our enterprises are increasingly showing their interest coming to the market of Serbia. So, as Mr. Botzios said before me, the aim of our Institute is to attract more and more, in spite of the period of crisis. Of course, we cannot expect next year something exceptional or wonderful, because the crisis is deep all around the world. But, we are here just to make clear to our Italian enterprises that Serbia is a market with great potential in this area, maybe the most interesting of this region. As I have told you this is attributable to the position of the country, to the features of the labor force and to all the opportunities that include the legal framework that this market could give to our enterprises. In the next month we are going to organize an important economic mission from Italy, headed by the Italian Minister of Foreign Trade. We are hoping that this will be the first signal in this year, showing how important Serbian market must be for our enterprises. In the next few weeks the process will start. We have to stay here, to be here, because here we can take good and long-term opportunities for our industry.

Take you very much.

ITALIA
Istituto nazionale per il Commercio Estero

RONCUCCI&PARTNERS

Business opportunities for Italian companies in SERBIA

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Belgrade, June 2009

ITALIA

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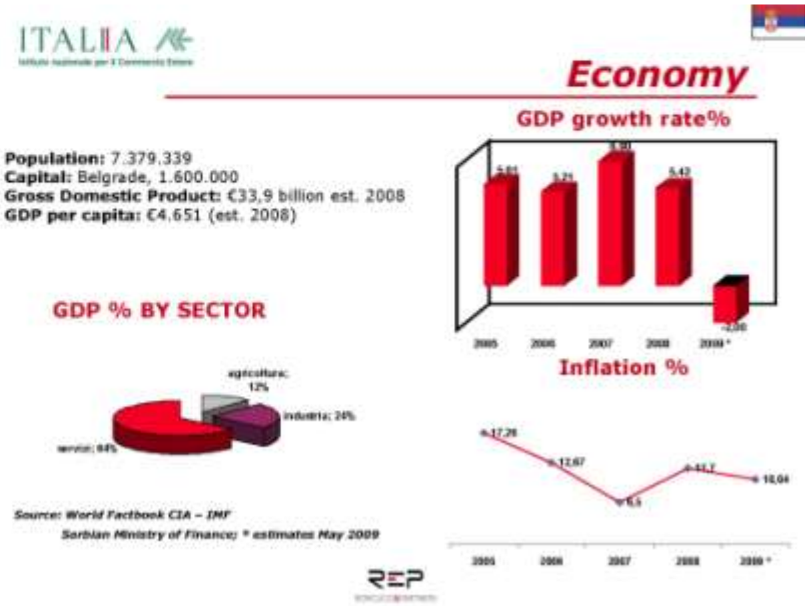
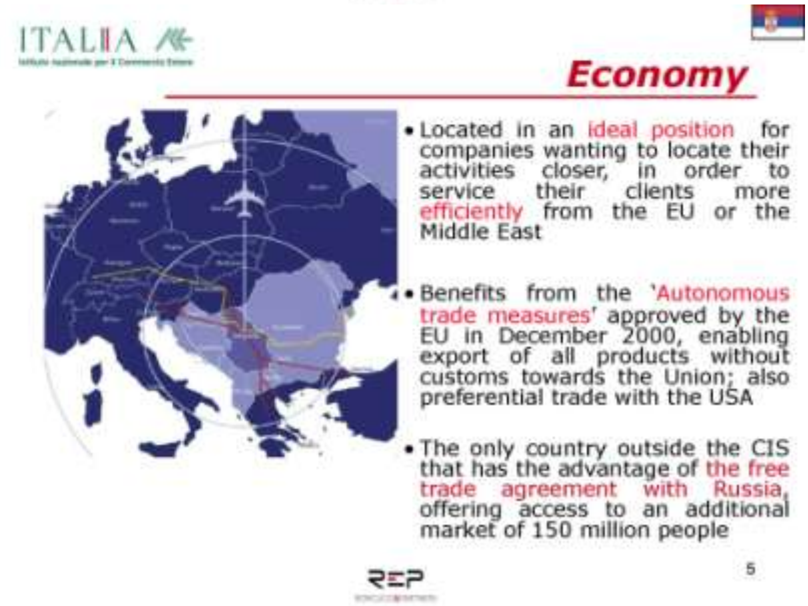

ITALIA
Economy
GDP growth rate%
Population: 7.379.339
Capital: Belgrade, 1.600.000
Gross Domestic Product: €33,9 billion est. 2008
GDP per capita: €4.651 (est. 2008)
GDP % BY SECTOR
agricoltura: 12%
industria: 24%
servizi: 64%
Inflation %
17,26
12,67
11,7
10,04
6,5
Source: World Factbook CIA – IMF
Serbian Ministry of Finance; * estimates May 2009
REP


ITALIA
Economy
• Located in an ideal position for companies wanting to locate their activities closer, in order to service their clients more efficiently from the EU or the Middle East
• Benefits from the 'Autonomous trade measures' approved by the EU in December 2000, enabling export of all products without customs towards the Union; also preferential trade with the USA
• The only country outside the CIS that has the advantage of the free trade agreement with Russia, offering access to an additional market of 150 million people
REP
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ITALIA
Economy
In 2008 the GDP of the Republic of Serbia registered the growth of 5,5%, reaching around 34 billion euros in line with the tendencies of the past seven years
The macroeconomic indicators of Serbia during the transaction years (2001 – 2007) are generally characterised by constant growth of GDP rate , decrease of inflation , strong rise in foreign trade, but also by strong trade deficit with salaries rising more than productivity
REP
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Foreign Trade

According to the latest statistics from the Statistical Office of the Republic of Serbia, in the year 2008 trade between Serbia and the rest of the world has additionally grown, registering an increase of 15,4% in exports, the equal of 7,5 billion euro, and a rise of 15,5% in imports, that have amounted to 15,6 billion euro

The balance of trade is negative - 8 billion euro, a structural phenomenon caused by the rising need for energy products and raw materials

7

Foreign Trade

Serbian imports for the period January-December 2008 (in .000 euro)

Countries			
1.	Russian Federation	2.370.329	**+23,9**
2.	Germany	1.826.831	**+ 14,5**
3.	**Italy**	**1.477.009**	**+13,0**
4.	China	1.247.106	**+ 25,6**
5.	Hungary	548.838	**+ 4,8**
6.	Bulgaria	505.564	**+ 18,7**
7.	France	504.352	**+ 19,8**
8.	Ucraina	441.442	**+ 59,0**
9.	Bosnia – Herzegovina	437.295	**+ 16,2**
10.	Romania	428.796	**+ 37,6**

Source: Statistical Office of the Republic of Serbia

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Foreign Trade

Serbian imports for the period January-December 2008 (in .000 euro)

Countries			
1.	Bosnia - Herzegovina	907.352	**+ 19,5**
2.	Montenegro	865.635	**+ 25,1**
3.	Germany	772.653	**+ 13,0**
4.	**Italy**	**763.338**	**- 4,5**
5.	Russian Federtion	374.120	**+ 14,7**
6.	Slovenia	338.685	**+ 13,6**
7.	FYR Macedonia	334.044	**+ 5,0**
8.	Austria	309.866	**+ 40,7**
9.	Croatia	294.466	**+ 22,3**
10.	Romania	272.791	**+ 41,0**

Source: Statistical Office of the Republic of Serbia

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ITALIA

Foreign Trade

In the year 2008 Italy was the third trade partner of Serbia

According to Statistical Office of the Republic of Serbia the total exchange between the two countries amounted to 2,2 billion euro, 1,47 billion euro of which, Italian exports into Serbia (+13% a rise compared to the same period of 2007) and 763 million euro of Italian imports from Serbia (-4,5% compared to the previous year)

The balance of trade amounted to 713 million euro in favour of Italy

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ITALIA

Foreign Trade

With regard to Foreign Trade by commodities and products between Italy and Serbia, the most notable were:

Serbian imports from Italy:

Metal (steel and iron)
Textile products
Shoes
Food

Italian exports into Serbia are mainly:

Vehicles
General Industrial Machinery
Specialized Industrial Machinery
Clothes

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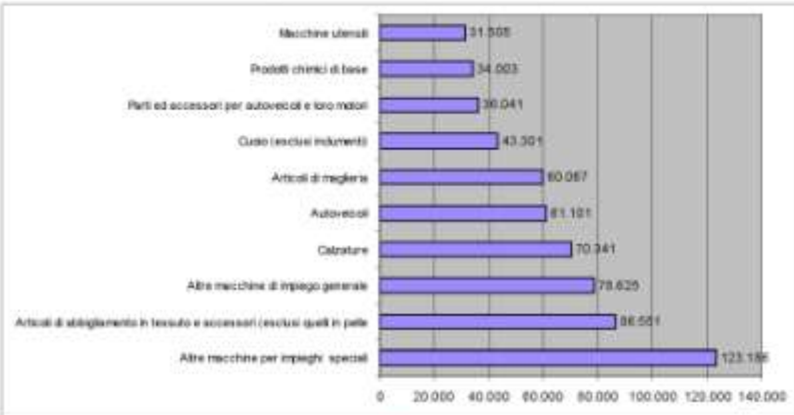
ITALIA

Foreign Trade

Top ten commodities exported from Italy to Serbia (in millions of euro)



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Fonte: ICE su dati ISTAT

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Foreign investors

(in .000 US$)

N.	Paese	2004	2005	2006	2007	2004-2007
1	Austria	146.104	201.180	520.356	1.161.056	**2.028.745**
2	Greece	52.968	249.536	923.698	336.401	**1.562.603**
3	Norway	0	29	1.546.993	3.187	**1.550.209**
4	Germany	51.985	187.320	905.824	69.530	**1.214.659**
5	Slovenia	15.706	183.563	201.241	92.856	**493.366**
6	Luxembourg	2.387	108.885	8.843	241.537	**361.652**
7	France	24.022	62.347	159.085	84.391	**329.845**
8	Hungary	16.567	24.677	244.045	31.494	**316.783**
9	G. Britain	79.620	63.330	135.915	26.504	**252.281**
10	Italy	10.149	18.316	52.732	153.363	**236.580**
11	Switzerland	29.403	56.990	15.421	56.157	**167.127**
12	Croatia	10.806	40.484	25.240	35.944	**112.474**
13	Bulgaria	9.910	655	54.270	46.516	**111.751**
14	Slovakia	0	25.447	19.325	3.084	**47.856**
15	Holland	102.008	92.113	-214.119	27.958	**-47.856**

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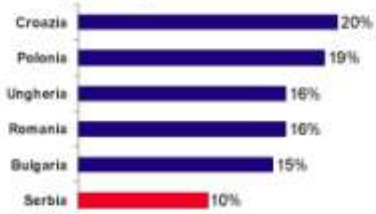
Tax Regime

Corporate profit tax rate



At 10%, corporate tax rate is the lowest in Europe

The standard VAT is 18%

For some sectors (food, publishing, utility etc.) there is a lower VAT of 8%

A 10-year corporate profit tax holiday for investment over €7.5 million and 100 new employees

REP

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Job Market

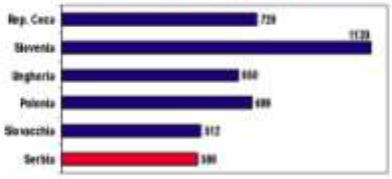
Knowledge of English

(Source: SIEPA)

The Serbian labour force is reasonably qualified, above the regional standard:

- **42% speaks English**
- **34,5% has a degree**

Gross monthly salary in euro



In spite of this the gross monthly salary is on average 500 euro, lower than in many neighbouring countries

REP

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Key Industries

The main Serbian industries are the following:

- FOOD
- METALWORKS
- ICT
- TEXTILE
- WOOD AND FURNITURE
- CONTRUCTION
- INFRASTRUCTURE

REP

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Key Industries
Food

Main sectors

- Meat Industry
- Fruit and Vegetable Processing Industry
- Mineral and Still Beverage Industry
- Sugar Industry
- Wine and Spirits Industry
- Frozen Food Industry

REP

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Key Sectors
Mechanics

Mechanics sector is very diversified and wide, with a total of around 900 companies. The main products, among others, are as follows:

- **general use machines**
- **agricultural machines**
- **tractors**
- **civil engineering machines**
- **machines for production and use of mechanical energy**
- **wood and paper processing machines**

The characteristic of this sector is technological obsolesence

REP

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Key Industries
Mechanics

Among the most promising sectors for market penetration of the Italian industrial system are:

- machines for food processing
- agricultural and forestry machines
- packaging machines
- printing machines

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Key Industries
Mechanics

AUTOMOTIVE focus

- Key sector of Serbian industry, with more than 36.000 employees
- Long tradition of cooperation with European countries
- Presence of local *suppliers* for production of parts and sufficient components for production of more than 250.000 cars a year
- Specialised labour force

There are around 100 companies involved in the production of parts for the automotive industry

The potential of this sector lies in its underused production capacities and specialized labour force

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Key Industries
Textile

The textile sector has a long tradition in Serbia and remains one of the most important in the country

Employs around 100.000 workers, contributes to the country's GDP by around 10%. Today it comprises of 1.600 companies, the majority of which are small and medium enterprises

Few Serbian stylists have opened their own shops, and many of them have moved abroad where they work for important fashion companies

The analysis of the industrial exchange with Serbia shows the Italian market share in textile industry greatly influenced by the contract work (lavorazione conto terzi)

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ITALIA

Key Industries
Textile

Serbian textile industry presents many advantages such as good quality, low cost of the work labour and the vicinity of European fashion centres

70% of the Serbian exports of textile products are at the moment directed toward the EU countries

The textile agreement between the EU and Serbia, from the 31st March 2005
Serbia exports textile products to the EU countries

free of customs taxes

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Key Industries
Construction

Residental construction, shopping centres, hypermarkets, and office space offer great possibilities. It is important to stress that the Serbian construction sector has a strong tradition

There are notable opportunities especially for Italian design, style and technology, such as interior and exterior design: floors, tiles, bathroom design, lighting, garden accessories, pools, murals

REP

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ITALIA

Key Industries
Infrastructure

Infrastructural and the sector of transports are considered a priority for the economic development, by the Serbian government, the International Financial Institutions (EIB and EBRD) and also by the European Agency for Reconstruction (EAR)

The geographic location presents one of the major "assets" of the country, which makes it interesting for development of large infrastructural transport networks, logistics and services to the companies

The country is developing more than 40.000 km of road network, and a railway network of 3.808 km. When it comes to river transportation, the most important navigable rivers in Serbia are the Danube and the Sava, which are part of the Paneuropean corridor 7. The traffic volume per year is 60.000 passengers

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Key Industries
Infrastructure

In spite of the good coverage of the total network and the fact that the employees in the sector are well-trained , the system of trasport in Serbia, like in the whole region of the Western Balcans, suffers due to its flaws and inefficiencies caused by the lack of investments during the 90s

The use of intermodal freight transport and logistic support of the businesses is scarce

In Serbia, there are no centers for intermodal transport. There is also deficiency in spaces and warehouses for the storage and movement of cargo, while there is a total lack of cold chains for distribution of fresh produce

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ITALIA

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Development Projects for Companies in Italy and Abroad

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REP
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Ing. Giovanni DE FILIPPIS
Genaral Manager, CEO Fiat Group Automobiles (FGA) Serbia

Ladies and gentlemen,

In addition to a more formal and structured presentation concerning the FIAT group that will follow, I would like to share with you some ideas concerning the consideration guiding the people and development of the people, which, of course, is one of the main subjects of this occasion.

Very briefly, I will tell you that FIAT is a multinational company, whose presence is, I would say, in most of the countries of the world from the commercial point of view, but from the industrial point of view, we have maybe something like fifty countries of presence and more than two hundred companies, even before the deal with Chrysler, that has given a big footprint also to the operation in the US, where we were already present with other companies of the group.

The company is an automotive company, so basically we produce cars, other automotive, like agricultural and commercial vehicles, and there are components, basically. Viewing the structure of a few years ago, the concentration of the company was the focus on all that is automotive.

Just few considerations about our presence in Europe. You will find that in Europe we are present quite in every country with commercial operation. What is more interesting, is that we are present with industrial operation in Poland, Turkey. We are having some joint venture in France with Peugeot. We are getting our vehicles produced in Hungary by Suzuki. And, of course, we are here in Serbia.

The approach and presence in different countries can be different according to the situation in the country and to the possibilities that can rise.

If you just consider the presence of the FIAT Group Automobili in the world, the main presence out of Europe is the one in Brazil, which is the world-wide leader in the market. We have also a significant presence in India with joint venture with Tata Motors and we are present in Russia and we have an assembly, according to the license agreement, in Iran.

I am just presenting these to you for one reason. Wherever we go to establish a production company, we always have in mind to develop something which is common in terms of quality, in terms of standards that we create. So, when we go to a country we may have different product, but the same quality. For example, if you are going to India, you need to have certain specification to resist to the roads, to the different condition of weather and maybe a number of options which are required and are very different from European countries.

But, in terms of quality, so in terms of organization of work and people, we do not want to have any difference anywhere in the world. And the approach that we are using is basically the same.

As I said, also a multinational group like FIAT is used to work in conditions in which there are certain alliances that are made for different reasons, in order to get some technology in use, to get volume, to reduce cost. So, you have synergies that are related to product development or engines, you are sharing know-how with companies, you are having products made by others. This is the case with FIAT Sedici produced by Suzuki. And you have many sourcing activities together with others or you are manufacturing together with other groups. Or, other reason to go to a certain country, or to make a certain kind of alliance can be to get access to the market. You go to a market and you produce there also, you may have the necessity to overcome some custom limitation, or you want to go to a certain country in order to get the advantage of the market.

I will say that in the case of Serbia the main reason to establish a plant here is related to the possibility of using it as a production base in order to export products mainly to the European Union, which is the base of our project, and possibility to export to Russia, which is interesting outside , and finally because there are certain advantages that we can use to sell in the country.

Let me just make very briefly some consideration about automotive industry and our location of factories. If you can see the last ten years - which in the present situation could be something like several hundred years ago - you would see that there was an increase of production capacity, which happened everywhere in western Countries, was an evaluation of the necessity to increase production capacity, which happened with 300,000 cars per year added to the European industrial footprint. But, what is more interesting is that anyway all these companies have moved this work, and a significant part of the operation has been moved to the Eastern Countries . Another significant part is that many Asian carmakers have come to Europe, and they of course came to countries, which were competitive.

I would not say only cost-competitive, because there are a certain number of criteria that are used to select a certain location. I would just like to make some comment about what were our considerations.

Our considerations were the following ones. Okay, you need to have a competitive plant, you need a country with a certain number of advantages, basically in Eastern Europe. We scouted in different countries and let us say that the key items, the key factors that we were evaluating in our job were labor cost, of course, but also the availability of skilled labor, presence of suppliers, existence of infrastructure, energy cost, fiscal and custom policies and incentives given by the government.

Then we were analyzing the opportunity of having an investment as a Brownfield or a Greenfield investment. I will make some comments about how we see Serbia positioned in these different items. Of course, in terms of labor cost Serbia is considered very competitive. About skilled labor we will make some more comments, because we see that there is some potential, but this potential needs to be somehow enhanced. Concerning the suppliers system, In Serbia the situation with suppliers is not like in many other surrounding Countries. Infrastructure, energy cost, fiscal and custom policies have need of improvements. I will put all these together to say that, if you want to have a very mighty industry, like the automotive industry, you need to have somehow in the beginning the commitment and the action that is coming from the government. Because, the government basically has a role to create all the conditions that can help the industry and that can guide a choice.

Even more than a direct incentive to an investor, what is important, more important is the readiness of a government to offer all this goods that industry need. I would say, just in terms of infrastructure, you are making a factory that is producing 200.000 vehicles per year, and you want to export 90-95% of your production. In this case, you are moving something like 40-50 trains per day, 200 trucks per day, you are establishing a suppliers' network, for which, if you are employing one person, normally the supply network is employing four people. So, you cannot imagine creating something like this alone, without any kind of action from the government. And this gives you an idea why, normally, government can be interesting in automotive industry coming to a certain country. Because, actually, a project like this is to be seen from day one as a project that has a huge impact, not only in the same area, not only near the plant, but in general like a huge impact in all the Country.

And then, the last consideration is creating a Brownfield or a Greenfield investment. So, is it better to make a factory which is completely new or you just enter into something and then you restructure?

If you ask, normally, to all our engineers, they would say – Definitely we want to go for something completely new. The problem is easier to solve from our point of view. The time is longer, but you can do whatever you want, you can define that. I see, personally, the main opportunity in restructuring activity because there are many challenges, and I will make some comment about the challenges that are coming out.

Finally, in our project the target was to achieve a factory that is working according to all the standards that we have reached in the rest o the world, that we call internally as "World-Class Manufacturing", which is the FIAT way of making production.

So, just very quickly, regarding what has already happened, we started discussing what the government committed to make in 2008. In a matter of two to three weeks we signed a memorandum, and then, in the next four month we begin the activity. Shortly, in five months we have reached an agreement and started a joint venture. Today we are producing the Punto, we are introducing a new engine, and we have taken the production capacity to a rate which is more than double than what the factory used to have in the last twenty years.

What is also interesting is that, if you were asking to all the people, they were not even convinced that it was possible to do something like this. And we have achieved, basically, with something related to skill, training and motivation of the people, rather than investment, which has been present but directed to few important items. So, this gives you the first indication of how the know-how, the training and motivation can change very significantly quickly the situation.

Let me say something else. When we have started the project, the main challenges that we were considering for us were the fact that we were entering into something interesting, the factory was possible to be developed and may completely to be restructured and, basically, a factory that was not using innovation. The factory made the same model for twenty years, had no reason to increase production, no reason to work for efficiency, no update of the skill of the people. If you were going outside, also, to the suppliers' system, basically, there are no suppliers in Serbia that are delivering items to carmakers. They are just supplying either, let us say, spare parts market, or they are supplying other suppliers.

In other words, you can say that you do not have know-how, you do not find investments, and there is also a critical financial situation. Also, in this case, the way of coming out of this is basically related to a big project that can lead an international supplier to come here and find it convenient to come to Serbia. And sometimes a sort of help or assistance from the government is required, at least in order to enhance the financial capability of the supplier and to create, also, conditions for other suppliers to come.

So, we were looking internally the situation, we were making some consideration about the people and, let us say, what is our finding about the labor market in Serbia? Very simple. You will find, in terms of white- and blue-collar in the area of Kragujevac good people, very good workers, in the factory but also outside the factory you will find good people. They are looking for jobs, there is a high unemployment rate. So, there is a big possibility to develop the area. Regarding top management, the situation is a little bit more difficult, because you do not find immediately executives that you can employ in the automotive business. Maybe, in other sectors the situation can be completely different. I am just saying what we find for our sector.

As I said, since what we want to do is a factory that is what we call "World-Class Manufacturing" standard, we needed from the beginning to create a proper selection, we needed to create a proper training. Let us start from the selection. When you have an average age of 52 years people of course you have good people, very experienced people, but you need also to create some more differentiation. You need this kind of people for sure, but you need also to have some young workers. And so, what we have set up as a process in order to guarantee that people we are going to take internally and externally are going to be the best that we can. And another point that is important is how to proceed with the integration of the people.

We have decided to go fast. But let us say that we have applied our logic on how we select and promote people internally. So, you have different approaches based on tests, but basically what you are looking for in people are – capacity of problem solving, orientation to quality, orientation to result, capability of working in teams and dependability. We have started to work and select the people based on this kind of consideration.

Now, where we are? We are in a moment where we have a clearer, much clearer picture about the present situation and we are in the phase of, let us say, starting training. Basically, we have already started with the Punto and when we were starting the production we created a team of fifty people from Italy that are staying here for more or less three months, in order to re-educate, retrain and increase the skill of the people. And now we are going to have different plans for blue -collar, for white -collar and for managers. And one thing that we are going to implement, that we want to implement is a sort of academy in which we take the people internally, but also the people that are coming outside, and we want to create a situation in which people can learn what we need, actually, can learn how to work. So, something that is immediately before entering into the work activity.

Just some comment that I wanted to make with you regarding what we found in assessment of the people in Zastava. Basically, I would say that the attitude is positive, that people want to work. They, of course, need to work, so you will find that most of the people have a situation which they see this coming as an immediate need. You will find something interesting that is very similar to what we have also in many factories. You have more passion for the work and for the product in the blue-collar status, than in the white-collars. So, normal people that are doing work and who are ready for the job are more attracted and more passionate for the job. And everybody is having a clear idea of the necessity of making a change.

Okay, this was the presentation and this is the situation where we are. And next steps are going to be, as I said, start of an academy in order to have proper training for the people and we will go on with other processes of recruiting and selection.

Thank you.


FIAT GROUP
Automobiles and Light Commercial Vehicles
International Conference- Business Opportunities in Serbia:
The case of the Italian Sector and the Role of Management Education
Fiat Automobiles Serbia Case: The restructuring of Zastava and its enhancement to the level of World Class Manufacturing
June 22nd 2009


Fiat Group today
Today Fiat is a large international Group operating in the automotive field.
It designs, manufactures and sells automobiles, trucks, tractors, agricultural and construction machinery, engines and automotive components and production systems.
The Group carries out industrial and financial services activities in the automotive sector through companies located in approximately 50 countries and has commercial relationships with customers in approximately 190 countries.
The Group has 203 plants and more than 198 thousand employees worldwide, in addition to 118 R&D centres on five continents staffed by approximately 14,500 highly qualified personnel.
June 22nd 2009
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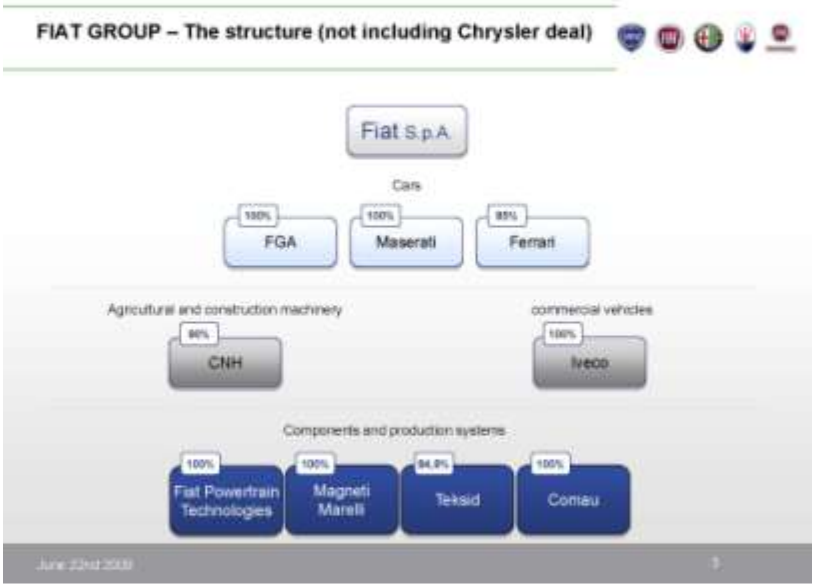
FIAT GROUP – The structure (not including Chrysler deal)
Fiat S.p.A.
Cars
100%
FGA
100%
Maserati
85%
Ferrari
Agricultural and construction machinery
90%
CNH
commercial vehicles
100%
Iveco
Components and production systems
100%
Fiat Powertrain Technologies
100%
Magneti Marelli
84.8%
Teksid
100%
Comau
June 22nd 2009
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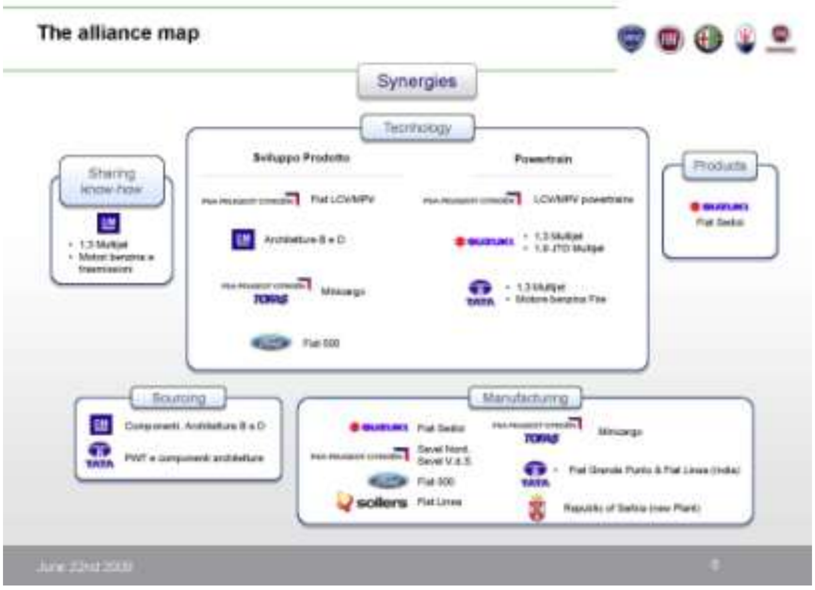
Presences in Europe
PRESENCES IN EUROPE
Direct industrial presences
Direct commercial presences
Indirect industrial presences+150 importers worldwide
Joint ventures
Irland
United Kingdom
Sevel Nord
Denmark
Tychy
Poland
Holland
Belgium
Czech Republic
Slovakya
Germany
Hungary
France
Austria
Serbia (FAS)
Switzerland
Spain
Portugal
Turchia (Tofas)
Greece


Presences in the World (not including Chrysler deal)
Direct industrial presences
Direct commercial presences
Indirect industrial presences+150 importers worldwide
Joint ventures
Russia (Severstal)
Iran (PDF)
Japan
India (Fiat India)
China
Marocco (Fiat Auto Maroc)
Brazil (Fiasa)
Argentina (Fiat Auto Argentina)
South Africa (Fiat Auto South Africa)


The alliance map
Synergies
Technology
Sharing know-how
Sviluppo Prodotto
Powertrain
Products
Sourcing
Manufacturing
sollers


The alliance map
Access to Markets
Turkey
sollers
Russia
TATA
India
Republic of Serbia
Serbia
License and distribution agreements
PIDF
Iran
Tech-New Group
China


EU facilities Opened and Closed (2000-2009)
Before the start of present crisis, across the European region in the last 10 years, capacity has increased and has gradually shifted east-wards
net effect on capacity installed: +300k
Localization: 67% of new capacity in New Member States
Car Makers: 65% of new capacity by Asian Makers
Source: PWC Automotive institute


Serbia as the location for a new production site
Also FIAT Group Automobiles (FGA) carried out a scouting for a new industrial location in several Eastern European Countries including Serbia, Romania, Hungary, Slovakia, Poland.
The following factors have been considered:
Labour cost
Availability of skilled labour (engineers, technicians, workers)
Presence of Suppliers
Infrastructures (Railway, Highways...)
Energy costs
Fiscal and custom policies
Local incentives for investments
Opportunity of a brown field investment vs a green field investment
The Acquisition of Zastava in Serbia was considered the best option, even with some concern on how restructuring the plant to enhance it to the level of a "world class manufacturing" site ....


FIAT AUTOMOBILES SERBIA: Main facts
All negotiations with the Republic of Serbia were extremely fast and in April 2008 a first MOU was inked
On September 29th 2008 a Joint-Venture investment Agreement between the Republic of Serbia and Fiat Group Automobiles was signed and on October 13rd 2008, FIAT Automobiles Serbia was established to manufacture vehicles under FIAT Group Brands to be mainly exported.
On April 2009, it was started the production of FIAT Punto Classic, representing a bridge towards new models
Today production rate is 100 units/day (double of rates achieved in the last 20 years)
In July a diesel version will be added and export to Bosnia will begin in September
10


Starting situation and challenges …
In Serbia, because of the wars and sanctions any technological development has been frozen for more than 20 years and such situation posed several challenges to our plans.
In Zastava in that period:
No new model was introduced
Production did not exceed the average rate of 1,000 u/month
Skill of people and job culture were partially lost
Suppliers have not up-dated their capabilities:
Investments in technology are required
Also Know-how acquisition is required to serve OEM
Financial Capability need be strengthened
11


Our findings on the Serbian labor market
Managers
Socio-cultural profile of the population
•Advanced educational system, however of a lower level with respect to other European countries, which does not favor basic educational preparation of people;
Availability on the labor market
•Difficult to find locally in Serbia high caliber managers; quality and availability increase in areas like Belgrade and Novi Sad, which are more economically developed;
Mobility
• Not very high; high expectations from managers regarding salary and general working conditions.
White and blue collars
Socio-cultural profile of the population
•Economical crisis favor mobility to find an occupation, however, at the same time, it decreases economic resources to afford a relocation;
Availability of technical schools and University in Kragujevac (Engineering) makes it easier to find resources locally then in other areas of Serbia.
Availability on the labor market
•Relatively easy to find human resources on the market considering the high unemployment ratio, especially in the area of Kragujevac;
Low salary standards in Kragujevac, lower then national average;
Hard working conditions and very little chances of development make it easier to find people positively oriented toward opportunities like FIAT.
Mobility
•Current economic crisis pushes flexibility, although this is more applicable to white collars rather then to blue collars.
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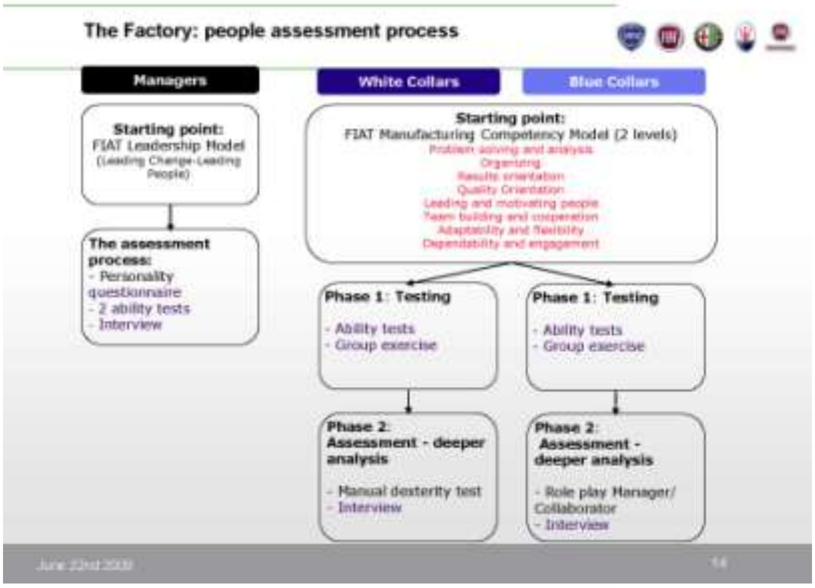
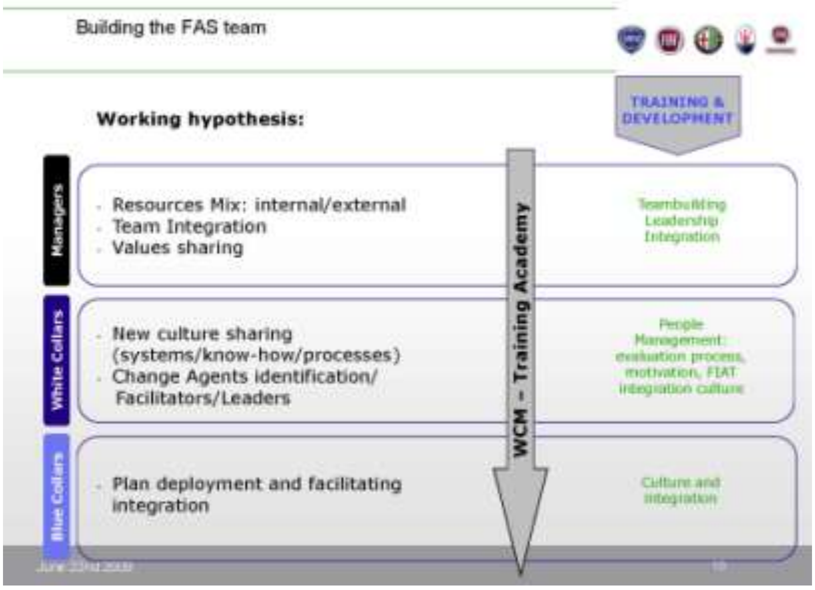
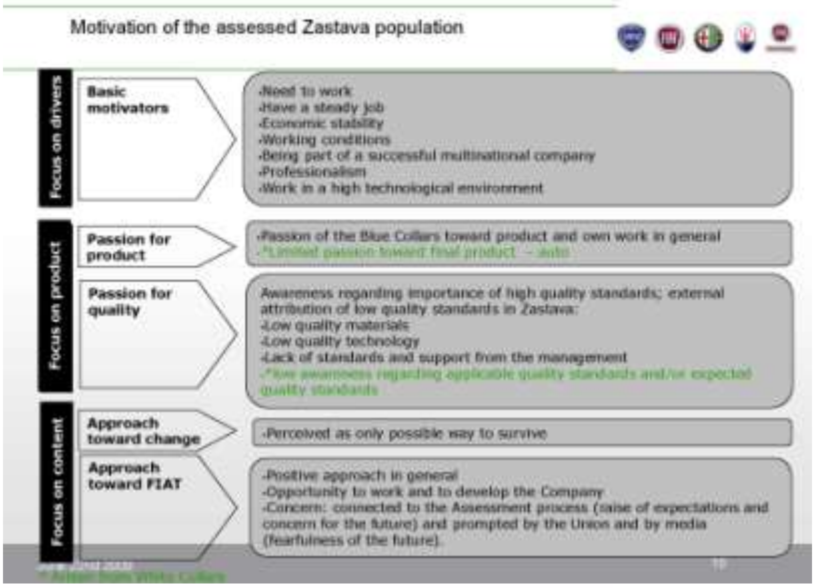
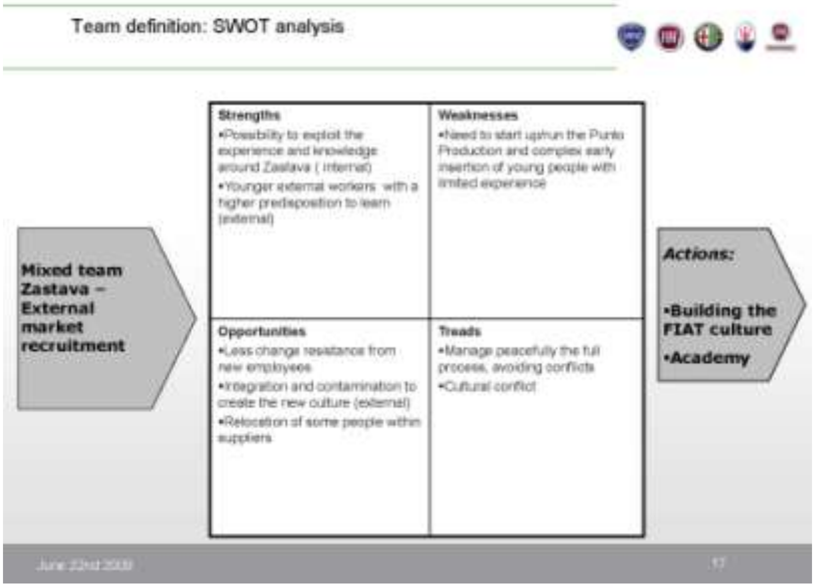
The Factory: The Human factor
FIAT
Organization model
Professional competences
Individual capacities
ZASTAVA
Assessment of internal resources
Assessment of external resources
Plant start up
Progressive Integration


The Factory: people assessment process
Managers
White Collars
Blue Collars
Starting point:
FIAT Leadership Model
(Leading Change-Leading People)
The assessment process:
- Personality questionnaire
- 2 ability tests
- Interview
Starting point:
FIAT Manufacturing Competency Model (2 levels)
Problem solving and analysis
Organizing
Results orientation
Quality Orientation
Leading and motivating people
Team building and cooperation
Adaptability and flexibility
Dependability and engagement
Phase 1: Testing
- Ability tests
- Group exercise
Phase 1: Testing
- Ability tests
- Group exercise
Phase 2: Assessment - deeper analysis
- Manual dexterity test
- Interview
Phase 2: Assessment - deeper analysis
- Role play Manager/ Collaborator
- Interview


Building the FAS team
Working hypothesis:
TRAINING & DEVELOPMENT
Managers
- Resources Mix: internal/external
- Team Integration
- Values sharing
Teambuilding
Leadership
Integration
White Collars
- New culture sharing (systems/know-how/processes)
- Change Agents identification/ Facilitators/Leaders
People Management: evaluation process, motivation, FIAT integration culture
Blue Collars
- Plan deployment and facilitating integration
Culture and integration
WCM - Training Academy


Motivation of the assessed Zastava population
Focus on drivers
Basic motivators
-Need to work
-Have a steady job
-Economic stability
-Working conditions
-Being part of a successful multinational company
-Professionalism
-Work in a high technological environment
Focus on product
Passion for product
-Passion of the Blue Collars toward product and own work in general
-*Limited passion toward final product – auto
Passion for quality
Awareness regarding importance of high quality standards; external attribution of low quality standards in Zastava:
-Low quality materials
-Low quality technology
-Lack of standards and support from the management
-*low awareness regarding applicable quality standards and/or expected quality standards
Focus on content
Approach toward change
-Perceived as only possible way to survive
Approach toward FIAT
-Positive approach in general
-Opportunity to work and to develop the Company
-Concern: connected to the Assessment process (raise of expectations and concern for the future) and prompted by the Union and by media (fearfulness of the future).


Team definition: SWOT analysis
Mixed team Zastava – External market recruitment
Strengths
•Possibility to exploit the experience and knowledge around Zastava (internal)
•Younger external workers with a higher predisposition to learn (external)
Weaknesses
•Need to start up/run the Punto Production and complex early insertion of young people with limited experience
Opportunities
•Less change resistance from new employees
•Integration and contamination to create the new culture (external)
•Relocation of some people within suppliers
Treats
•Manage peacefully the full process, avoiding conflicts
•Cultural conflict
Actions:
•Building the FIAT culture
•Academy
June 22nd 2009
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FIAT
FIAT Automobiles Serbia Doo
June 22nd 2009


The employees
By geographical area
Italy 30.557 58.1%
Europe (- Italy) 8.755 16.6%
Latin America 13.196 25.1%
Other 126 0.2%
TOTAL 52.634
By age and position
età media
Managers 1% 46
White Collars 26% 40
Blue Collars 73% 39
By professional area
7.68%
2.58%
1.06%
7.14%
Marketing & Sales 0.78%
Parts & Services 1.40%
Human Resources 72.20%
Development 0.30%
*Business Development, General Affairs, Communication, Compliance Officer, Product Portfolio Management
June 22nd 2009
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Our "cars of the year"
Fiat Group Automobiles has won the Car of the Year award, the most reputable prize attributed to the automotive industry in Europe, 12 times
1967 - Fiat 124
1970 - Fiat 128
1972 - Fiat 127
1980 - Lancia Delta
1984 - Fiat Uno
1989 - Fiat Tipo
1995 - Fiat Punto
1996 - Fiat Bravo-Brava
1998 - Alfa 156
2001 - Alfa 147
2004 - Fiat Panda
2008 - Fiat 500
June 22nd 2009
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Dr. Giancarlo MIRANDA
Deputy President of the Executive Board, COO Banca Intesa ad Beograd

Good Morning!

I am grateful for the opportunity I had to listen in the last couple of hours very interesting speeches on the banker's perspective in education, particularly from the perspective of Italian bank working in Serbia. I have a short presentation titled The Leading Bank in Serbia that you will find in the Conference proceedings. The Key issues that I have confronted myself with are: Why we are here? How we managed to become the biggest bank in Serbia?

There are many things that happened in the last few years. Definitely, bankers are not on the top of the list these days for what concerns the public opinion. One thing that really occurred in the last few months is to notice that bankers have become really macro economists. Quite to my surprise, I was noticing when Mr. Dinkic was speaking, very interesting convergence between what he was thinking about economy, and what we are in the economy as such. We have a very special angel in a bank. We see the economy developing in our eyes. We see many companies coming to knock on our doors, asking for funds. We see their problems. So, we really have the privilege of this sense. It's not, however, a privilege to work in the crisis situation. This is what it really turns out to be, and this gives us some hints at what the situation is.

What is the situation here? Mr. Dinkic said before we are talking about the crisis which is originated from banks, a a banking crisis. I would term it in a slightly different way. It's a liquidity crisis. But, fundamentally you cannot deny there that there is a conception, the assumption that we are talking about an economy whose fundamentals are regionally good. I am speaking about fundamentals in a more banking, financial terms rather than on the fundamentals. Fundamentals are something you have to work and build upon. Fundamentals are features, characteristics of a particular market. And in this particular market of Serbia, I think fundamentals are good since demand for fund is substantial. The country is definitely converging towards new consumption models, towards new economic development models. This is way I say that fundamentals are good. For a bank it is excellent, because when you see that the fundamentals are good you start motivating your presence in a way to respond.

Let me just tell you who we are. First of all, for quite a few of you and mostly for Italian visitors, this are known facts. I have to say that very often all looks quite impressive when we speak about Banca Intesa. In Serbia we are speaking about the largest banking institution. Being number one, however, also involves some sense of responsibility. Now, I was very pleased to hear Minister Dinkic commenting about our role and capacity to support the economy in this moment of crisis. This has to be seen in conjunction with the assumption of the features of the crisis in Serbia. As I said, it's definitely a liquidity crisis, which has in a way been compounded by the international liquidity base crisis.

Like elsewhere, also locally many, many deposits left the banks exactly, because of the crisis of trust into the banking sector which erupted across the globe. Nevertheless, at this point what should the banker do? What is the reaction to this, when you see deposits going out of the books, when you see international scenario drying up, when you see crisis booming, you see the end of your normal forecasting exercises, the crisis is coming.

What should the banker do? There is an easy way out, simply go to the shop. That is something the banker could easy do. If all the banks act in this way, then the economy acts in this way, and then it really induces as a bank a broader crisis into the economy. That is not what we did in Banca Intesa, and in many other banks. In particular we took the view that the first and foremost task for us in the crisis was to protect the companies we have been supporting for the last few years, good companies with good fundamentals, to protect them during the time of crisis by putting at their disposal some short-term liquidity facilities in order to bridge the cycle of shortfall, restricted liquidity, and go hand in hand in the investment side. That is why for us it was extremely important to see that the Government was intervening with special schemes to support SMEs in crisis. This was an important step since it responded to a critical issue: there was the risk that many companies couldn’t find or have access to credit, in a situation that was worsened by the huge price for the short-term facilities.

In that particular moment, if a good bank has sufficient liquidity to support this, it must feel the responsibility of supporting the whole system through the crises into the new investment cycle. We can see that we immediately stepped up our lending to the economy. We made liquidity available to the credible customers. You see how we grew both in absolute numbers and in the market shares. What Mr. Dinkic was saying before, he is quite right. This is number one position; the bank has number one position. We were 3% of the market, now we have in a few months, just in a few months, it was a tremendous opportunity, and we went to 17.4% in lending to corporate entities. It was a remarkable achievement. We wouldn’t see this type of achievement in normal times. Back then it was impossible to even imagine the erratic market shares of this type, we have seen this growth because of unfolding in the market. Retail did not fall the same. Why? Because of one thing Mr. Dinkic said before. I think that he is totally right, because we also have a psychological crisis. Families looking at an expected crisis immediately react by restraining their consumption - and that influence the borrowings. They borrow less because they don’t feel as safe as before, as secure as before, which is quite wise, quite understandable. That is why growth in absolute terms of lending to retails was not as dynamic as in the case of corporate, that is why our market share remained quite stable.

We give you another hint to look at corporate deposits whereliquidity is much more volatile in the course of time. I am always talking about the crisis period which lasted from September last year through April this year. This does not mean that the crisis is over, but because that was really the height of the crisis when everybody thought that the world would collapse. That was not the case, there were some problems, and what we see, the retail deposits, because there was actually the decrease of deposits if we look at September- December figure. It was a decrease of the deposits in the banking sector. Luckily enough for us, it was quite significant that our market share remained stable. That means that it was a systemic problem. Deposits fled from the banking sector but across the borders, all the banks were affected by that.

I must now turn my attention to the purpose of this meeting which is something different as it deals with the issue of integrating management of the banks. The previous speaker had few interesting hints. Unfortunately, I do not have interesting hints to show to you, just some hard facts and figures. But anyway, we came to Serbia in 2005; in 2006 we started our evaluation process, the Terminus process, when we revised all processes. In Fiat they had to revise production process. We have production as well, since we produce banking product. We had therefore to revise the main engine for producing our product, the credit process that we had to completely renew to distribute it. We then had the reorganization of our back office, and how to do the branding. Branding was one main message we had to give to the public in Serbia. All this was performed within the Terminus project that was carried out by an Italian specialist, plus approximately five fulltime employees and some clerks The team has been working for one full year over the various segments. Not the same people, but a multidisciplinary group of people working in different areas.

I think that Fiat will have more time and more FDI to configure. Then we had other events in the course of time. In 2007, we integrated and merged Panonska banka, which was a subsidiary of San Paolo Bank with which we merged in Italy. With this, suddenly some real management triggered, since now we had a new platform working in Serbia. We have now to put people in the position of managing the platform. We managed this through a delicate work involving thorough interaction with our parent company. We integrated regional management of resources to get acquainted with the practices. Practice is what we normally use as a synonym for platform. We have banking practices, and we want to enforce those that we have at the central entity, Pardeno level, and transplant them into the local operation. That is why we don't have the local manager, but the local manager has to be staying elsewhere to become fully acquainted and in line with the practices of ours. Of course, then we changed our project. We revised several times, used it, approved. Something you have to do in order to stay close to the market and here we are now, final step. We have achieved this governance alignment program that really is the banking governance program has to be the same that we apply elsewhere in the world. And we did that by introducing the project management office. We had some specifics regarding new directive in our bank group, particularly new members.

Finally we achieved what we wanted. Our Intesa-Paolo Group is not dogmatic. Instead we are open, we do not take a specific model and transplant it in the sense that everything from the way people speak to the way the product is sold complies with that. Products must have a local design but in line with some governance and general policy prescription that are dictated by the central offices. That's why we call it soft integration, not a strong integration. It is a model that gives a lot of space to the local management to design and devise their own strategy. I think it was quite successful model of integration.

Now we can see the inside, after three or four years. Results are speaking for themselves, and show our fast growth in lending, how fast our growth in deposit action, the number of clients introduced. We couldn't expect more than these actually. We are speaking about the number of customers and the amount before. It is difficult to increase the number of customers. And we have here performance indicators which are absolutely rewarding in any sense, including the efficiency, and the stability of efficiency. Operating cost grew, but there is lower base, which led us to the baby jump of the profit before terminus.

To conclude, the integration model we adopted was quite successful. Manager exchanges are quite regular, constant, let say daily. I could verify personally, because I sign everyday authorization for people to travel to Italy or elsewhere to get in touch with their peers. Definitely something we would have to consider about management training, what Mr. De Filippis mentioned before, the internal academy is one model, is one idea. I think that it could also be a possible project here in Serbia because it is definitely something that is adding value to the quality of our services. Probably we still have to take the last few steps to insure that investment, but it could be well in our perspective in few years.

Thank you.

BANCA INTESA

Banca Intesa Beograd

THE LEADING BANK IN SERBIA

Giancarlo Miranda - COO, Banca Intesa Beograd

Belgrade Banking Academy - June 22nd, 2009

INTESA SANPAOLO June 2009

Banca Intesa Beograd ('BIB') at a glance

Who we are... The Number 1 Bank in Serbia

- Number 1 by total assets with 14.7% market share
- Number 1 by total placements to customers with 15.4% market share
- Number 1 by total customer deposits with 16.5% market share

Moreover:

- We are present in all major cities in Serbia with 217 branches
- BIB is leader in number of POS (over 18.900) and ATM (240) and in electronic banking and payment card operations for a long time
- Leader in payment cards, with over 1.000.000 issued cards, largest POS and ATM network
- We employ more than 3.000 staff

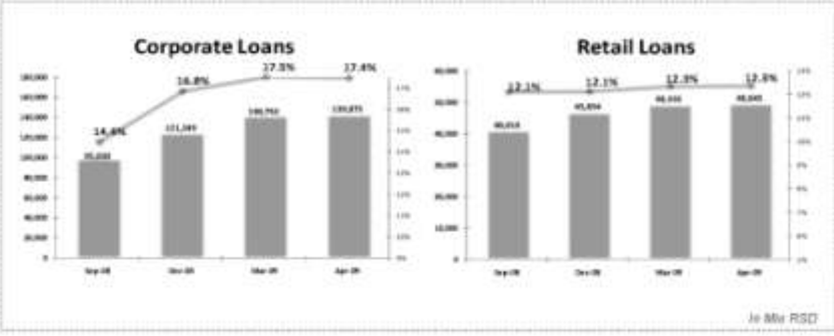
BANCA INTESA

BIB: a domestic leader in placements to clients

Source: National Bank of Serbia

3 BANCA INTESA

Banca Intesa Beograd: market share by segments – corporate and retail



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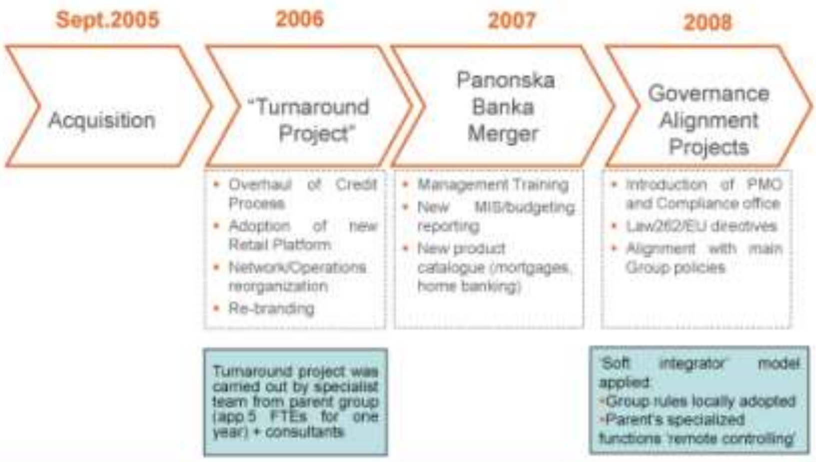
Banca Intesa Beograd: market share by segments – corporate and retail

5

BIB and Gruppo Intesa Sanpaolo – Steps Toward Integration



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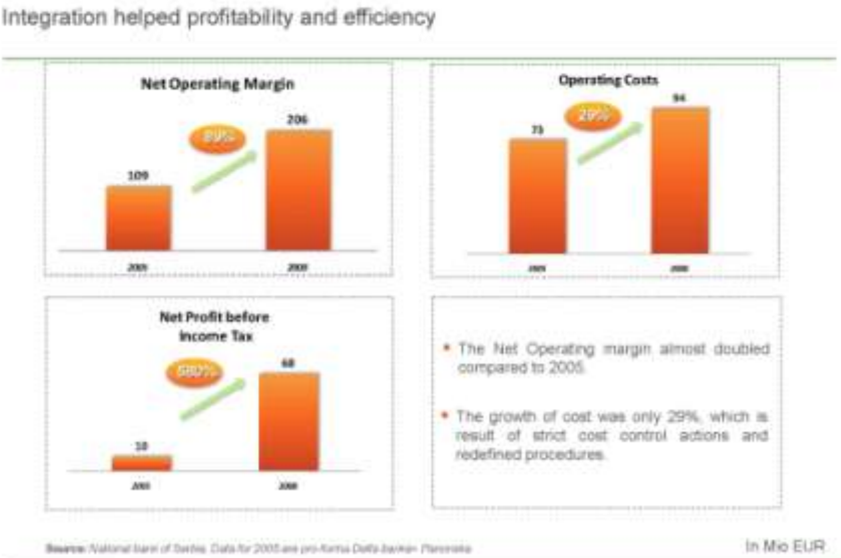
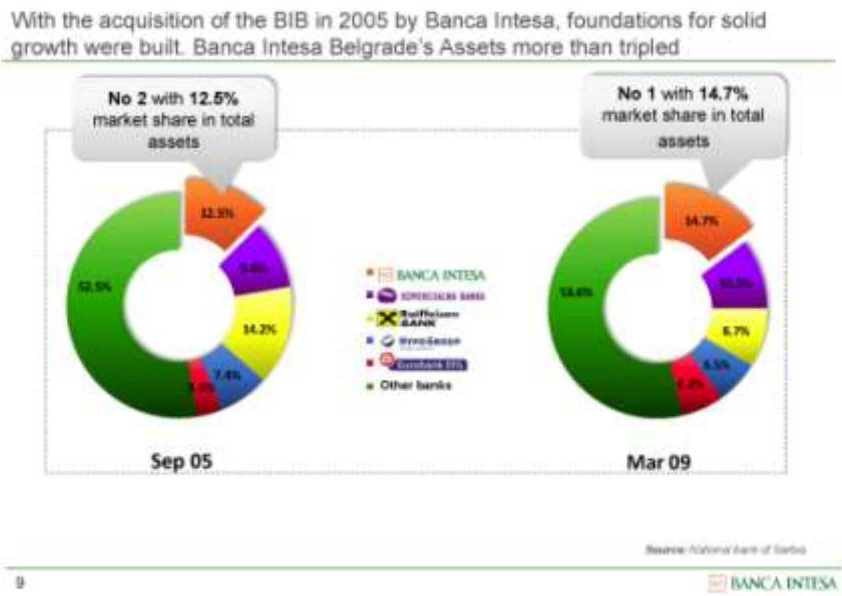
BIB managed to maintained its leading position in wholesale banking simultaneously transforming into a top retail player in mass market
Placement to Clients
1,857
485
Liabilities to Clients
Number of Clients in Millions
1.1
1.4
27%
Retail lending share increased from 8% in 2005 to 12%
In the same period, capital increased to EUR 480 Mio
In Mio EUR
7
BANCA INTESA


Integration helped profitability and efficiency
Net Operating Margin
109
206
89%
Operating Costs
73
94
29%
Net Profit before Income Tax
10
68
580%
The Net Operating margin almost doubled compared to 2005
The growth of cost was only 29%, which is result of strict cost control actions and redefined procedures
In Mio EUR


With the acquisition of the BIB in 2005 by Banca Intesa, foundations for solid growth were built. Banca Intesa Belgrade's Assets more than tripled
No 2 with 12.5% market share in total assets
No 1 with 14.7% market share in total assets
12.5%
52.5%
14.2%
7.4%
14.7%
6.7%
BANCA INTESA
Raiffeisen BANK
Other banks
Sep 05
Mar 09
9
BANCA INTESA

Dr. Christian NEU
Deputy General Manager of the Fondiaria - SAI group

Ladies and gentlemen,

I am very honored to be invited to this event and I am very glad to be given the opportunity to elaborate shortly on the considerations of foreign investments in the Serbian insurance sector. I represent Fondiaria SAI, a company which most of you might never have heard of. To increase the familiarity, we will first focus on an overview of the group by glancing at some slides that you will find for your convenience and closer analysis in the Conference proceedings.

Fondiaria is one of the three big insurance groups in Italy, with a turnover of 12 billion Euros. About 30% of the total is in life insurance, 50% in car insurance, the rest other types of insurance business. Our group acquired a bit more then a year ago a DDOR Novi Sad in Serbia, and this is the general background of our situation. With the 12 billion turn-over, Fondiaria SAI is the 11th insurance group in Europe.

Among groups of this size, Fondiaria is, maybe not the only one, but one of very few, which was until recently very much concentrated on its domestic market. So, three years ago we decided to diversify geographically our group. And, we find a number of criteria with regards to this diversification.

We wanted to make not just one acquisition aboard but several of them. We have basically an amount of one billion Euros earmarked for our geographic diversification, one billion Euros without leverage. With leverage we are talking about let say 2 billion Euros. We wanted to invest into countries which were not too far away from Italy, neither from a geographically nor from a cultural point of view. We wanted to get involved in the growing markets not on over saturated markets, and we wanted to invest in markets which were neither too small nor too big for our project. Not too big, for example going to Russia, going to China with 2 billion Euros. It doesn’t make sense it not enough. Going to markets like the three Baltic States doesn’t make much sense either, because these are too small. So, we were looking at something in between and we quickly looked towards South-Eastern Europe: the Balkans, Turkey, Romania.

And there was one more important criterion. We said we didn’t want to invest into a foreign company which is marginal in its own market. So we said we wanted to buy a company in the foreign market but it should be the leading company in its own markets.

So, when we applied all these criteria, to certain extent your project becomes opportunity. We looked at other countries in this region. We looked at Serbia, but in the end it was opportunity that brought us to Serbia because when DDOR Novi Sad was privatized we looked at the company. We liked it and this brought us into this dimension.

The second topic I want to address deals with how we looked at the Serbian market when we started our project. The following slides represent a view of Serbia market as of, let say, one or two years ago.

I came to this country for a year and bit more now, on average two days a week and I can say that I am more positive about the situation in this country than most of investors and international organizations would tell you. When we are looking at Serbia we clearly take a glance on its future development. Our overall impression was that Serbia had underperformed, had not lived up to its possibilities for many, many years. Serbia fifteen, twenty years ago was the country in this region with the highest living standards. And, then for a number of reasons which you know better than me, the country got entangled in many, many problems in many respects. So, we clearly we took a bet on political stabilization and on clear orientation of the country towards the European Union. And, we took a bet on substantial foreign investment to be made in this country.

We were then positive, we were optimists about political development, we were positive about the economical evolution of the country even now when the world wide financial crisis has changed the picture a little bit. The crisis is not over yet, and nobody can predict today how it will end. But it's a problem for everyone, and we still think that if Serbia uses its chances intelligently, and if Serbia uses its options wisely in this situation it is well prepared to get out of the crises better or at least not worse than many other countries in this region. As a result we think that in the medium term the overall economic situation in the country will really improve, can only improve and will continue to be very happy about the overall situation.

Let me now briefly comment on the data that you will find in the presentation. I don't want to elaborate on these details now. Let me just talk briefly about the prospects and the situation of the Serbian insurance market. The Serbian insurance market is relatively small, since the sum of all premiums on this market is just five hundred fifty million Euros, which is less than half of what Croatia has, and roughly less than one third of what Slovenia has. Nowadays we measure the size of insurance market in what we call penetration. That is the percentage of insurance premium of overall cross-national program and here Serbia we have a rate of just 1.8% compared to 8% in Western Europe. This is a market which we could call uninsured, and therefore a market with a considerable growth potential. We expect in the next year despite of the crisis a growth in very basic insurance products like fire insurance and things like that. But we also expect a growth in very sophisticated lines of business like life insurance and pension insurance because this country heavily relies on social pension insurance which have become unsustainable in many, many countries and also people in this country will want to save more for their old age.

So, we are happy also with regards to the evolution of the Serbian insurance market as such. We also like the overall structure. There are number of insurance companies but basically the market is in the hands of few. Insurance is volume based: big volumes, with rather small margins. So, if you are too small you become irrelevant, and do not make too much sense. In the country 80% of the market is in the hands of three or four companies which, of course, generate though competition, on the other hand, also it is clearly that all of these major competitors abide by the same rules, they respect the laws of gravity, the laws of economics in our business. So, from this point of view we think the market is really well based.

Now I would like to comment for a moment about our investment in Serbia, our subsidiary in Novi Sad. You look at the company with a balance sheet of around 160 million euro, a premium income of around 150 million Euros, around 2200 employees and what we call a combined ratio. Combined ratio is important performance indicator. In insurance industry it simply is the claims and administration cost expressed as a percentage of premium income. This company, more or less like the rest of the market, runs with combined ratio of slightly above 100% meaning that for every premium, we pay around 75% claims and 30% of administration cost. So, our claims and costs are slightly higher than our premium income and we must find a remedy for this with the investments income of the company. These are economic data that apply not only to our company, they relate to the entire insurance industry. It is a market with a very small margin, in many, many cases negative margin to insurance companies.

I will speak now briefly about problems of this company. As the problems of our subsidiary that are similar to those of the whole insurance market and in some respect of other markets in this country. Our subsidiary, when we took over it was organized in extremely complicated way. I have seen a similar situation in other business in this country. It was heavily decentralize despite the fact the company turnover amounted to about 150 million euro, which is small volume for our business. Instead of being organized as efficiently and simply as possible, this company was organized, in a way that was as complex as possible. It was also heavily decentralized, with 25 branch offices around the country. Each branch seemed to me a kind of autonomous republic with no incentives on sale. This needed to be reorganized completely. We have a reorganization project underway which relies heavily on centralization. We are centralizing all that can be centralized, through intensification of central controlling in terms of planning, and leaving decentralized just the things which can't be centralized. In a centralized framework we consider our being locally present as an important asset. These are, basically our sales people, the people who sell the policies, who advise the clients. These have to be locally disbursed, present in as many places as possible. But, most of the back office has to be centralized to bring down the cost.

I told you about combined ratio which claims and administration cost relative to premium income. Costs in this country in the insurance sector run at 35, in some case even 40%. In more developed markets, 22%, 23% is not the best practice, but it is acceptable. You see then how far away we still have to go in order to achieve a degree of efficiency which is normal in other markets. But, I am optimistic also in this respect. Even though, restructuring can be painful, it certain cases is inevitable. And, I have found in the subsidiary a decent amount of people, who understand that, and people who are willing, and qualified to drive for change. And, this is for me the most important of many positive aspects we have found with our new foreign investment in this country.

This is my short presentation about our venture in Serbia. I wish you well for the continuation of your master studies. I got a masters degree from New York University, and I remember very well and with great pleasure the years of those studies, On the commencement day, the then Chairman of U.S. Federal Reserve, Mr. Paul Walker, ended his speech with the words that a "master program is as good as the jobs the country finds afterwards". In this respect I just wanted to let you know that we are a significant foreign investor in this country. We are looking for qualified people willing to drive for change. So, I just wanted to let you know that, and in case you are interested you can always talk to us.

Thank you very much!

Considerations of a Foreign Investor in the Serbian Insurance Market

DDOR NOVI SAD — GRUPPO SAI FONDIARIA

Belgrade Banking Academy

June 22, 2009

FONDIARIA-SAI GROUP OVERVIEW

Group Profile

- **Fondiaria-Sai** is a market leader in the Italian insurance industry and the parent company of one of the country's largest insurance groups.
- Fondiaria-Sai Group is made up of more than 100 subsidiary and affiliated companies, operating not only in the insurance, finance and banking sectors, but also in real estate, agriculture, health, assistance and services.
- The Group originated at the end of 2002 form the merger between two historical Italian players in Property & Casualty market (SAI and La Fondiaria) and is mainly focused on P&C business and specially Motor TPL.

Insurance

- In 2008, with written premiums of 11,5 billion Euro and a customer base of over 8 million clients, Fondiaria Sai ranked as the 2° largest insurance group in Italy.
- The Group operates in the insurance sector through two companies quoted on the Italian Stock Exchange: the parent company FondiariaSai and Milano Assicurazioni and through a number of specialist companies operating in specific market sectors; among which: Siat in Marine Insurance,Liguria Assicurazioni & Liguria Vita, Systema and Capitalia Insurance in Bancassurance, Dialogo (direct distribution channel motor/health/accident), Europa Tutela Giudiziaria in Legal Insurance, The Lawrence Re Ireland Ltd in Reinsurance.

Finance

- The Group's main shareholder - Premafin Finanziaria S.p.A is also a key investor in the Italian financial system.

Banking

- The Group is active in financial sector through its own bank, BancaSai and Asset Management through SAI-A.M. SGR with its Mutual Investment Funds and Personal Portfolio Management.

Real Estate

Services

- Assistance services are offered by Pronto Assistance, Consultancy and IT services through Scai and Starvox, Agricultural Estates through Saiagricola, Real Estate assets managed directly by FonSai Group after acquisition of Immobiliare Lombarda (2008).
- In 2008 FondiariaSai acquired ATA Hotel S.p.A – one of main hotel resorts in Italy.

International Presence

- On January 31, 2008 FondiariaSai acquired 83,32% stake in the share capital of DDOR Novi Sad than, in October 2008 another 15,9% and the whole process was finalized on December 9,2008 when FondiariaSai became the sole owner of DDOR Novi Sad.

FONDIARIA-SAI GROUP KEY FINANCIAL DATA 2008

Key Business Data 2008 — Eur mln

Fondiaria-Sai Group	2008	2007	Cge.%
Total premiums written	11,506.4	11,882.3	(-3.2)
Consolidated profit	98.8	628.1	(n.s.)
Group net profit	87.4	507.8	(n.s.)
Combined Operating Ratios Cons.	96,1%	92,1%	
Combined Cons.Ratio	98,6%	94,8%	
Proposed dividend per ordinary share	0,78	1,18	(-0,40)
Proposed dividend per saving share	0,792	1,192	(-0,40)
Group net equity	3,098	5,171	
Equity attributable to the Group	2,935	3,858	

Premium split — Eur mln

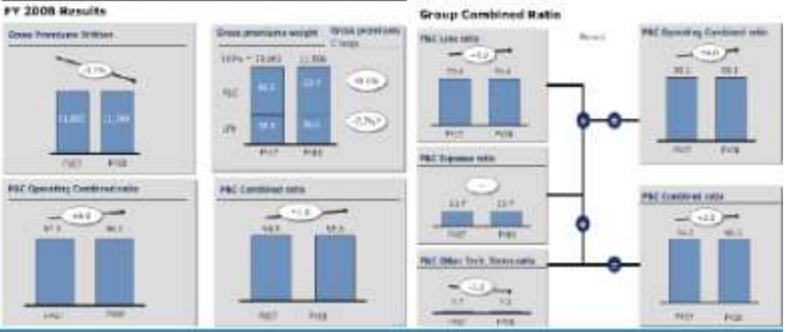
Direct & Indirect premiums	11,506.4
Consolidated direct premiums written	11,490
Non-Life direct premium	7,286
Life direct premium	4,206

Solvency Margin

Solvency I	Solvency II	Capital Model	
1.3	1.5	ca 112%	(x)/%
[illegible]	1,300	400	Eur/mln

FY 2008 Results

Group Combined Ratio



Perspective on the Serbian economic and political landscape

Current situation

- Serbia has experienced **a growing economy over the past 8 years** (GDP growth of 6% per year since 2002) ranking among the highest in the South Eastern European countries; the economic growth was mainly driven by:
  - Increase in **international business/ trade**, in particular FDI with the entry of major international companies
  - Natural catch up effect of the **domestic demand** after recent wars
  - **Development of strategic sectors** with structural competitive advantage
- The Government has reached a good level of **political stability** with the establishment in 2007 of the **Democratic Party** and it is pursuing the strategy to fulfill all the requirements to be accepted in the European Union

Future perspectives

- Going forward, **substantial growth is expected** to continue (5-6% p.a), mainly thanks to productivity improvement driven by:
  - **Shift of the economy** from low-productivity sectors (e.g., agriculture) into higher-productivity sectors (e.g., construction, services)
  - Expected **fiscal reforms**, increase of the **market liberalization** and **privatization**
  - Government plans to **develop/improve infrastructures**
  - **Domestic demand increase** driven by a stable social/political environment and the increase of the salary level

Potential challenges

- Despite strong fundamentals, **several key challenges** need to be addressed by local Government in order to meet the growth expectations:
  - **High unemployment rates** which can lead to social unrest
  - **Slow down of FDIs** (mainly caused by the global financial/liquidity crisis) which can impact of the privatization plans of the local Government
  - **Slow down of the infrastructure upgrade** leading to low productivity level
  - **Low savings rate** causing large current account unbalances financed through the rapid increase of indebtness (current public debt equal to 37 as % of GDP)
  - Control of the **currency exchange rate vs Euro** which might be suffering in the next few years (2009-10) due to relevant Government's exposition to FDIs to balance country expenditure

Serbia has experienced a significant growth in the past 5 years and it is the largest but the poorest in the Region...

BACK UP

Country	Population Millions, 2007	GDP per capita '000 EUR, 2007	Historic GDP growth CAGR 02-07	GDP weight per sector** %, 2008E
Serbia	7,5	4,0	5,9	12 / 24 / 64
Croatia	4,6	8,5	4,8	17 / 29 / 54
Slovenia	2,0	16,3	4,6	2 / 34 / 64
Bosnia & Herzegovina	3,9	3,3	5,7	10 / 24 / 66
Total SEE countries*	**25,8**	**5,0**	**4,9**	**13 / 28 / 59**

* Including: Serbia, Slovenia, Croatia, Bosnia & Herzegovina, Macedonia, Albania, Montenegro and Kosovo
** Agriculture / Industry / Services
Source: IMF; European Commission; CIA World FactBook, Global Insight, team analysis

In the future, growth is expected to continue as political and economic stability increases

BACK UP

Country	GDP growth, CAGR 2007 – 2012, %	*(CAGR 2002-2007, %)*	Additional observations
Serbia	5,3	*(5,9)*	• Large amount of historical baggage (e.g., war crimes, Kosovo independence) • New government led by pro-Western parties has the best chance of turning the page on the past in many years
Croatia	3,3	*(4,8)*	• EU candidate in advanced stage of negotiations • Relatively good political and economic stability; with remains of protectionism
Slovenia	2,9	*(4,6)*	• EU member • Most advanced of the East European EU entrants
Bosnia & Herzegovina	5,2	*(5,7)*	• Country divided into two semi-independent units and multiple kantons • Separate entities typically required to run business in both parts of the country • Low political stability, government near insolvency, potential for country to split
Average SEE countries*	**4,2**	***(4,9)***	

* Including: Serbia, Slovenia, Croatia, Bosnia & Herzegovina, Macedonia, Albania, Montenegro and Kosovo
Source: IMF, European Commission; Global Insight; team analysis

Additional macro-economic/demographic indicators
2008E

BACK UP

Country	Unemployment rate 2007 %	Doing Business Ranking 2008	Doing Business Ranking 2009	Gross fixed investment % of GDP	Public debt % of GDP	Current account balance % of GDP	Inflation rate %
Serbia	19	91	94	20	22	-12	7
Croatia	10	107	106	32	49	-10	6
Slovenia	8	64	54	28	37	-6	6
Bosnia & Herzegovina	39*	117	119	N.a.	40	-15	8

* 2007 estimate
** Official unemployment rate is 12% but including subsistence farming the rate can exceed 30%
*** 2007 data
Source: CIA World Factbook, Doing Business 2009

Perspective on the Serbian insurance market

Current situation
- The **Serbian Insurance Market** has experienced **significant growth** (~9% CAGR) over the past 5 years, although:
  - It is much smaller compared to CEE and West European countries
  - It is largely **dominated by traditional channels** (tied-agents, branches)
- The market competitive landscape is characterized by:
  - **Relatively high concentration**, with top 3 players holding 69% of market share
  - Specialized operators in the motor market raising the competition and driving down the profitability especially in the MTPL line of business
  - Presence of several small/mid-sized players with no distinctive value propositions beyond basic execution

Future perspectives
- The Serbian Insurance market is still **attractive** with expected grow rate of **10% per year in next 5 years**
- **Current low penetration** should gradually disappear allowing the market to converge to Western European standards, thanks to:
  - Development of key drivers of insurance penetration (e.g., **car penetration** increase)
  - **Fiscal and structural reforms** underway – especially the pension and health systems - that will probably facilitate the penetration of the Insurance products
  - Improvement of the **insurance product offering** (standard product at the very early stages) to grow especially the retail business
- **Further concentration** of the market with potential exit of small players

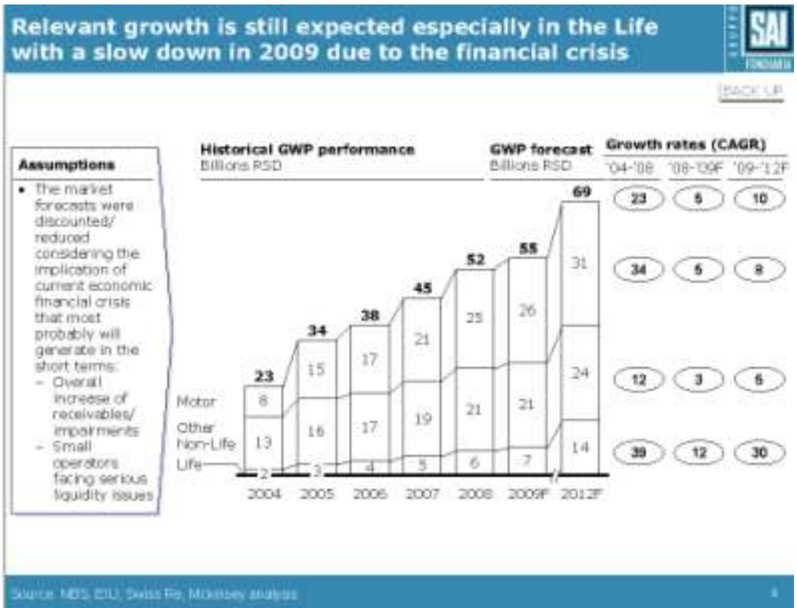
Potential challenges
- Despite solid mid-term growth expectations, the insurance market will be hit in the short terms by current economic and financial crisis, generating:
  - **Limited overall grow rate in 2009** (3-5%)
  - Reduced profitability
  - Relevant increase of receivables and impairments
  - Small operators facing relevant liquidity issues

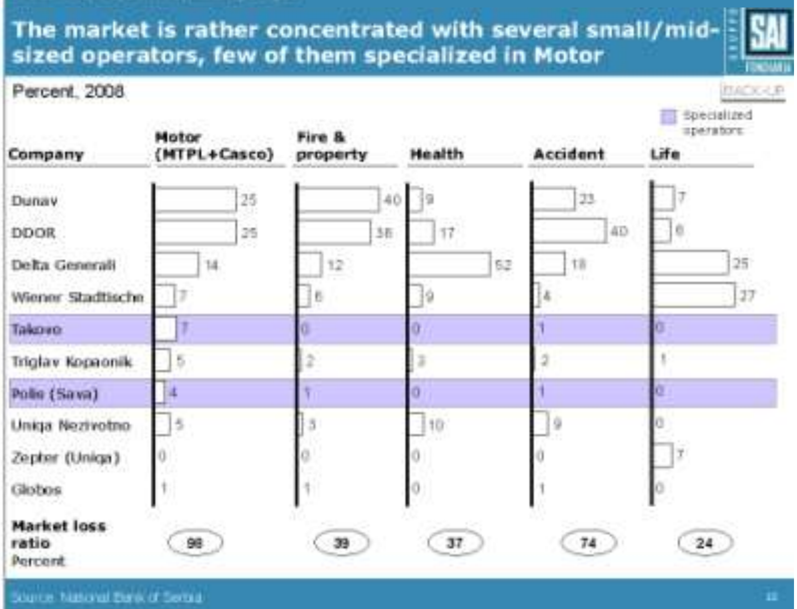
The Serbian insurance market is a fast-growing with a relevant gap of penetration compared to Western Europe

BACK UP

Country	GWP, 2007 EUR million	Historical GWP growth CAGR 2002-07	Expected GWP growth CAGR 2008-12	Penetration 2007 GWP/GDP
Serbia	548	9	10	1.8
Croatia	1,234	10	8	3.3
Slovenia	1,894	10	8	5.8
Bosnia	206	9	9	1.2
SEE countries*	4,529	10	9	N.a.
CEE countries	38,768	13	11	N.a.
Western Europe**	1,133,831	5	5	8.1

* Including: Serbia, Slovenia, Croatia, Bosnia & Herzegovina, Macedonia, Albania, Montenegro and Kosovo
** Western Europe includes 17 countries with total population of 404 mn
Source: Swiss Re, national insurance supervisory bodies, insurers' associations, McKinsey analysis



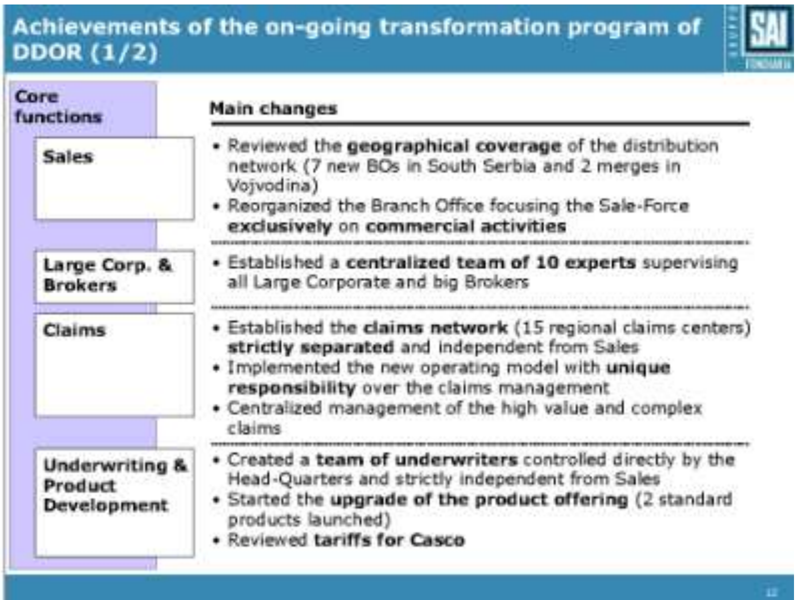


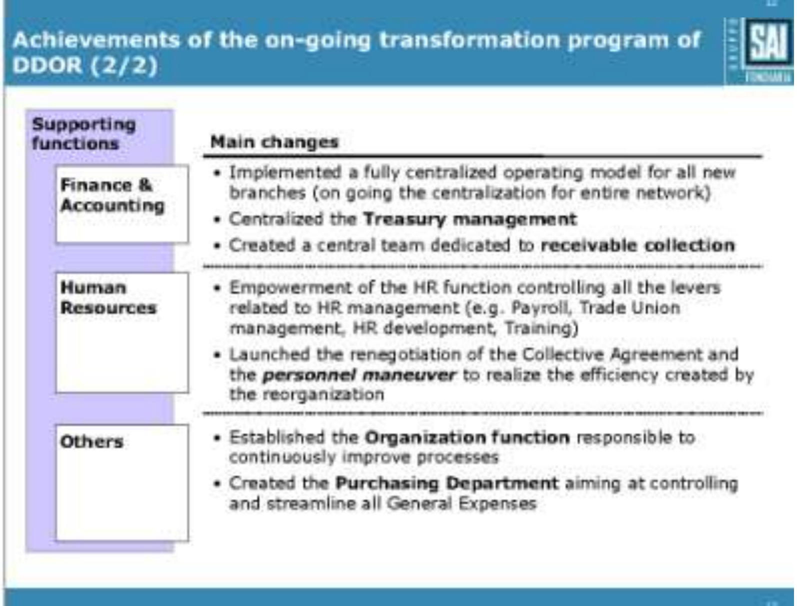
DDOR performances in 2008 - key financial data

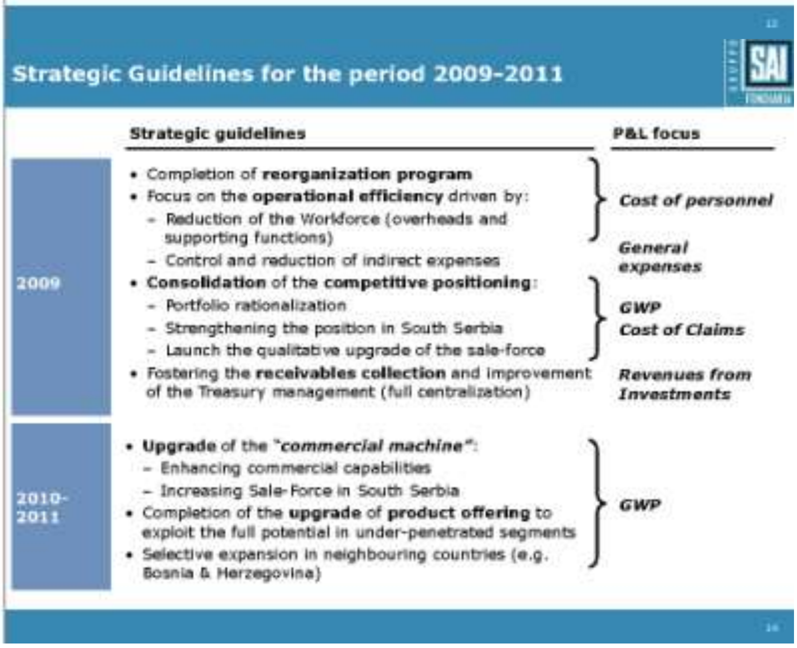
Data in million RSD, Per cent

		2007	2008	2008 vs 2007
Balance Sheet	**Total Assets**	**14,488**	**15,285**	**+5.5**
	Property, Plant & Equipment	4,332	5,237	+21.2
	Equity investments	3,175	710	-77.6
	Receivable	2,648	3,059	+15.5
	Total technical reserves	9,075	11,414	+25.8
	Equity & capital reserves	4,286	2,706	-36.9
Income Statement	**GWP**	**12,627**	**13,100**	**+3.8**
	Cost of claims	7,855	8,421	+7.2
	Acquisition & administration expenses	4,435	4,491	+1.3
	Net technical results	-956	-517	N.a.
	Net Income	294	38	-86.9
Key Ratios	Claims ratio	70.3%	68.8%	
	Expenses ratio	39.7%	36.7%	
	Combined ratio	110.0%	105.5%	
	ROE	6.9%	1.1%	

Source: DDOR Accounting and Strategic Planning


Achievements of the on-going transformation program of DDOR (1/2)
SAI
Core functions
Main changes
Sales
• Reviewed the geographical coverage of the distribution network (7 new BOs in South Serbia and 2 merges in Vojvodina)
• Reorganized the Branch Office focusing the Sale-Force exclusively on commercial activities
Large Corp. & Brokers
• Established a centralized team of 10 experts supervising all Large Corporate and big Brokers
Claims
• Established the claims network (15 regional claims centers) strictly separated and independent from Sales
• Implemented the new operating model with unique responsibility over the claims management
• Centralized management of the high value and complex claims
Underwriting & Product Development
• Created a team of underwriters controlled directly by the Head-Quarters and strictly independent from Sales
• Started the upgrade of the product offering (2 standard products launched)
• Reviewed tariffs for Casco


Achievements of the on-going transformation program of DDOR (2/2)
SAI
Supporting functions
Main changes
Finance & Accounting
• Implemented a fully centralized operating model for all new branches (on going the centralization for entire network)
• Centralized the Treasury management
• Created a central team dedicated to receivable collection
Human Resources
• Empowerment of the HR function controlling all the levers related to HR management (e.g. Payroll, Trade Union management, HR development, Training)
• Launched the renegotiation of the Collective Agreement and the personnel maneuver to realize the efficiency created by the reorganization
Others
• Established the Organization function responsible to continuously improve processes
• Created the Purchasing Department aiming at controlling and streamline all General Expenses


Strategic Guidelines for the period 2009-2011
SAI
Strategic guidelines
P&L focus
2009
• Completion of reorganization program
• Focus on the operational efficiency driven by:
– Reduction of the Workforce (overheads and supporting functions)
– Control and reduction of indirect expenses
• Consolidation of the competitive positioning:
– Portfolio rationalization
– Strengthening the position in South Serbia
– Launch the qualitative upgrade of the sale-force
• Fostering the receivables collection and improvement of the Treasury management (full centralization)
Cost of personnel
General expenses
GWP
Cost of Claims
Revenues from Investments
2010-2011
• Upgrade of the "commercial machine":
– Enhancing commercial capabilities
– Increasing Sale-Force in South Serbia
• Completion of the upgrade of product offering to exploit the full potential in under-penetrated segments
• Selective expansion in neighbouring countries (e.g. Bosnia & Herzegovina)
GWP

Dr. Ivano CANTERI
Global Marketing Manager, Centro Estereo per l'Internazionalizzazione, PIEMONTE

Thank you very much ladies and gentlemen for inviting me to this seminar; it is key for the development of the activities of organisations like the one I represent to attend as much as possible, as many times as possible, this sort of events.

I have to say that, in order to leave sufficient room to other speeches and save everybody's time I'll try to keep mine to five minutes so that the discussion can carry on on topics much more focused on today's theme.

As a matter of fact, my speech is a bit eccentric compared to those presented by all the other distinguished guests who spoke before me. The reason for this is that I represent a public body which has been founded by the Regional Government of Piemonte, northwest of Italy, and the Union of Chambers of Commerce of this region. Ceipiemonte (Piemonte Agency) is a body entrusted with the task of working to increase the international exposition of our economic system – internationalisation of the region.

Such a task means to be able to work on the two "sides of the coin" which is, let's say, on the one hand to boost the ability of our own companies to get international – helping them to create relationships, common ventures, co-operations, cross border research and development and, on the other hand to increase the flow of investments from other geographical areas to Piemonte. This is why we do not talk about "import" and "export" as this emphasizes the commercial side which is not, in itself, a proof of real ability for a territory to be open to the global market.

Bearing this in mind, this is really why I am here today: just to tell you just a bit about our Regional Government and Chambers of Commerce approach to the problem of boosting or supporting its economic development through what is called as internationalisation.

Our agency, which has been created in 2006, it is not exactly a brand new initiative because it gathers together the experience of some former organisations which were entrusted with different areas of involvement in economic development at the international level.

These organisations were working in five different areas which took a new shape inside Piemonte Agency now embodied by departments entrusted with different tasks in promoting the international presence of Piemonte: Business Promotion, Inward Investment, Tourism, Agri-food Marketing, Foreign Trade Training. I am personally in charge of the global marketing management inside the Inward Investment Department, which is the one entrusted with attracting investments from foreign countries. But what my team is significantly involved in is the co-operation with the other departments of our Agency as we reckon that the international marketing can get fully-fledged only by approaching the matter of internationalisation both ways: in and out. There is nothing like a company uniquely interested in going somewhere without having an interest in developing strong connections with the local economic and industrial environment and this one cannot live, even exist in today's world, without being projected outside its borders, no matter how far or long they are.

Thus, in many ways I am also involved in promoting the activity of our colleagues from the business promotion division which is the one which is probably most important to focus on today.

Just a few words, some basics about the creation of this organisation. The promoting members of the agency (the Union of the Chambers of Commerce and the Regional Government of Piemonte) they both own 48% of the shares.

But what I would like to underline is the fact that under the assumption that the synergies between all the so-called "stakeholders" acting at various degrees of involvement in the economic, social, industrial and academic fabric of a territory are key to any action willing to be successful in boosting local development, the project, I mean Piemonte Agency, is based on having as many institutions of this sort as possible involved in the process. This accounts for the presence in the minority shareholding of these other crucial members like our national banking association, three universities of our region; (University of Turin, University of Eastern Piemonte and Polytechnic School of Turin), palities, provincial governments, entrepreneurial associations, and so on.

This body and its "architecture" are unique in Italy, as well as the services and policies implemented and integrated by Piemonte Agency.

Speeding up to the end of my speech, let's get into this slide because it may be of your interest with special regards to the topics discussed toady. As I was saying two main areas of action of Piemonte Agency are the Inward Investment division which is aimed at attracting foreign investment and the second but not least one is the Business Promotion division.

I want to point out a couple of remarks on the Business Promotion department of the Agency: this is the area with the longest of experience and tradition amongst all the departments. You remember that Piemonte Agency is the result of the merger of all these different bodies…..one of the bodies was originally the Foreign Trade Center of the Chambers of Commerce of Piemonte from which the Business Promotion department took shape; this was founded about 35 years ago and during all of these years this working team developed very close relationship with a number of countries especially when talking about Europe and its Eastern regions as the Balkans.

In addition, part of the activity which is run by the Business Promotion side is what we call long-term projects. These are specially funded project which are focused on specific sectors and industries. And for the first one of these, From Concept to Car won, just two weeks ago in Kuala Lumpur in Malaysia, the prize for the best chamber of commerce project worldwide aimed at boosting the international growth of a specific industrial sector.

Simply put, this gathers together 150 most advanced companies producing components for the automotive industry. And important thing is to allow these people to get in touch with other companies and to do things together.

I am stressing this because due to this new fear in the market we heard about this morning with special regards to the automotive industry, I do believe that you soon will see many opportunities to get to know companies coming from our area under the umbrella of this project, companies trying to establish relationship with the local community.

Getting to the end, clearly the work of our agency is not exclusively focused on the automotive sector: by responding to Regional and territorial policies our efforts are aimed also to biotech, nanotech, renewable energy and environment and the ICT sector, just to mention the main ones. I hope we have the chance of meeting again soon on the base of some common project or initiative.

Thank you very much to you all.

Prof. Valter CANTINO
Dean, Scuola di Amministrazione Aziendale dell'Università degli Studi di Torino

Conveying knowledge to complex environments: how to think about new educational paths for managerial education for the academic community

It is indeed a great pleasure to be here, to work in close relation with the Belgrade Banking Academy and with important Italian and Serbian institutions, with the common aim to share our knowledge in management and financial education, to support the development of our institutions and of course of our countries, in this critical time characterized by the global crisis.

The previous speakers explained how the BUONA project has been a good beginning, and I am sure that we will be equally successful in the implementation of new projects involving new partners in the near future.

This conference therefore provides a good example of our way to build an education project where bringing together the competencies of companies and universities efficient and effective results can be achieved.

The role of the government and of other public institutions to will of course be very important in the development and in the support of new and adequate educational programs.

This is particularly important in periods like the present one. The deeps crisis that is affecting the world require forceful reactions, and education, through the acquisition of upgraded skills and competencies in general and in the field of management education can play a crucial role.

I will therefore contribute to this important issue by providing you a brief description of the history that can be useful to prove our ability to support your country in this challenging but necessary task.

I will then share with you the main lines of development that we envisage for the future of management education. I will conclude by describing the concrete actions that we have taken in order to insure an up to date educational program

The Scuola di Amministrazione Aziendale (SAA) is a management school that was founded in Turin in 1957, 52 years ago with the mission to train women and man for managerial positions in a growing business sphere. A remarkable feature of the SAA offer was from the onset a strong cooperation between academia and business in the design of the programs and in the delivery of classes. Considering the time of establishment, just 12 years after the end of Second World War, this has been a pioneering vision that was proven right by the subsequent developments.

Our first degree was in business administration. It was a very intensive course concentrated in two years - compared with what was normally taught in four academic years at the Faculty of Economics.

The same degree was organized on a part time basis a few years later for working people to create a school of management for managers.

In December 1963 the school became a member of the University of Turin as a school designed for specific studies in the area of management.

I bring to your attention that the University of Turin is now one of the biggest universities in Italy we have more than 60 thousand students at 13 faculties, 65 departments and many other research centres. For the second consecutive year, the University of Turin has been ranked number one in the category of the big universities in Italy.

The MBA program was launched in 1978 and has been operating ever since Our MBA program is one of the oldest in Italy. It is a post graduate university course in general business management created on the models of the most prestigious European and American schools of management.

Recently the extraordinary times we are living, characterized by the impact of globalization on the corporate scenario and by the dramatic increase in the dimension of risk affecting the financial markets first and the real economy afterwards have lead us to a serious review of the basic features of the educational model, in order to insure its consistency with the new requirements.

The basic conclusions that we have reached is that periods of economic turmoil provide the unique opportunity of redesigning management education in terms of career paths with the "maintenance" and the broadening of knowledge. The strengthening of managerial competencies will prove to be a strong competitive hedge as soon as the economic cycle turns around. The "must" therefore is to be found in the guarantee of a future employability, a feature that adds to the social role of those who carry out the investment. This also brings to the people attention the care devoted to growth and contributes to lessen the anxiety stemming from the uncertainty about the future.

We need therefore to identify new educational models that are a real answer in supporting the individual change in order to enforce new growth paths.

The challenge is to make available the "knowledge endowment" that is resident within each one of us operating within a group (classroom or work environment), to share it with others. Lecturers must therefore change their attitude of owners of knowledge and make themselves available to the group as facilitators of the best practices that often are not resident in one person but must be broken down into their elementary components and reassembled into complex schemes through a process shared by a plurality of people.

In this environment, the development of a new educational path requires that great attention be devoted to the environment and to the didactic methodologies that must become decreasingly bound to the physical space. At the same time, however, they must increasingly become the "space" that facilitates the feelings of contact with the others in order to support a communication tuning that is found in the "social network". Didactic methodologies must move from the one way delivery approach towards a shared style in order to empower and sustain the circulation of knowledge.

Together with the didactic methodologies, universities that pursue excellence must develop the research according to models of accreditation and of quality control. Attainment of quality becomes essential in the models of economic sustainability and of teachers' promotion. The care devoted to the "clients" becomes an "ethical" and economic driver for an education that seeks solid theoretical foundation to support decision making.

For this reason it is necessary to involve those who possess managerial knowledge regardless of their academic standing to define the content of the educational paths and the modes of their delivery.

The challenge ahead for tomorrow's educators can be met if one is enabled to develop knowledge within complex and interdisciplinary environments. In higher education the ideal setting is to be found in the doctoral schools that must be involved not only in the scientific growth of the individual. But also develop science communication methodologies that become precious when a person is involved in the path described above

A strong cross feeding between academia and business society is found within the university incubators, where PhD students introduced in the incubated companies can live a unique experience. This will allow them to increase today their individual managerial skills that will be so important to blend the academic and institutional worlds. Tomorrow those PhDs that will continue in their academic career will be able to explain not only the theoretical foundations of the discipline, but also the operational environments within which they develop.

The basic features of our new vision are summarized below.

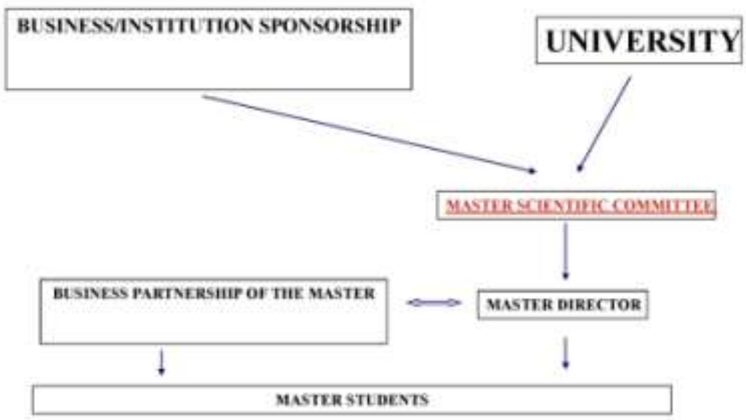
The role of management and financial education

Prof. Valter Cantino

Dean of the School of Management University of Torino

Area of activities

Planning and integration in managerial training processes: "Master" model



SAA — UNIVERSITÀ DEGLI STUDI DI TORINO / UNIVERSITY OF TURIN

Our focus on people in training programs

Companies are focused on **middle management** competencies and skills which a particular attention on :

- **Followership style**
- **Accountability process**
- **Execution and delivery**

SAA — UNIVERSITÀ DEGLI STUDI DI TORINO / UNIVERSITY OF TURIN

No more "talents for life" but "improvement in an incubator" (growing in a sustainable way step by step)

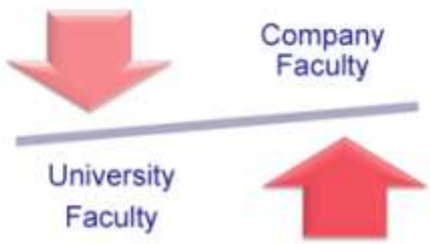
The " **incubator** "model is focused on:

- **Value**: giving value and empowering value to the people .
- **Speed**: training programs and projects are based on **a "fast track"** to accelerate career and knowledge improvement of the people
- **Visibility**: confirming to the management the potential and followership of the people with an outstanding evaluation

SAA — UNIVERSITÀ DEGLI STUDI DI TORINO / UNIVERSITY OF TURIN

Continuous improvement structures

- Balancing and reinforcing the link from University and Company building a continuous improvement platform with the contribution of both Universities Academic programs, research experiences and Companies best practices
- Building a "**Open University**" integrating the "**Corporate University**" model in which the School of Management is playing as "knowledge system integrator" and the Company acting as continuous "testing place"



Part II.

BASIC INFORMATION ON MASTER&MBA STUDY PROGRAM DEVELOPED WITHIN BUONA TEMPUS PROJECT

GRADUATE MASTER & MBA STUDIES: FINANCIAL BANKING AND BUSINESS MANAGEMENT (MMB)

After less than one year of cooperation within the TEMPUS project "Business University of the New Age in Serbia (BUONA)", Scuola di Amministrazione Aziendale - SAA (The School of Management of the University of Turin, Italy) and Belgrade Banking Academy (BBA) - Faculty for Banking, Insurance and Finance - have reached an agreement on widening their cooperation beyond the scope of TEMPUS and initiating joint MASTER&MBA study program: Financial / Banking And Business Management. According the Agreement at the end of their studies, students will be granted two diplomas, a Serbian master, and one issued by the University of Turin, which is a strong certification of the quality of the BBA Master & MBA program.

The cooperation involves the following basic features:

- Joint development of program curricula
- Joint development of courses. Under the TEMPUS BUONA project, Serbian professors spend in average two weeks at SAA where, in close cooperation in with Italian professors, they select literature, develop courses contents, and become acquainted with modern teaching methodologies
- Delivery of part of the lecturers by Italian professors
- Mandatory study visits of Serbian students to Turin to attend classes and visit Italian businesses
- Development and introduction of European quality standard system at BBA

The agreement, signed by the rectors of the two universities SAA and BBA belong to, i.e. the University of Turin and the Union University of Belgrade has a far reaching strategic relevance for both BBA and the Serbian education community, considering that according to the latest surveys, and the University of Turin is ranked no. 1 among large Italian Universities.

The implementation of superior standard s in the education process and the enforcement of European quality procedures s will open unique opportunity for Serbian students to obtain MASTER and/or MBA DIPLOMAS by studying at BBA in Belgrade, which will be valid all over Europe.

What is the main goal of the MMB study program?

By carrying out the MMB program, Belgrade Banking Academy in cooperation with prestigious partner from Europe[3] - the SAA of the University of Turin, provides students in Serbia with the opportunity to study in Belgrade according to the highest European standards and achieve both the Master BBA degree an the other one recognized in EU countries, which opens the door for better employment in financial institutions and companies throughout Europe, by equal conditions granted to students from other European countries.

How will the program be performed, how long do the MMB studies last, and which degree is granted?

The courses at the MMB studies are performed by remarkable teachers from the University in Turin (Italy) Seville (Spain), and other European universities, together with top national professors trained at European universities in the frame of Tempus program. The textbook literature is in English and Serbian. The way of taking exams will be completely adjusted to the partners' respecting EU standards. In order to further strengthen equivalence with international standards a seven days professional visit and internship at the University of Turin will take place. The studies last two years (four terms) granting **120 ECTS**. In accordance with Serbian Law on Higher Education and Bologna Declaration, upon the successful completion of the Master studies, the student will be granted academic title **Graduated Manager Master.**

[3] In the year 2008 the University in Turin, comprising the SAA, was entitled the best quality university in Italy.

What knowledge and skills are achieved on the MMB and where the graduate student can find a job?

The students of MMB, thanks to the use of modern teaching methods, will acquire complex knowledge and professional skills in various management disciplines, as well as general management, and will be capable to work in banks and companies covering practically all business activities and, by gaining adequate experience, to achieve top management careers in Serbia, EU countries, and other countries of developed market economy.

Upon completion of the MMB studies, the students will be granted simultaneously the **Master Degree Diploma issued by BBA**, in compliance with accreditation criteria of higher education institutions in Serbia, and **SAA Diploma,** of the School of Management, Turin, accredited in accordance with Italian and European standards, recognized in all European countries. These diplomas provide students with the opportunity to find jobs in banks and other financial institutions and companies in Serbia and EU countries.

Who can enroll in the MMB studies?

BBA graduate students, as well as students who graduated from three and four year undergraduate academic studies coming from the Faculty of Economics, Faculty of Organizational Studies and other faculties in the field of management and business or other similar faculties are eligible to enroll in Master studies – second level academic studies (120 ECTS).

PROGRAM COURSES OUTLINE

Master Course Content (120 Ects)
Financial & Banking And Business Management

	COURSE	Semester	ECTS
1.	International Business and Finance	I	8
2.	EU Law	I	8
3.	Marketing Management	I	7
4.	Management Science	I	8
5.	Management Information Systems	II	7
2 SUBJECTS TO BE ELECTED OUT OF 4			
6. 7.	Risk Management	II	7
	Financial Management	II	7
	Banking Management	II	7
	Human Resource Management	II	7
8.	Strategy Process	II	8
2 SUBJECTS TO BE ELECTED OUT OF 4			
9. 10.	Organizational Behavior	III	8
	Leadership and Soft Skills Development	III	8
	Business Ethics in Finance	III	7
	Mergers & Acquisition	III	7
	SIR for MASTER 1		
	MASTER THESIS I	III	15
2 SUBJECTS TO BE ELECTED OUT OF 4			
11. 12.	Financial Statements Analysis	IV	8
	Operational Management	IV	8
	Portfolio Management	IV	7
	Corporative culture	IV	7
	SIR for MASTER II		
	MASTER THESIS II	IV	15
	MASTER DEGREE - TOTAL		**120**

ADDITIONAL SUBJECTS FOR MBA COURSE DEGREE

13.	Managerial Accounting	V
14.	Advanced Business English	V
2 SUBJECTS TO BE ELECTED OUT OF 4		
15. 16.	Entrepreneurship and Innovation Management	V
	Corporate Governance	V
	Contemporarily Investment Banking	V
	Financial Derivates	V
	MBA THESIS	
	MBA DEGREE - TOTAL	**150**

Subject:

INTERNATIONAL BUSINESS AND FINANCE

Instructors:

- Guiseppe Dutto, Ph.D., Visiting Professor, School of Management – Turin
- Marko Malovi , Ph.D., Assistant Professor, Belgrade Banking Academy, Belgrade
- Du an Kosti , Ph.D., Assistant Professor, Institute of Economics Sciences Belgrade Banking Academy, Belgrade

Topic
International Trade Theory and Policy • Ricardo's HOS Theory • Intra-industry Trade and Monopolistic Competition • Trade Policy in Perfectly-competitive Market • Trade Policy in Presence of Domestic vs. Foreign Monopoly
Balance of Payments, Exchange Rate and International Economic Linkages • BoP Categories • Forms of International Capital Movement
Foreign Exchange Market and Currency Derivatives • Currency Market: Structure, Quotations and Mechanics of Spot Transactions • (Un)Covered Interest Parities and Forms of Arbitrage • Hedging with Currency Derivatives
Country Risk and International Financial Crises • Political and Country Risk Analysis • Factors that Affect the Equilibrium Exchange Rate • Expectations and Central Bank Intervention across Different Exchange Rate Regimes • Emerging Market Currency Crises
Multinationals and Global Business Finance • FDI and the Rise of Multinationals • International Financial Centers, Euromarkets and Off-shore Markets • Eurocurrency and Euro credit Markets • International Bond Market
Financing Foreign Trade • Payment Terms and Documents in International Trade • Financing Techniques in International Trade • Current Asset Management and Short-term Financing • Government Sources of Export Finance and Credit Insurance
International Portfolio Investment (2x45min. Sessions) • International Diversification: Prospects and Limits • The Risks and Benefits of International Investment – Overview of Different Institutional Investors

Course Description and Objectives

International Business and Finance course focuses on executive level decision making in an international context. After passing the exam, students will be well-acquainted with theory and policy of international operations and finance, and capable of taking up a range of strategist/executive posts in global arena of international financial management, international banking and multinational corporations.

Specifically, emphasis has been put on:

- motivation for trade and effects of different trade policies in different market structures,
- organizing and financing foreign trade
- understanding and interpreting balance of payments data and its linkage with exchange rate,
- explaining mechanics of foreign exchange markets, FX risk and hedging techniques with currency derivatives
- ability to rationalize and improve performance of international and transnational economic activity,
- definition and estimation of political and country risk, as well as to avoiding and/or coping with hazards of international financial crises from both macro and micro stand-point,
- inbound as well as outbound FDI theory and practice,
- current asset management in a multinational firm,
- multiple currency management,
- grasping intricacies and superiority of euro markets and off-shore financial centers, and finally,
- prospects and limitations of international financial diversification.

Subject:

EUROPEAN UNION LAW

Instructors:

- Predrag Dedei , Ph.D., Assistant Professor, Belgrade Banking Academy, Belgrade
- Christina Barettini, Ph.D., Visiting Professor, School of Management, Turin

Topic
The Development of European Integration • History of Integration • General Principles of the Unity • The Status of member • The National Programme for Integration with the European Union
The Sources of Law and the Institutions • The Nature of EU • The Nature of EU Law • The Institutions of EU • The Sources of Community Law
European Market Law • Economic and monetary union • Competition: general principles • Competition: practices contrary to Article 81
European Market Law • Competition: abuse of a dominant position and mergers • State aid • Consumer protection
European Company Law • European Company • EGEI • Company law harmonization
Miscellaneous • Tax harmonization • Financial services: Investment firms

Course Description and Objectives

The international legal environment has become an essential factor in the business arena. This course aims at presenting the basic principles of European law. European rules on institutions, internal market, company and financial law, competition and consumer law will be introduced in order to develop the ability of identifying potential legal issues in the business management area. The European Law course will provide the student with an overview of the legal and market environment of the European Union, to the benefit of future managers of a multinational European company.

After completing the course students should be able to:

- understand the European legal and institutional environment,
- analyze and understand the basic rules of the EU,

- work out legal strategies for decision making in European business environment,
- Apply and develop decision making competences as well as analyses and problem solving skills acquired through the discussion of court cases, both at personal level and team level.

Subject:

MARKETING MANAGEMENT

Instructors:

- Hasan Hani , Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
- Ivana Domazet, M.A, Associate Teacher, Institute of Economic Science & Belgrade Banking Academy, Belgrade

Topic
Understanding Marketing Management • Defining Marketing for the 21st Century • Company Orientation Towards the Marketplace • Fundamental Marketing Concepts, Trends and Tasks
Developing Marketing Strategies and Plans • Marketing and Customer Value • Corporate, Division and Business Unit Strategic Planning • The Nature and Contents of a Marketing Plan
Creating Customer Value, Satisfaction and Loyalty • Building Customer Value, Satisfaction and Loyalty • Maximizing Customer Lifetime Value • Customer Relationship Management • Customer Databases and Database Marketing
Identifying Market Segments and Targets • Levels of Market Segmentation • Segmenting Consumer Markets • Bases for Segmenting Business Markets • Market Targeting
Setting Product Strategy • Product Characteristics • Differentiation • Product and Brand Relationships • Packaging, Labeling, Warranties and Guarantees
Developing Pricing Strategies and Programs • Understanding Pricing • Setting the Price • Adapting the Price • Initiating and Responding to Price Changes
Designing and Managing Services • The Nature of Services • Marketing Strategies for Service Firms • Managing Service Quality, Service Brands • Managing Product Support Services
Designing and Managing Integrated Marketing Communications • The Role of Marketing Communications • Developing Effective Communications • Deciding on the Marketing Communications Mix • Managing the Integrated Marketing Communications Process
Managing Mass Communications

• Developing and Managing an Advertising Program • Deciding on Media and Measuring Effectiveness • Sales Promotion • Events and Experiences • Public Relations
Managing Personal Communications • Direct Marketing • Interactive Marketing • Designing the Sales Force • Managing the Sales Force • Principles of Personal Selling

Course Description and Objectives

The course is designed to provide a thorough understand concept of the marketing strategy as essential part of contemporary marketing management and process.

After completing the course students should be able to:

- understand basic foundation of marketing management
- identify sources of competitive advantage, basic element of successful marketing strategy in every company explain “7P’ and “7C” instrument for marketing mix
- identify all communications tools available to company and understand IMC
- Explore different approaches to formulation of marketing strategy using different (direct or mass) techniques of integrated marketing communication evaluate the results of marketing campaign and their strategies.

Subject:

MANAGEMENT SCIENCE

Instructors:

– Neboj a Mari , Ph.D., Full Professor, University BK Belgrade Banking Academy
– Ivana Simeunovi , M.A., Associate Teacher, Belgrade Banking Academy
–

Topic
Management Science (MS) • The origins and development of MS • The methodology of MS and the computer solution
Linear Programming: Model Formulation • Formulation: Profit maximization • Graphical solution of profit maximization • The Simplex method • Formulation: Cost minimization • The dual formulation
Linear Programming: Computer Solution and Sensitivity Analysis • Solving a linear program using the Excel Solver • The transportation problem and Solver • Sensitivity analysis • Changes in the objective function • Changes in constraints
Integer Programming • Modeling with integer variables • Representing Yes-or-No decisions using binary variables • The branch-and-bound method • The cutting-plane algorithm
Nonlinear and Dynamic Programming • Examples of nonlinear programming problems • Lagrange multiplier method • The Kuhn-Tucker conditions • Dynamic programming • The shortest route problem
Project Management • Project networks • Formulating the CPM/PERT network • Critical path scheduling • Cost analysis • The Microsoft Project software
Multi-criteria Decision Making • Goal programming • The Analytical Hierarchy Process • Method ELECTRE • Method PROMETHEE
Game Theory • Games with pure strategies • Games with mixed strategies • Dominated strategies • Solving mixed strategy games using simplex method

Probabilistic Models • Waiting line system • Stochastic matrices • Markov chains • Stationary distribution of Markov chain
Special Topics • Simulation • Decision analysis • Decision trees • Utility theory

Course Description and Objectives

This course introduces several quantitative approaches and computational techniques used by managers to determine solutions to complex business problems.

After completing the course students should be able to:

- determine which techniques are appropriate for solving a particular type of a management decision problem
- successfully analyze the situational dimensions, implement mathematical models on a computer, and interpret the modeling results
- use different software tools to develop linear programming solutions
- demonstrate capability to interpret model solutions and then subject these solutions to sensitivity analysis
- Demonstrate understanding of multi-criteria decision models, including criterion choice, weight assessment, and model scoring understand the critical factors in assessing network modeling problems, including shortest route and maximal flow problems.

Subject:

MANAGEMENT INFORMATION SYSTEMS

Instructors

– Hasan Hani , Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
– Aleksandra Bradi -Martinovi , M.A., Associate Teacher, Belgrade Banking Academy, Belgrade

Topic
Knowledge and Information Technology • Knowledge Explosion and IT
Relation Between Organization and IS • IS and Organizational Changes
IS as a Function of Management • Deciding Process and IS
Information Resources and IS • Identification, Components, Resources and Types of IS
Development of Information Systems • Strategic IS Planning Process • The Purpose and Process of Planning Strategic IS
IS in Environment of Internet Technology • The Characteristics of Business Management in Network Environment
Development of Date Warehouse - DW • Dimensional Data Modeling • Construction of Data Warehouse, Architecture, Construction &Using of DW
E-Business • Transition Between Traditional and E-Business • Development Strategy of E-Business • Resources for E-Business (Outsourcing in E-Business)
ERP and CRM Systems • Enterprise resource planning (ERP) • Customer Relationship Management (CRM)
Business Intelligence • The Basics of Business Intelligence; -The Characteristics of Data Quality • Development of Business Intelligence Concept • Business Intelligence in Banking and Insurance
From Data to Knowledge • OLAP Tools • Data Mining • Expert Systems
Management Support Systems • The Types of Decisions • Decision Support Systems (DSS)

• Architecture for DSS ***Basel II and Information Support***
Value Creation and Strategic Information Systems • The Analysis of Added Value • Strategic IS and Values Creation
Value Creation With IS • Traditional Models of Value Creation with IT • Value Chain of Customer Service Life Cycle & Emerging Frameworks
Appropriating IT-Enabled Value Over Time • Sustainability Framework • Making Decisions
Protection Information Management • Basics and Elements of Information Protection • Development of Systems for Protection • Protection of Data in Internet Environment ***Privacy and Ethics in IT***

Course Description and Objectives

The course is designed to provide a thorough understanding concept of business strategy as essential part of contemporary strategic management process.

After completing the course students should be able to:

- understand theoretical foundation of the strategy process within the complex business and corporate environment
- use different techniques in strategic analysis and strategy formation
- identify the sources of competitive advantage, and element of successful strategy in every organizations
- explore the different approaches to strategy formulation on different levels – corporate, business, functional and international
- identify all aspects of strategy implementation including its controlling and evaluating.

Subject:

FINANCIAL RISK MANAGEMENT

Instructors:

– Peri a Ivanovi , Ph.D., Associate Professor, Belgrade Banking Academy
– Jelena Minovi , M.A., Associate Teacher, Belgrade Banking Academy, Belgrade

Topic
Banking Risks • Risk vs. return for investors and companies • Banking risks • Bank capital • Bank profitability
Bank regulation and Basel II • Reasons for regulating bank capital • Positive banking regulation • Basel II • Asset-Liability Management • ALM Overview
Credit Risk • Credit Risk • Credit risk instruments • Estimating credit losses • Methodology of evaluation and management of credit risk. • Aspects and emanations of Credit Risk in global banking
Correlations and Copulas • Definition of volatility • Estimating volatility from historical data • Definition of correlation • Copulas
The VaR measure • Properties of risk measures • Definition of VaR • Choice of parameters of VaR • Marginal VaR, incremental VaR, and component VaR • Credit VaR
Meteorology, Energy and Insurance Derivatives • Meteorology Derivatives Risk • Energy Derivatives Risk • Insurance Derivatives Risk
Market risk VaR • Historical simulation approach • Model-building approach • Monte Carlo simulation • Calculating Greek letters • Greek letters and risk management with trading desk
Credit Derivatives Risk • Credit Derivatives: Definitions

• Credit Derivatives Risk • Applications of Credit Derivatives
Operational Risk • What is operational risk? • Determination of regulatory capital • Categorization of operational risks • Allocation of operational risk capital

Course Description and Objectives

This is introduction course to financial risks and procedures, which include identification, evaluation, management and control of financial risks. The main focus is on latest quantitative methods applied to measure and control financial and other risks. Other covered risk types are market risk - foreign exchange risk, interest rate risk and price/position risk (Value at Risk, market volatility, expected loses, stress situations test, scenario analysis), credit risk (at debtor level, at transaction level, portfolio level, rating models, market models, credit derivatives), liquidity risk, operational risk and requests for capital related to mentioned risks (management of economic and regulation capital – Capital at Risk).

Subject:

FINANCIAL MANAGEMENT

Instructors:

- Guiseppe Dutto, Ph.D., Visiting Professor, School of Management – Turin
- Svetislav Paunovi , Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
- oran Grubi i , Ph.D., Associate Professor, Belgrade Banking Academy, Belgrade

Topic
Introduction • Financial management in turbulent business environment • Business organization, financial markets and tax environment
Valuation of long-term investments • Time value of money • Risk and Required rates of return concept • Bonds and stock (preferred and common) valuation
Capital budgeting • Capital budgeting - non discounted cash flow and discounted cash flow criteria • Advanced topics in capital budgeting (project ranking, size disparity, time disparity, unequal lives)
Cost of capital • Cost of debt, cost of preferred stock and cost of common stock • Factors determining the weighted cost of capital • Level of financing and the weighted cost of capital
Financial structure and dividend policy • Operating leverage, financial leverage and combination of operating and financial leverage • Capital structure vs. financial structure • Basic tools of capital structure management
Dividend policy and internal financing • Does dividend policy affect stock price? (Dividend policy is irrelevant; High dividends increase stock value; Low dividends increase stock value) • The residual dividend theory
Financial forecasting, planning and budgeting • Sales forecasting (“Percent of sale” method of financial forecasting) • Cash budget • Pro forma Financial Statement
Working capital management • Risk-return tradeoff from investing in current assets and risk – return tradeoff from using current liabilities • Appropriate level of working capital -Hedging principle • Cash vs. marketable securities management (when cash balance is certain; when cash balances fluctuate randomly)
Working capital management • Account receivable management • The use of “Marginal analysis” in Account receivable management • Inventory management
Short-term financing

• Unsecured sources • Secured sources (account receivable loans, inventory loans) • Estimation of the cost of short-term financing
Long-term financing • Long-term loans • Repayment schedule • The lease vs. purchase decision • Mix of corporate securities sold in the capital market • Determining of the cost of long-term financing • Convertible securities and warrants

Course Description and Objectives

The course is designed to enhance the understanding of financial theories, methodology and the best practices in order to manage corporate financial resources effectively. Students will address the most important financial management issues faced by decision-makers and will improve analytical skills in order to deal with various financial topics. Topics covered include: concept of the time value of money; risk and required rates of return concept; valuation of the long-term investments; capital budgeting; cost of capital; operating and financial leverage; dividend policy; financial forecasting, planning and budgeting; working capital management; short-term financing; long-term financing.

After completing the course, students should be able to:

- Understand the proper role of financial management;
- Describe financial management in terms of the three major decision areas that confront the financial manager;
- Understand major financial management concepts and apply different techniques;
- Understand the financial consequences of the major corporate decisions involving the investment decision and working capital management;
- Understand the impact of financial management decision on the sustainability of company's growth.

Subject:

BANKING MANAGEMENT

Instructors:

- Branko ivanovi , Ph.D., Associate Professor, Belgrade Banking Academy
- Gradimir Ko etinac, Ph.D., Associate Professor, Belgrade Banking Academy
- Milena Kova evi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Introduction   Latest trends and diversification of activities in modern commercial banking
Management of modern organizational forms and structures in corporate and retail banking
Commercial bank adaptability management in relation to current CB's monetary policy
Commercial bank liability management and current liability pricing models (basics of ALM management)
Interest rates and FX rates transformation management in commercial banking
Management of credit approval procedure in modern commercial banking
Commercial banking risk management
Modern strategies of capital adequacy formation policy in commercial banking management
Innovative business and cross-selling models in modern commercial banking management (private banking, insurance, leasing, factoring…)
Mergers and acquisitions - banking systems reconstruction in transitional economies

Course Description and Objectives

This course is designed to provide a thorough understanding of key banking categories, modern organizational structures and business trends in commercial banking nowadays. The course should develop student's abilities to identify market opportunities and react timely to them with in advance conceived alternative tactics in terms of achievement of potential profitability and influence to the bank value.

After completing the course students should be able to:

- understand theoretical foundation of banking management within the complex and turbulent financial market,
- to acquire quickly, analyze and make decisions related to mobilization and investment of banking resources with clear and predictable results by using different strategies and techniques of modern commercial bank management,
- work with financial and non financial reports in order to assess client's credit worthiness,
- understand complex relations in different segment of financial market and create an optimal commercial bank portfolio,
- Recognize possibilities of modern cross selling of banking products (factoring, leasing, insurance, private banking...).

Subject:

HUMAN RESOURCES MANAGEMENT

Instructors:

– Gianpiero Bigando, Ph.D., Visiting Professor, School of Management – Turin
– ivka Pr ulj, Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
– Marija Lazarevi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Managing human resources: development and challenges • Characteristics of the modern approach to management of human resources • Environmental, Organizational and Individual Challenges • Strategic Human Resource Management
Managing Work Flows and Conducting Job Analysis • Strategy and Organizational structure • Design the Organization • Work/Flow Analysis • Job Analysis and Job Description
Staffing • Strategic Aspects of Staffing • Recruitment • Selection • Organizational Exit and Retention of Staff
Performance Appraisal and Managing Performance • Identifying Performance Dimensions • Measuring Performance • Managing Performance
Training and Development • Strategic Aspects of Development • Managing the Training Process • Developing Careers
Managing Compensation • Strategic Aspects of Compensations • Design Compensation Systems • Compensation Plans • Design Benefits
Labor Relations and Employee Relations • Legal Framework of Labor Relations • Relations with Unions and Collective Bargaining • Managing Discipline • Conflict in the Workplace • Negotiations
Managing Workplace Safety and Health • Workplace Safety and the Law • Risks to the health and safety at work: the physical risks, stress, alcohol, smoking, drugs

• Safety and health Programs
International HRM Challenge • Forms of international engagement of employees • International Polices and Practice of Human Resource Management
Partnership Managers and HR department • Responsibility for human resources • Role Managers and HR Professionals • Professionalism and Specialization

Course Description and Objectives

The course is designed to provide a thorough understand of all aspects of human resources management as an integral part of management activities in modern companies.

After completing the course students should be able to:

- understand theoretical foundation of human resources management
- use different instruments and techniques human resources management,
- be able to identify the basic problems of human resources management and their causes,
- be able to make structures, procedures and systems of human resources in companies.

Subject:

STRATEGY PROCESS

Instructors:

- Enrico Guzzeti, Ph.D., Visiting Professor, School of Management, Turin
- Zvonko Brnjas, Ph.D., Associate Professor, Belgrade Banking Academy
- Dejan Eri , Ph.D., Full Professor, Belgrade Banking Academy Institute of Economic Science, Belgrade
- vonko Popovi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Strategy • Strategy • Identifying the strategy issues • Structuring the strategy debates • Developing an international perspective
***Strategy Process:* Strategic thinking** • The issue of strategic reasoning • The paradox of logic and creativity • Perspective on strategic thinking
Strategy Process: Strategy Formation • The issue of realized strategy • The paradox of deliberateness and emergence • Perspective on strategy formation
Strategy Process: Strategy Change • The issue of strategic renewal • The paradox of revolution and evaluation • Perspective on strategic change
Business Level Strategy • The issue of competitive advantage • The paradox of markets and resources • Perspectives on business level strategy
Corporate and Network Level Strategy • The issue of corporate configuration • The paradox of responsiveness and synergy • The issue of inter-organizational relationship • Perspectives on corporate and network level strategy
The Industry Contexts • The issue of industry development • The paradox of compliance and choice • Perspectives on industry context
The Organizational Context • The issue of organizational development • The paradox of control and chaos • Perspectives on the organizational context
The International Context • The issue of international context • The paradox of globalization and localization • The perspectives on the international context

Organizational Purpose
- The issue of corporate mission
- The paradox of profitability and responsibility
- The perspective on organizational purpose

Course Description and Objectives

The course is designed to provide a thorough understanding concept of business strategy as essential part of contemporary strategic management process.

After completing the course students should be able to:
- understand theoretical foundation of the strategy process within the complex business and corporate environment
- use different techniques in strategic analysis and strategy formation
- identify the sources of competitive advantage, and element of successful strategy in every organizations
- Explore the different approaches to strategy formulation on different levels – corporate, business, functional and international identify all aspects of strategy implementation including its controlling and evaluating.

Subject:

ORGANIZATIONAL BEHAVIOR

Instructors:

– ivka Pr ulj, Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
– Marija Lazarevi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Characteristics and development of scientific disciplines • Definition scientific disciplines • Development of organizational behavior • Principles and Objectives • Levels of study
Individual level • Personality, personal traits, skills, emotional intelligence • Perception and attribution • Attitudes and values • Learning
Individual level • Motivation • Job satisfaction • Stress • Fluctuation and absenteeism • Individual decision making
Group lavel • Groups and teams • Groups decision making • Power, influence and politics • Communication • Intraindividual Conflict • Leadership
Organizational lavel • Organizational structure and design • Role in the organization • Organizational Culture as a variable in organization behavior • Organizational change and behavior

Course Description and Objectives

The course is designed to provide a thorough understand of all aspects of human resources management as an integral part of management activities in modern companies.

After completing the course students should be able to:
– understand theoretical foundation of organizations behavior
– use different instruments and techniques human resources management,
– be able to identify the basic problems of people behavior in organizations and to find a solution for them,
– be able to control and adapt to organizational behavior factors in order to achieve greater business efficiency and satisfaction of employees.

Subject:

LEADERSHIP AND SOFT SKILLS DEVELOPMENT

Instructors:

– Svetislav Paunovi , Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
– Dragan Milinkovi -Fimon, Ph.D., Associate Professor, Belgrade Banking Academy
– vonko Popovi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Leadership Defined, Leadership Described • What is leadership? • What makes a leader? • Is leader always admirable? Why? • Examples: past, present, future
Historical aspects of leadership • Confucian Asia leadership profile • Latin America leadership profile • Anglo leadership profile • Sub-Saharan Africa leadership profile • Eastern Europe leadership profile
Psychodynamic Approach • Description, Background • Types of leadership
Communications styles • International examples, styles of leadership • Thinkers, doers, hybrids
Culture and leadership • Culture defined, related concepts • Culture with different communications context • Clasters of World culture
Bilding oneself • One’s own leadership styles • „Tool bucket“
Development of tools and skills • Daily tool bucket review • Organizational charts • Hierarchy
B d ’ • Lead • Follow • Or get out of the way
Leadership mantras • Dealing with Adversity and Disappointment • Dealing with Challenges and Failure • Risk management • Time management

What is your mission?

- Developing you, your team, your people
- Passion, Vision, Enthusiasm
- Conviction, Action, Results.

Course Description and Objectives

The main goal of this course is to help candidates develop their personal leadership potential by identifying leadership preferences, strength blind spots, and strategies which can be used to start their transformation into the best leader they can possibly be. The course includes several quick reviews of classic and modern dimensions of leadership as the basis for exploring each individual's leadership potential and style. The pace of the class will be fast but with reasonable amount of time to make sure all candidates understand the issues discussed. Rather than diving deep into historical management and leadership issues, most of class time will be allocated to "living" the present issues in simulated leadership exercises, and developing strategies to deal with current events and future challenges for those candidates who choose leadership positions in their personal life or in business situations. Candidates will be invited to immerse themselves in a series of reality situations (every-day life), to face challenging situations, and to provide answers which can be clearly communicated, and hopefully accepted by all members of the class, by great majority, or in some cases, by no one. Copying someone else's leadership style will be discouraged during this course. After completing the course candidates should be able to continue their own personal development as future leaders, with a very personal brand of leadership in a way that will feel inherently natural and comfortable to each one of the participants.

Subject:

BUSINESS ETHIC IN FINANCE

Instructors:

– ivka Pr ulj, Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
– Marija Lazarevi , M.A., Associate Teacher, Belgrade Banking Academy, Belgrade

Topic
Concept and definition of ethics and morals • Ethics areas and degrees of generality – general and applied ethics • Nature of ethics argumentation: utilitaristic and deontological approaches to ethics
Ethic and business • Reasons for introducing ethics in business; • Levels of business ethics analysis • The myth of amoral business; ethics versus laws; stakeholder theories and theory of enlightened self-interest • Concept of corporate social responsibility and its relation to the concept of business ethics • Ethical foundations, norms and aims of professional codes
Ethics in the financial business • The nature of morality and ethics in the financial services • The basic ethical issues in the financial business
Ethics in Accounting and Auditing • The basic ethical issues in accounting • Ethical principles in audit and audit conflict
Ethical banking • Basic ethical principles in the banking business • Trends in European, American, Japanese and Islamic banking from the angle of ethics • Ethics and alternative banking • Banks and world debt
Ethic and many • Corruption and cultural diversity • International business and ethic

Ethical Issues in Investment Decisions • Socially Responsible Investing • Investment and the New Finance • Ethical dimension takeover and restructuring corporations
Professional Standards and Practice • CFA Institute Code of Ethics and Standards of Professional Conduct • Professionalism • Integrity of Capital Markets • Duties to Clients

Professional Standards and Practice
- Duties to Employers
- Investment Analysis, Recommendations, and Actions
- Conflict of Interest
- Responsibilities as a CFA Institute member or CFA Candidate

Course Description and Objectives

The course is designed to provide a thorough understand all aspects of organizations as social systems.

After completing the course students should be able to:
- understand and apply fundamental knowledge in the field of business ethics in the financial sector,
- develop a sensitivity to professional and ethical responsibility,
- explain, represent and defend the principles and ways of dealing with sensitive ethical issues at the operational and tactical level in the financial sector.

Subject:

MERGERS AND ACQUISITIONS

Instructors:

– Dejan Eri , Ph.D., Full Professor, Belgrade Banking Academy Institute of Economic Sciences, Belgrade
– Jelena Minovi , M.A., Associate Teacher, Belgrade Banking Academy, Belgrade

Topic
M d ’ r d M d B • M&A Terms comprehension • M&A Process
M d ’ r d M d B • M&A through history • M&A waves • Legislative and institutional framework of M&A
Firm theory and corporative activities • Different approaches of theory of the firm • Corporative activities comprehension
M&A strategic aspect • M&A as strategic alternatives • M&A types and categories • Theories of M&A
M&A strategic aspects • M&A management aspects • M&A organizational aspects • M&A as decision-making process • Customer strategy analyses, vendors strategy analyses
Case study analyses • M&A strategic and management aspects- customer’s position • M&A strategic and management aspects-vendor’s position
M&A process • Possible analytical accesses to M&A • Due diligence as a step of M&A process • Due diligence reports – elaboration accesses
M&A processes • Negotiation management • Transaction realization • Post-integration problems • Takeover strategies • Takeover defenses
M&A financial aspects • Investment bankers role in M&A activities • Alternative financing sources • Financial analysis for M&A necessities
M&A financial aspects • Financial analysis for M&A necessities - continuation • M&A accounting aspects • Fiscal aspects

Course Description and Objectives

The course is aimed to fifth year students who already have overwhelmed many scientific disciplines in order to get acquainted with complex problems of emerging new business combinations through mergers (fusions, affiliations, mergers, etc) and acquisitions (buying off, taking over, etc.).

Besides other, the main course objectives are as follows:

- To capacitate the students for understanding the nature of strategic decisions on external growth methods, as a way to realize general objectives growth and business organizations development together with development strategies components on different levels,
- Capacitating for understanding decision-making process on mergers and acquisitions (M&A),
- Comprehension of M&A decision implications on organizational structure, culture and development of organization involved in the processes,
- Get acquainted with basic knowledge and skills on merging strategy's methods and techniques,
- Comprehension of basic elements together with due diligence process implementation,
- Comprehension and analysis of financial analysis methods and techniques for involved organizations,
- Comprehension and analysis of alternative financial transaction sources,
- Comprehension and analysis of financial transactions legislative aspects,
- Develop abilities for post-integrative processes comprehension and management.

Subject:

ANALYSIS OF FINANCIAL REPORT

Instructors:

- Gordana Vukeli , Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
- oran erkovi , Ph.D., Full Professor, Belgrade Banking Academy, Belgrade

Topic
Theory of analysis • Concept analysis • the purpose of analysis - analysis of the business and scientific purposes • Goals and objectives analysis • Methods of analysis
Types of analysis • The instruments of analysis – relations of the size of statistical and mathematical methods • Types of analysis
Profit and loss account analysis • Form, content and methods of developing profit and loss account • The total cost • The effects of the sale • The relationship between the financial results and billing costs system • The relationship between financial results and billing of income system
Yield Analysis • Form and contents of profit and loss account scheme • Analysis of financial results • Analysis of the structure of the financial results and risk analysis of the financial results and the lower point of profitability • Analysis of financial power • Analysis of cost effectiveness
Analysis of possibilities of getting out of the loss zone • Analysis of the negative impact on financial results • Analysis of possibilities to achieve a neutral financial
Analysis of balance sheet • Classification and order of financial positions • Form and contents of balance sheet scheme • Disposable capital, deferred tax assets and deferred tax liability • Analysis of property position • Analysis of the structure of business property • Analysis of fixed assets
Analysis of working capital • Definition and forms of working capital • Analysis of the structure of working capital. • Analysis of trade of working capital • Analysis of changes in speed of working capital trade
Analysis of capital and property • Analysis of invested capital • Analysis of the efficiency of assets
Analysis of financial position

• The concept and analysis of financial balance • Analysis of short-term and long-term financial balance • Analysis of indebtedness • Analysis of solvency • Analysis of maintenance of the real value of capital • Analysis of reproduction ability
Analysis of opportunities for improvement of financial position • Analysis of overt and covert losses • Analysis of opportunities for improvement of financial balance by re-structuring assets and sources of funding • Analysis of possibilities of securing insufficient capital

Course Description and Objectives

The course is designed to enable the students to understand all aspects of financial report analysis in terms of reporting in the company.
Upon completion of the course students will be able to:

- Understand the theoretical basis of analysis of financial statements, use their presentation in the complex business environment,
- Use methods of analysis of financial statements,
- Master methodology of analyzing income, property and financial position of enterprises,
- Master approach, procedures and methods of financial report analysis in the analysis of income position in terms of getting out of the loss zone,
- Master approach, procedures and methods of analysis of property and financial position regarding improvement of financial position,
- Identify segments of the analysis of financial statements, according to the order and purpose of analysis in the company.

Subject:

OPERATIONS MANAGEMENT

Instructors:

- Besim ulahovi , Ph.D., Visiting Professor, Faculty of Economics University of Sarajevo, Bosnia and Herzegovina
- Zvonko Brnjas, Ph.D., Associate Professor, Belgrade Banking Academy
- vonko Popovi , M.A., Associate Teacher, Belgrade Banking Academy
-

Topic
Introduction into operations management: competitiveness, strategy and productivity & production system designing
Analysis and planning of location & Transportation model
Technology process selections and layout strategy
Management of new products development
Quality management
Human resources and creation of new working posts
Value chain management & Forecasting of demand and procurement management
Stocks management and stocks costs & Material balance planning
Capacity management in the uncertain environment
Agregate and operations planning & Project management
Capacity management in the uncertain environment

Course Description and Objectives

The course is designed to provide a thorough understanding of complex operations within contemporary companies.

After completing the course students should be able to:

- understand the way in which company can improve its productivity and efficiency in the process of resource utilizations; this will include general as well as a view which will focus on specific business function
- become capable to analyze specific problems within domain of operational activities in the companies
- be capable to use adopted knewladge through individual as well as team work in the process of business decision making in the real life situation.
- Obtain practical knowledge and skills to manage operations of companies so that it will enhance its overall efficiency and to improve its performances.

Subject:

Portfolio Management

Instructors:

- Sa a Popovi , Ph.D., Visiting Professor, Faculty of Economics, University of Podgorica
- Mali a Djuki , Ph.D., Assistant Professor, Belgrade Banking Academy, Belgrade
- Du ko Kne evi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Introduction • Financial Securities • Financial Markets
Portfolio analysis: Portfolio Theory • The Characteristics of the Opportunity Set Under Risk • Delineating Efficient Portfolios • Calculating the Efficient Frontier
Portfolio Analysis: Portfolio Selection Process • The Single-Index Model • Multi-Index Models • Grouping Techniques
Portfolio Analysis: Selecting the Optimum Portfolio • Utility Analysis • Other Portfolio Selection Models
Models of Equilibrium in the Capital Markets • The Standard Capital Asset Pricing Model • Nonstandard Forms of Capital Asset Pricing Models • Empirical Tests of Equilibrium Models • The Arbitrage Pricing Model
Security Analysis and Portfolio Theory • Efficient Markets • The Valuation Process • Earnings Estimation • Interest Rate Theory and the Pricing of Bonds
Management of Bond and Stock Portfolios • Duration • Protecting against term structure shifts • Management of yearly returns • Swaps
Management of Bond and Stock Portfolios • Active management • Passive versus active • International diversification
Management of Bond and Stock Portfolios • Absolute return strategy vs. relative return strategy • Total return strategy • Product range: investment funds, hedge funds, SICAV, ETF, discretionary mandate

Evaluation of Portfolio Performance

- Evaluation techniques
- Decomposition of overall evaluation
- Multi-index, APT and performance evaluation
- Mutual fund performance

Course Description and Objectives

Portfolio management course covers modern investment and portfolio theory for investment selection and management. Modern theory includes the examination of asset pricing models and efficient market hypotheses. Portfolio management strategies for both equity and bonds are explained throughout the course. For tracking the portfolio performance, a variety of measurements are presented.

After completing this course, students will be able to explain and apply concepts of investing in securities and portfolio management. They will be able to analyze and interpret financial data and demonstrate knowledge of portfolio management strategies.

Subject:

CORPORATE CULTURE

Instructors:

– ivka Pr ulj, Ph.D., Full Professor, Belgrade Banking Academy, Belgrade
– Marija Lazarevi , M.A., Associate Teacher, Belgrade Banking Academy

Topic
Corporate culture as a new organizational paradigm • Changing the focus of management theory • Organizations as social systems • Development of the concept corporate culture
Elements of corporate culture • Cognitive elements • Behavior elements • Material elements
Culture, strategy and structure organizations • Culture and strategy • Culture and structure
The relationship of culture to the image, identity and business ethics • Differences in content and terms • Cultural influence on the image, identity and ethics
Communication and Culture • Language as a characteristic identity • Culture with different communications context
Types of corporate culture • Different approaches typology • Typology of Charls Handy
Culture and organizational performance • Determinants of success • Forces of culture and performance
Culture, power and leadership • Power in organization • Leader as creator and promoter of culture • Pathology culture
Organizational versus national culture • Comparative cultural research • Characteristics of particular culture - cultural map • The influence of culture on business environment
Organizational change and culture • Culture as a determinant of change • Change of culture

Course Description and Objectives

The course is designed to provide a thorough understand all aspects of organizations as social systems.

After completing the course students should be able to:

- understand importance of corporate culture for organizations performance,
- be able to identity corporate culture
- be able to identity limitation corporate culture and need to change, be able to identify some factors influence the behavior of employees and sources of organizational power.


SAA
UNIVERSITÀ DEGLI STUDI DI TORINO
UNIVERSITY OF TURIN
Value for people value for organization
Sharing
Freedom and ethics
Helping
Listening
Knowledge sharing


SAA
UNIVERSITÀ DEGLI STUDI DI TORINO
UNIVERSITY OF TURIN
University and Company Cycling relation
Employability
Execution
people
Accountability

Part III.

SCIENTIFIC PAPERS

DEVELOPMENT OF INFORMATION SYSTEMS IN ZASTAVA AND THE FUTURE WITH FIAT

Aleksandra Bradić□Martinović[4], *Marija Džopalić*[5]

Abstract

□ecessitate for information technology in business is undeniable. The company "Zastava" from Kragujevac realized this fact at the very beginning of its development and has improved business in the direction of continuous progress in the field of information technology. Following the progress of IT sector, "Zastava", we can practically follow the development of information technology.

The IT development in "Zastava" has started in early 1960 by establishing the Office for the organization and systematization. The first IT organizational unit in the factory "Zastava" was Electromechanical de□ partment. The first computer for automatic data processing ever installed in an industrial company in □u□ goslavia, was in that department. End of sixties and the seventies were characterized by remote and auto□ matic data processing, while the eighties introduced distributed data processing. □ineties followed the idea of information system based on the principles of integrity and data distribution. Today IS in "Zastava" relays on the integral PC and network technology.

This segment of company, unfortunately, has suffered great damage during the bombing in 1999, but then it continued development and now are based on a modern technological solutions.

The Memorandum of strategic cooperation between FIAT and "Zastava" has been signed on May 2008. According to estimates of leaders in the Zastava's IT sector, the main direction of development will contin□ ue, and they expect further investment in the IT. They also expect that FIAT will probably apply the model they already used in the similar arrangements □a separation of IT department and forming a new company whose services will be used by the factory (outsourcing model).

Key words: *Zastava, FIAT, information systems, information technologies, computers, network*

Introduction

When we speak about information systems, we confuse that term with information systems support by information technology. It is common, since "it is hard these days to escape the hype and publicity surrounding information technology (IT) and its business applications. For business, IT has become a critical resource, and for many organizations it represents the 50 percent of capital spending. Information is a critical organizational resource" , p. 5 . But in early sixties was not like that. Information technology was at first stages of development, the machines were very large, very expensive and there were not enough educated staff to cover that field of business. Also, "the use of computers and information technology has brought many changes in organizations. Changes are felt in areas such as the structure, authority, power and content of jobs, progress in the career of employees, supervision and business managers" 2, p. 70 .

Today, the importance of development of information systems (IS) is widely accepted by both researchers and practitioners, but Zastava realized that fact in early sixties and start their long process of IS development.

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1. The phases of information system development in Zastava[6] - Kragujevac

The **first phase** of development of information system in Zastava can be called ***electromechanically data processing***. It began in 1960 when the company **concluded a contract with IBM** on the delivery of electromechanical set of machines for electronic processing of data. It was computers from II generation: IBM609, tabulator (WTC Computing Accounting Machine) IBM421, End Printing Reproducing Punch – IBM 519, Electric Punched Card Collator – IBM077, Card Sorter – IBM082 and the machines for punching and verifying cards. At that time, main memory medium for keeping and transmitting information was punch card. As a parallel process, Zastava need to educate working stuff, so they can use the acquired equipment and to provide the space with air conditioning and other adequate conditions for work.

Realization of the contract began in 1961 when IBM delivered first machines for data processing. Zastava got machines for material management and salaries, and then for processing tools, working orders, working units, registration number of workers[7], etc.

IBM 609 machine

They worked with those machines few years, but they were very slow and with low capacity, so existing needs in Zastava were exceeded their ability. As a result of that, during 1966 Zastava started preparations for introducing new machines from the III generation – electronic data processing (computers). After that, we can talk about **second phase** of development – ***automated data processing***.

In 1968 Zastava bought computer IBM 360/30 with 16Kb RAM and appropriate peripherals (4 hard disks, 1 printer, 2 control units, 1 reader and punch card machine). The configuration was very powerful at the time and provided integration of business data, which was very important for future development of information system. That computer was the first ever installed in a company in Yugoslavia. Zastava was a pioneer in that area as well. Acquisition of this computer changed an organization of IT sector and they started to develop new features, such as application and system programming. There were significant changes in data preparing, system analyzing and the way of IT organization. The biggest changes are, however, made in the way of using equipment.

Few years later Zastava indicated the need for expansion of equipment, so they obtain 2 units of magnetic tapes and with additional 16Kb of RAM, so they had 32Kb. The configuration enabled construction of first technological data bank in with BOMP[8] database management system. The system could produce over a 200 user's information.

Zastava has a very intensive development in those years, especially in the car industry, so the computer system they had was unable to satisfy the needs. In 1972 they decided to get new computer configuration with remote data processing.

Since 1973 we can recognize the **third phase** in information system development in Zastava – ***remote data processing***. In 1974 they obtained the IBM 370/145[9] computer with 212Kb RAM memory, updated existing IBM 360

IBM System with its associated equipment

[6] The full name of the firm, from 1946 was Crvena Zastava – Kragujevac and from 1990 just Zastava

[7] It required creation of first numerical code system for each segment of business.

[8] The BOMP (Bill of Materials Processor) was a specific-purpose system based on a network that had a much lower expressive power than Bachman's: 2-level network (may be characterized as a free network to which we add the following restriction: "children" are not "parents").

[9] The IBM System/370 (often: S/370) was a model range of IBM mainframes announced on June 30, 1970 as the successors to the System/360 family. The series maintained backward compatibility with the S/360, allowing an easy migration path for customers; this, plus improved performance, were the dominant themes of the product announcement.

to 64Kb and rented complete set of peripherals (4 hard disks, 1 printer, 2 control units, 1 reader and punch card machine). Equipment also included process computer IBM S/7 [10] with 33 terminals (IBM 2790) for remote data processing.

In the same year Zastava completed the construction of new building and they are using it for IT sector nowadays.

New building for IT sector in Zastava

Remote data processing enabled design of first online information for management process of car construction. The total amount of batch information for end users was approximately 800.

Growing number of information increased the need for more comprehensive and global automated data processing, especially in the area of planning and monitoring of production and commerce. Because of that, in 1978 Zastava rented and installed new computer - IBM 370/148, with 1Mb RAM memory, 4 HDD devices, 3 units for magnetic tape and 4 mini computers – series S/1 with 24 terminals for interactive work. Finally, the old computer, IBM 360/30, was finally excluded from the use, after ten years of proper work.

New computer configuration allowed installing DOS/VSE operation system, hierarchical organization of data – DL/1 and development of on line applications.[11] Since then we can talk about **fourth phase** of information system development – ***interactive data processing***.

On the basis of the above, we can conclude that Zastava, as a manufacturing and business system, changed and renovated its computer equipment every four of five year, according to trends of IT development in the world and conform it to its need. The same situation repeated in 1984, when they switched rented computers with new generation – IBM 4341/L11, with 4Mb RAM memory, 12 hard disk units (each of them had memory space of 9GB), 4 units for magnetic tape (each of them had memory space of 320Mb) and 102 terminals 3270 for on line monitoring of work process. These computers had VM/SP and DOS/VSE operation system, DL/1 and VSAM[12] data management system and VTAM communication system, with software for computer graphic design – CADAM[13]. At that time, the old computer was traditionally turned down after 10 years of use.

Previous phases of IT development in Zastava can be marked as centralized period. Whole manufacturing and business system was at one location. At 1984 Zastava accepted medium term development strategy of IT sector, which was characterized as ***distributed data processing on polycentric bases*** – **fifth phase** of information system development.

Zastava created new autonomous computers centers:

a. Center for distributed data processing for management of car spare parts (1984), with computer DELTA 4850-VAX[14];

[10] The first customer delivery of an IBM System/7 was made on September 16, 1971, to American Motors Corporation (AMC) at Kenosha, Wisc. Zastava bought it in 1974. There is no need to mention that the price of this computer was extremely high comparing with today prices. Purchase price was about $64.000.

[11] DOS/VS offered five partitions (later 7) and a relocating loader for effective multiprogramming. Database/Data Communication (DBDC) became a fundamental part of VSE as the use of CICS grew. A hierarchical database known as DL/1 was available as well. At this time, DOS/VS became something we would clearly recognize today as a VSE system. (**Source:** *http://www-03.ibm.com/servers/eserver/zseries/zvse/about/history1970s.html*)

[12] Virtual Storage Access Method (VSAM) is one of the access methods used to process data.

[13] CADAM (Computer Augmented Design And Manufacturing) is a CAD related product that was developed by Lockheed. CADAM is/was software originally written for IBM mainframes and later ported to UNIX workstations. A variant of CADAM called MicroCADAM was also developed, which also ran on PCs under DOS. /(Source: http://mbinfo.mbdesign.net/CAD-History.htm)

[14] This computer started to work at 1987.

b. In period from 1986 to 1987 few DELTA-400 computers had been installed in Belgrade, Sombor, Zagreb, Kragujevac and Sarajevo;
c. Center for distributed data processing had been created in 1986 for weapon factory, with IBM 4381/12M computer, terminal network, graphic points and plotters, so engineering and graphic calculations could be realized there;
d. During the astava, also created center for distributed data processing in Fabrika "Ramiz Sadiku" in Pec, as a first self-supporting center with IBM 4361/5 computer and a network with 23 terminals. From the main IT center in Kragujevac, they transmited applications for accounting, fixed assets, tools business and the main product and stuff databases;
e. During the 1987/88 the main building had been reconstructed and the second floor was added;
f. The second self-supporting and independent center was creating during 1988/89 in the HTD factory in Ohrid. They had an IBM 9375/60 computer and network with 41 terminals.

At the same period, in the field of engineering graphic, Zastava provided license rights from IBM for "DEMO presentations for using program packages CADAM and CATIA" and the rights for instructing a new users in the field of projecting and constructing.

Table 1. Development of IT in Zastava from 1960 until today

Phase	Type of data processing	Processor and memory	Operation system	Data organization	Progr. language	Comm. sys.	CAD/ CAM
First 1960-	Electro-machanicaly			Punched cards			
Second 1968-	Automated	IBM 360/30 (16, 32, 64 KB)	BOS DOS	Sequential, index and BOMP	ASSEMBLER PL/I RPG		
Third 1974 -	Remote	IBM 370/145 (208 KB)	DOS DOS/VS	BOMP	ASSEMBLER PL/I, RPG, FORTRAN	BTAM	
Forth 1978 -	Interactive	IBM 370/149 (1 MB)	DOS/VS DOS/VSE CICS/VS	BOMP DL/I VSAM	ASSEMBLER PL/I, RPG, FORTRAN, COBOL	BTAM	
Fifth 1984-	Distributed	IBM 4341 (8 MB)	VSE/SP VM/SP CICS/VS	DL/I VSAM	ASSEMBLER PL/I, FORTRAN, COBOL	VTAM	CADAM
Sixth 1989-	Integral and distributed	IBM 3090 (32 MB)	MVS/XA VSE/SP VM/SP CICS/VS	DB2 DL/I VSAM	CSP, PL/I, FORTRAN, COBOL	VTAM	CATIA CAEDS
Seventh 1999-	Integral based on PC technology	Do 1 GBy	Windows	Access, SQL Serever	Delphi, Visual studio	Windows	CATIA AutoCAD

The **sixth phase** of IT development in Zastava is the phase of ***integral and distributed data processing*** (1989-1999), and this period was based on *Project of information system of RO FAZ*[15] *supported with automatic data processing* (October 1987). New equipment had been installed during the September 1988 and was included: IBM 3090/150E computer with 32Mb of RAM and 80Mb of external memory in direct approach, OS MVS/XA, relational databases DB2, CSP program language of forth generation, software for business graphic AS and software for computer graphic CATIA and CAEDS. The terminal network had been extracting to 128 new terminals and during 1989/90 they added 66 more terminals, so the network had 405 terminals connected with the main center. That configuration provided ability for development of new on line software applications.

From 1999 started the **seventh phase** ***Integral phase based on PC technology***. Significant special feature that characterized the beginning of this phase was the destruction during the NATO bombing. The bomb hit the main building exactly on 7th April and destroyed all central resources, so the rest of the network became unusable. Soon after that event Zastava started to construct new information sys-

[15] RO FAZ was the name for Factory of Automobiles Zastava

tem in Zastava car factory according to *Investment plan of temporary solution and new information system of Zastava automobile*.

IT building after NATO attack

They decided to relay on Delphi programme language, Windows operation and communication systems with Access and SQL for data management. Internet had become a part of everyday use with all supporting services and advantages for employed stuff and external users. The communication infrastructure today is based on combination of optical cables, UTP connectors and wireless technology.

Big problem of consistency of data was override by conversion of all databases which was supported with DB/2 to new Access and TXT format.

They created two languages web presentation for Zastava automobili, and that presentation can be found on url: http://www.zastava-automobili.com/sr/zastava.htm.

The future of IT development in Zastava depends on the attitude of their strategic partners FIAT.

Web presentation of Zastava

2. Few words about IT in FIAT

The history of information systems in FIAT is as interesting as it is in Zastava. The main difference is that Zastava relay on their own resources from the first day and they were buying hardware and software for internal development of databases and data processing. Until 2000 FIAT has the same way of IT development, more or less, although the FIAT is much more extended system in compare with Zastava.

Then they decided to switch their information and communication development to technological services and solutions for **outsourcing** information systems and development of eBusiness solutions and telecommunications. The necessities for all required information in FIAT have been covered by the list of these firms:[16]

ITS S.r.l. This company offers its clients a **complete range of infrastructural services for the management of hardware systems and communications networks**. ITS is present directly or indirectly in all the countries where Fiat operates. Fiat

G.S.A. S.r.l. This company focuses on the **development and maintenance of application software**, providing knowhow in all the principal areas of information technology and covering every aspect of business operation. GSA is present directly or indirectly throughout the world.

[16] http://www.fiatgroup.com/en-us/shai/banns/budgets/Documents/BIL2000_Rel_Gest_ING.pdf

eSPIN S.p.A. This company was created toward the end of 2000 as a joint venture of Business Solutions (70%), Cap Gemini- Ernst&Young (20%) and Oracle (10%) to **provide companies with a complete, integrated and innovative range of business-tobusiness solutions and corporate management systems**.

Koinet S.p.A. Koinet is a communications and service portal created **to offer businesses and managers a wide range of information, news and professional services that can facilitate the handling of management tasks**.

Atlanet S.p.A. Created toward the end of 2000 by merging Telexis and Acea Telefonica, Atlanet is a joint venture of Fiat (about 30%), IFIL (3%), Acea (33%) and Telefónica de España (34%). It develops **telecommunications, data transmission and general connectivity services**. It also holds a 12% interest in IPSE 2000, which was recently awarded an UMTS license in Italy.

Web presentation of FIAT

Fast Buyer S.p.A. This company acts as a **procurement center for purchasing raw materials, corporate services, auxiliary production materials and commodities**. It handles a business volume that has already exceeded 1.5 billion euros. **Through its portal, it offers e-procurement, marketplace and value-added services to corporate users**, making a large array of industrial items available to its clients. Drawing on the expertise and technology the Fiat Group developed in this area, it delivers solutions that help clients improve the efficiency and effectiveness of their procurement systems.

The most recent significant step for IT development in FIAT was the decision of buying integral information system SAP[17]. Following its 2005 decision to reorganize and improve some of its key processes in accordance with the strategic guidelines of the FIAT Group, Fiat Auto chose SAP for Automotive as the foundation to harness and simplify the complexity of its business processes. Fiat Auto is now underpinning its core business processes with industry-specific functionality from mySAP ERP, integrating disparate legacy systems that it needs to keep online with the SAP NetWeaver® platform, and cutting out redundant data entry processes.

“SAP software is a key enabler helping us achieve the aims we’ve set for our business transformation,” said Vincenzo Giannelli, CIO, FIAT Auto. “In the first wave of the rollout, we’ve gained tighter control on financial and procurement processes. With the rollouts of SAP’s automotive suite applications, we’ll have a worldwide standard set of end-to-end business processes.”

With its January 2006 go-live with mySAP ERP and mySAP Supplier Relationship Management (mySAP SRM), the company achieved the first milestone in its global SAP rollout. The integrated enterprise resource planning (ERP) and SRM solution is helping Fiat Auto production sites in Italy gain centralized control over workflows in finance, analytical accounting and procurement, accelerating the processes of managing indirect materials, contracts and purchase orders.

“With the first wave, we have implemented the SAP solution covering seven legal entities and six manufacturing sites in Italy for a total of more than 5,000 users,” said Vittorio Boero, SAP program manager, Fiat Auto. “The same solution also will be also implemented in our production sites in Poland and Brazil, for which the activities have been started already in April and are scheduled for completion in January 2007.”

Supporting Fiat Auto’s aims to keep all information and communications technology (ICT) systems linked for seamless workflows, SAP NetWeaver enables the interface of SAP applications to the software installations that Fiat Auto is keeping online for product development and manufacturing execu-

[17] The name SAP is acronym for Systems, Applications and Products in Data Processing (the original name was German: *Systeme, Anwendungen, Produkte*). It started in 1972 by five former IBM employees in Mannheim, Germany and it states that it is the world largest inter-enterprise software company and the world’s forth-largest independent software supplier, overall. SAP is an extremely complicated system where no one individual can understand all of it.
(**source:** *http://searchsap.techtarget.com/sDefinition/0,,sid21_gci21□190,00.html*)

tion. The SAP implementation at Fiat leverages the end-to-end process integration capabilities of the SAP NetWeaver® platform in particular, SAP NetWeaver® Exchange Infrastructure to simplify and unify purchasing processes and data exchange with suppliers.

When the rollout is completed, the ERP and SRM solution will be handling a half-million messages per day with Fiat's more than 20,000 key suppliers. These highly efficient and collaborative capabilities will play a key role in enabling the company's expansion plans. Following the rollouts of SAP applications powering core processes, Fiat Auto aims to extend the deployment of mySAP ERP. The company is now working on the integration of direct material in the materials management and procurement processes, a phase of the rollout project that soon will go live in Italy. The carmaker is also currently defining the next steps of the SAP implementation, both in terms of functional and geographical extension.[18]

3. Conclusion - as a a s f r IA

When we conclude this research there were no new steps in astava's IT development. The Memorandum of strategic cooperation between FIAT and Zastava has been signed on May 2008. According to estimates of leaders in the astava's IT sector, the main direction of development will continue, and they expect further investment in the IT. They also expect that FIAT will probably apply the model they already used in the similar arrangements - a separation of IT department and forming a new company whose services will be used by the factory (***outsourcing model***).

They also realized that some of operations they used are not according to FIAT standards. For instance, FIAT wants to follow each part in manufacturing process, in any time, but Zastava does not yet have sources to provide that information.

Integral software in Zastava today

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CRISIS CONSULTING IN FUNCTION OF BUSINESS ENVIRONMENT DEVELOPMENT IN SERBIA[1]

Branko Mihailović, Jonel Subić, Drago Cvijanović[2]

Abstract

Inadequate economic development of Serbia is determined by many factors, among which the following stand out: a country geopolitics position decline, disadvantageous economy structure, loss of traditional markets, financial indiscipline at all levels, and management capacity and skills insufficiency. Companies have performed their activities in such business environment characterized by inefficiency and employees lack of motivation. In such circumstances, the economic system of Serbia is also confronted with global economic crisis unpredictable effects, what additionally aggravates domestic companies actual situation. So the measures that are worked out should stabilize business and create the opportunity to turn to profitable business. Also, the crisis situation resolution is being analyzed through participatory consulting, by merging the necessary human resources in terms of nonstructured business problems.

***Key words**: crisis, consulting, management, consolidation of companies*

Introduction

The government of Republic of Serbia described in 6 items the mechanism, according to which world financial crisis influenced unfavourably to our economy.[3]

1) Due to insolvency of developed markets has been decreased the inflow of foreign credit assets for Serbia, while the inflow of direct foreign investments has been decreased or decelerated.
2) It opens an issue how to finance a deficit of current accout, and boosts pressure on foreign exchange reserves and exchange rate, which leads to decrease of domestic production volume.
3) Therefore consumption must be decreased by state intervention or market its self, through significant devaluation of dinar and internal inflation.
4) Decrease of demand volume in the country, in combination with decreased size of demand in the world, influences unfavourably on production, which furthermore decreases the growth of Serbian economy.
5) At the same time intensify tensions of foreign producers for placing products on Serbian market, while the placement of domestic goods in abroad has been hindered, which had created a problem of Serbian economy non-competitiveness.
6) All together slow down or completely stop the economy growth, which reflects on employment, life standard and total life in Serbia. The crisis makes the strongest impact to metal complex and construction industry; the following one is to food industry.

In such conditions, the enterprises were enforced to use resources more rational and allocate them efficiently according to deteriorated business conditions. One of the way for enterprises to confront the crisis influence is exactly efficient allocation of working resources, i.e. personnel, which imply also regional experts exchange. Considering that future managers in domestic enterprises do not have enough business experience in market conditions, where the effects of global financial crisis additionally hinder business of the enterprise, there is inevitable external support in crisis management.

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[3] http://www.b92.net/info/vesti/index.php?yyyy=2009&mm=01&dd=17&nav_category=206&nav_id=339731

Classical consulting implies that consultant executes creation of enterprise's analysis and concept how to get out of the crisis. Its participation in operational daily process of decision-making is almost imperceptible. The consultant supplies management with analysis results, which are the base for decision-making. In this type of consulting, the management keep managing the enterprise and stays at disposal to the consultant, as contact person and partner for discussion. However, engaging the consultants is generally observed very critically. External consultants in some situations do not dispose with enough information, specific for the branch and specific enterprise. There is necessary enough time for the consultant to have access to unformal organization of the enterprise in crisis. On the other hand, he leans on advices and observes of employees in the enterprise, but it is limited by numerous factors of subjective nature.

Considering previously mentioned possibilities of consultants engagement, there can be said that the middle solution is the best one. It is necessary to invite the consultant as an active member within management of enterprise in crisis. Hereby, he becomes active and equal partner in management of enterprise.

Participative consulting is offered when the potential of enterprise's management is weak, but need to be expected its upgrowth, by consultant integration, which would futher lead to efficiency growth.[4]

1. Nature and causes of crisis in organization

Crisis situations are phenomena which follows functioning and development of crisis management, either as ex-ante activities to prevent crisis, or as ex-post activities to get out of already existing crisis.[5] However, the enterprise overpasses sequential phases of development, crisis and radical organizational (and other) changes. Whether will small enterprise run down (bankrupt) or survive, functioning with approximately identical number of employees, or even keep growing, depends on successful organizational (and other) changes in relation to existing enterprise's crisis repression[5].

Business of enterpise is unique process and its partition on growth and development phases, as well as crisis phases has been imposed in order to make easy the analysis of the enterprise in specific performances zones of its business. The concepts growth, development and crisis have the arbitrary nature and depend on adopted criteria (quality measure). Each organization is opposed to natural growth of entropy, i.e opposition to disorder and inordinateness[6].

The crisis in past decade had resulted macro-economic instability, market loss and isolation from technological progress[7]. Crisis condition is obvious in many organizations in Serbia, which is manifested through decrement of market participation and profitability, increased duties, inadequate investments and multiplication of new business attempts at the expense of the primary business. The crisis symptoms have characteristic to show mostly ex-post on situation in the enterprise.

Chronology of appear is as following: firstly develops strategic crisis, than success crisis and at the end – solvency crisis. However, the chronology of detection is completely reversed. In the first phase, the banks stint credit approval and than dramatically decreases own capital. At the end realizes the oversight to place on market, in time, the production inheritors and therefore stops the sale decrement.

Consulting company *Deloitte Touche* has developed the methodology of turning point in enterprise's business, which had consisted of three integrated steps[8]: Condition diagnosis of financial and productive possibilities of enterprise; Crisis management and Management of turning point. The first step involves the analysis of client's enterprise financial possibilities and gives insight in current financial position and projection of earning power, if current trends continue. The diagnosis of productive possibilities comprises: the analysis of supply and sale market, the analysis of production process and

[4] Seni , R., ( ): *Crisis management,* Library Dijalozi, Belgrade, 1996, p. 45.
[5] Cvijanovi , M. J. (2004): *Organizational changes*, Instute of Economy, Belgrade, p. 230.
[6] Cvijanovi , M. J. (2004): Organizational changes, Economic Institute, Belgrade, p. 232
[7] Cvetkovi , N. (200): „Restructing of enterpise in crisis conditions“, *Business policy*, 2003, vol. 32, no. 2, pp. 50-53.
[8] Deloitte & Touche, *Corporate Recovery Services in Central Europe*, 1994, p. 2

productive program, prices strategy, source of competitive advantages and similar. Recommendation of strategic alternatives for client's enterprise is based on diagnosis of financial condition and productive possibilities. The second step is crisis management, which, according to *Deloitte Touche* approach, comprises five activity groups: financial restructuring, sale of needless assets, product rationalization, regularly determination of employee number and review of market. The third step in crisis surpassing is management of turning point, which comprises financial and productive restructuring. This step goal is to enter the enterprise into profitability zone. The strategic turning point provides enterprise to make an adequate position on the market.

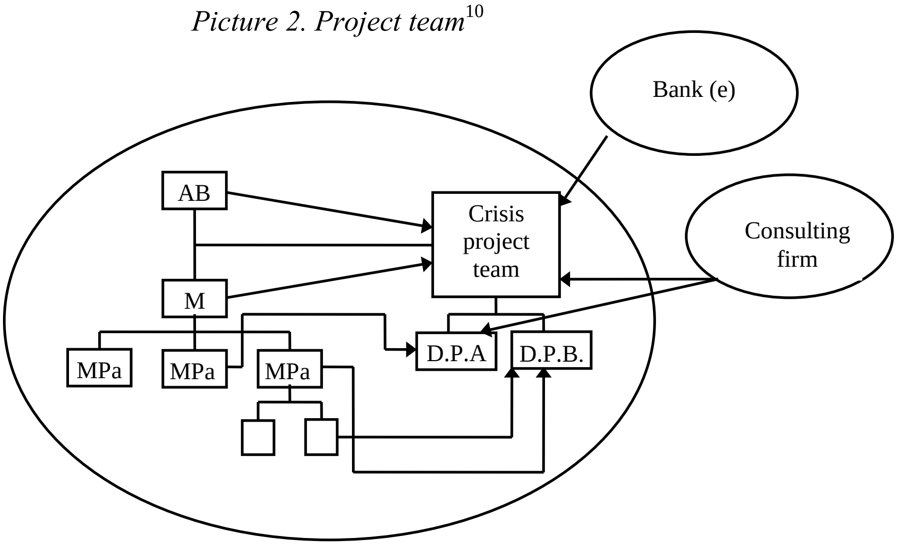
Often happends that enterprise's management in the crisis vacillates in overtaking the first step in interrupting the collaps of the enterprise. Fast and synchronized actions are necessary, in order to make swift, positive results in crisis repression. Innitial positive effects should strenghten future measures conduction.

2. Organizational forms of crisis management

Organizational forms of crisis management depend on size of the enterprise, as well as on manager's capability. It is considered [9] that exist three organizational forms of crisis management: project team, “manager in shadow”, “individual fighter”. The project is a way for the enterprise to solve problems it faces with. The process of crisis repression could be interpreted as the project due to its time-limited effect and problems, which comprise more fields. In that situation can be applied concept of projects managing, considering that there can form **one or more projective teams**, specialized for the crisis repression. Picture 2 shows a scheme of such projective organization.

The consultant is invited as an active member of management of the enterprise in crisis. In such conditions, he becomes an equal partner in overcoming the business problems. Nevertheless, the team approach, which implies close cooperation of the consultant with other members of enterprise's management applies, in order to create concrete measures for crisis repression and active participation in their conduction. Here is to express the significance of personnel issues resolution and internal structuring of crisis team. As members of crisis team can be: representative of Administrative Board and management, representatives of the most estimated banks, consulting company. The size of working team should stay tightly restricted. Experience shows that the optimal number is between three and five persons. Thereat are very important, so called, action teams (Task Force), which participate in solving the specific problems in projective activity. Model of projective team has major appliance in big enterprises.

Picture 2. Project team[10]

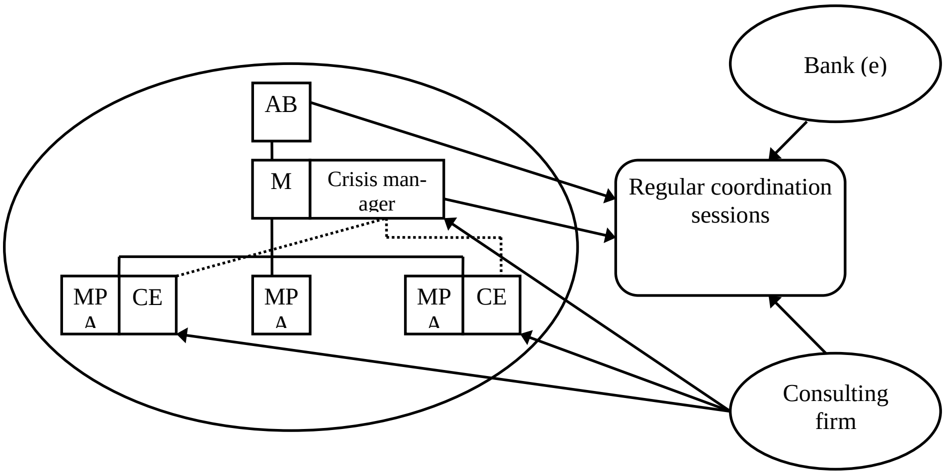


[9] Luthy, M. (1988): *Unternehmenskrisen und Restrukturierungen*, Verlag Paul Haupt, Bern and Stuttgar, p. 130.
[10] Luthy, M. (1988): *Unternehmenskrisen und Restrukturierungen*, Verlag Paul Haupt, Bern and Stuttgart, p. 131.

M - Management
AB – Administrative Board
MPA – Management of partial area
D.P.A. (B) – Detailed project A (B)

The second organizational form, especially in our small and medium enterprises, has been presented by special crisis manager, i.e. " **ana r n s ado** in consideration that he was placed alongside with existing management (picture 3.).

Picture □. Model of "manager in shadow"[11]



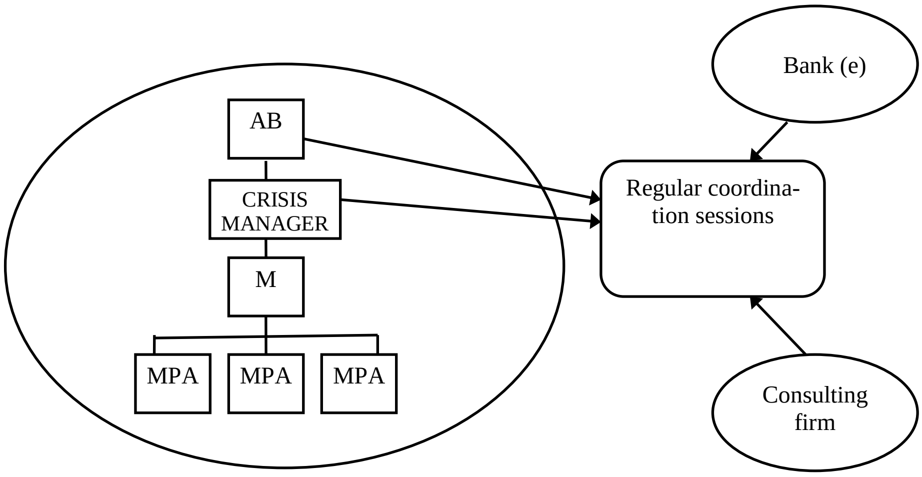
M - Management
AB – Administrative Board
MPA – Management of partial area
D.P.A. (B) – Detailed project A (B)
CE – Consultant of the enterpise

In this case, as it is presented in the picture, through periodical coordinative sessions maintains contact with consulting company, instead of taking over the bank representatives and consultants in formal crisis body of the enterprise. »Manager in shadow« takes over the role of crisis manager. The activities of crisis manager are primarily planning and restructuring conduction, and less – operational issues of current business. Successful appliance of this model implies ability of current management to coordinate with crisis manager, as well as capability and will to implement restructuring concept, the manager in shadow has done.

Model of " **nd d a f r** (picture 4) is applicable so far as it is shown that in small and medium enterprise existing management can not carry out necessary measures for crisis repression. Than the crisis manager takes formally position, with full line competence.

[11] Luthy, M. (1988): *Unternehmenskrisen und Restrukturierungen*, Verlag Paul Haupt, Bern and Stuttgart, p. 134.

Picture Model of "individual fighter"[12]



M - Management
AB – Administrative Board
MPA – Management of partial area
D.P.A. (B) – Detailed project A (B)
CE – Consultant of the enterpise

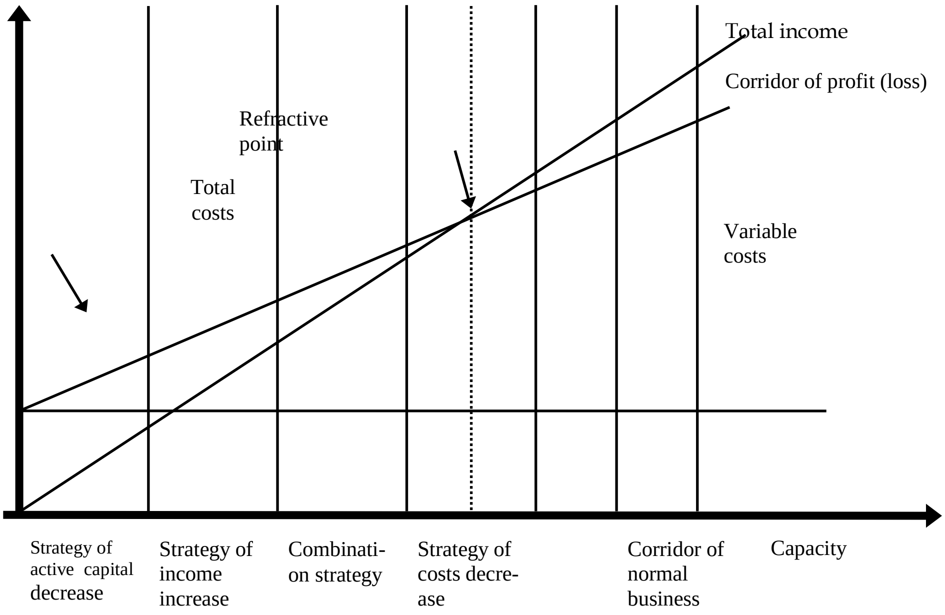
The analyzed models can combine, due to various applied concepts on various hierarchical levels. There can be established careful balance between short-term benefits and long-term losses, during formation of emergency measures and revitalization measures, in order not to jeopradize main strategy of the enterprise.

3. Necessary measures in crisis repression

The consultant has to find well compromise, considering that even the best long-term concepts are useless, if enterprise collapses in a short term. In this situation, the consultant has not got enough time for detailed evaluation of condition. Elementary, rough evaluation is enough. The most important is that the consultant gets support by enterprise's management for undertaking emergency measures in crisis repression. In phases of prosperity, enterprises often buy property not directly related to their basic activity. Sale of such property can mobilize significant solvency reserves. Emergency measures (income inrcease, property decrease, decrease of costs and their combination) are mostly determined by enterprise resources and by distance degree of enterprise business from breakpoint, as on picture 5.

[12] Luthy, M. (1988): *Unternehmenskrisen und Restrukturierungen*, Verlag Paul Haupt, Bern and Stuttgart, p. 135.

Picture . Decision making on type of following operational strategy[13]



If the consultant manages to motivate employees and thereby realizes short-term improvements in business, there can be expected, with high certainty, repression of crisis situation. Besides, there is a need for adequate value analysis, which represents a process of identification and elimination of unnecessary costs, especially product or service.

4. Financing the consultative services in crisis conditions

Developed market economies, as an answer to global crisis effects, use non-orthodox package of measures (combining monetary relaxation and fiscal stimulus). It is directed to crisis repression, overcoming the recession tendencies and setting up the thrust in key market institutions, financial institutions and modern financial instruments. According to the considerations, we can learn a lesson and basic message for Serbian economy and other transitional economies, which complete, with delay, institutional frame of modern market economy.[14] In such conditions, **enterprises in Serbia are in paradox situation**: a way out from crisis "looks for" consulting services, which are very expensive, and the main reason for enterprise restructuring is financial crisis. The enterprises have no assets to buy consulting services and find the way out from "vicious circle". In past practice stand out three specific variations of financing the consulting services in enterprises which do not have enough own resources.[15]

Consulting services, financed by loaned assets from banks for development. In developing countries, many invest projects, than projects of structural adjustments and other projects, are financed by credits authorized by World Bank or other banks for development. The procedures used for identification, selection and engagement of the consultant have to be in harmony with rules, determined by the bank.

[13] Hofer, W. C. (0): „Turnaround Strategies", u W. F. Glueck, Strategic Management and Business Policy, McGraw – Hill Book Company, New York, p. 276.
[14] Vujovi , D. (200): „Global financial crisis – instructions and lesson for late transitional economies", *Enterprise s economics,* 2008, vol. 56, No. 1-2, pp. 28-38.
[15] Petrovi , P. (2002), „Demand increase for services of financial consulting", *Financies,* 2002, p. 556.

Consulting financed by various donations and loans. Many consulting services are financed from donations and loans, got through bilateral and multilateral programs. Each agency has its procedure, described in books of regulations and books of references. In some cases, accepting support inevitably implies also engagement of the consultant from donor-country, i.e. from the group of donor-countries, if it is about support by regional economic associations (like EU).

Consultative model for subsidizing small businesses. In some countries, small and medium enterprises can apply for grants and subsidies, which can use for engagement of consultants in specific purposes. In order to get the grant, potential client has to contact the Agency for Development of Small and Medium Enterprises and has to follow specific procedure. In major cases is given grant up to 50% of project prices, in consideration that there is a top limit.

Conclusion

Taking into consideration non-development of domestic enterprises' research capacities, consulting becomes necessary activity, which should accelerate transformation process and provide revitalization and permanent revival. There should discuss also on complexity and overall of business changes, in conditions of global economic crisis, considering that it is about non-structured issues which our enterprises face in business for the first time. Namely, business crisis is characterized by “chaos” and lack of adequate information. The crisis increases the entropy, i.e. enterprise's disorganization. In consideration that the entropy is defined as ambiquity measure, as a consequence of uninformed system, there can be consenquentially concluded that the entropy decreases in organization, as a system, with additional information. Therefore is necessary continual and adequate research, in order to provide always real information on problems in functioning, information on market, i.e. buyers and competitiveness. Such information provides to the enterprise that, through own action and business, decreases its own system entropy, or prevents its growth.

Consulting, as a professional discipline, represents exactly a product of enterprises' increased requirements for numerous and integrated information. The organization, by its business activities, will lead to reduction of entropy within system and produce positive effects on business ambience, as far as it has adequate and timely information. The significance of consulting is exactly in supplying the enterpise with needed business information for crisis overcoming.

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9. http://www.b92.net/info/vesti/index.php?yyyy=2009&mm=01&dd=17&nav_category=206&nav_id=339731

ADEQUATE FX REGIME MODEL SUITABLE FOR ITALIAN AND OTHER FOREIGN BANKS IN DOMESTIC BANKING SECTOR

Branko Živanović[1], *Milena Kovačević*[2]

Abstract

The so-called managing float FX regime of dinar causes mainly short-term financing of bank assets on one side and provides expensive and short-term liabilities on the other. International bank headquarters ("mother banks") commit their finances only in a short-term, bearing a different types (economic and translational) of risks present in the domestic banking sector. This in turn drives commercial banks to deal and invest in the short run and in a speculative way.

Implementing a different, a more appropriate FX regime model of RSD such as crawling peg as a bridge solution to a full euroization of the national economy, would put under control the economic and translational FX risks. The country credit rating for financing in the longer run would undoubtedly improve from speculative (BB-) to non speculative grade (BB+) using as reference the grading scale of rating agency S & P.

As the best midterm solution for the banks with majority of Italian and foreign capital and pure domestic banks in the Serbian market, the authors suggest crawling peg FX regime.

This regime will bring a lot more certainty in current exchange rate fluctuations of dinar and significantly decrease exposure of bank's assets by uncontrolled fluctuations of the national currency. This will enable withdrawing of cheaper liabilities in the significantly longer run by domestic banks with majority of foreign capital (daughter and granddaughter) from their foreign headquarters (HQ).

***Key words**: FX rate, national currency, floating rate, fixed rate, managing float, crawling peg and euroization.*

Introduction

No issue is more antique and traditional than dinar`s exchange rate model suitable for domestic banking sector. Hints of internationalization of domestic banking sector have actually been around for the last decade, even though they made only a small impact, however, the availability of foreign capital has not been used in a full scope capacity, due to the inadequate domestic FX regime. During 2000s the floating exchange rate of the national currency has been seen as one of the greatest achievements of the national economic and monetary policy. Most of the time, it has been talked about managed floating of dinar (RSD) as to get speculating at times about pure floating of the national currency and even of its perfect convertibility. The latest turn of the events in the national economic environment has proven just the opposite and questions this monetary policy stance. The authors' stand point is that we never had a perfect floating national currency exchange rate on one hand, and that so-called managed floating national currency exchange rate was a wrong approach on the other hand. Furthermore, the managing float approach causes mainly short-term financing of bank assets on one side and provides expensive and short-term liabilities on the other. Italian and other foreign banks headquarters invest their finances only in a short-term, bearing different types (economic and translational) of risks present in the domestic banking sector. This in turn drives their Serbian subsidiaries -domestic commercial banks to deal and invest in a short run and in a speculative way.

Replacing the existing so-called managed floating dinar's regime by an appropriate F regime model such as crawling peg as an arch to full euroization of the national economy, is likely to put under control the scope of FX risks – transactional, economic and translational. The adequate FX regime would stabilize dinar's volatility in the long run, which would undoubtedly upgrade Serbian credit rating from speculative (BB-) to non speculative grade (BB+) using as reference the grading scale of rating agency S & P

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1. Presence of Italian banks in the Serbian market

There is an evident presence of Italian banks in the Serbian market. Among those banks are: Unicredit Bank, Intesa SanPaolo and Findomestic bank. It is distinctive for them a high market share in financing retail and corporate business, high level of capital and significant capital adequacy, considerable number of clients and different type of open accounts. Banca Intesa is the biggest by the assets in the local market and it is the local banking leader. Another Italian bank, Unicredit is second best by the value of its assets and market share. Findomestic bank, last comer, has by far the smallest market share of them all. These banks with majority Italian ownership are accounted for 20% of the overall total balance sheet of domestic banking sector.

It is obvious that they have come with a mission, and have long term goals in the Serbian market.

Table 1. Italian banks in the Serbian market

Bank	Assets (RSD million)			Market Share (%)			Total Credit Exposure (%)			Deposits (%)		
	2006	2007	2008	2006	2007	2008	2006	2007	2008	2006	2007	2008
Banca Intesa a.d. Beograd	125220	194758	250201	10.70	8.02	15	10.16	12.55	16	15.76	15.94	14
Unicredit Bank Srbija a.d. Beograd	68380	73070	89514	5.8	4.51	5.04	4.88	5	4.5	8.25	6	5.5
Findomestic banka a.d. Beograd	6164	8095	12110	0.53	0.41	0.68	0.49	0.54	0.76	0.66	0.54	0.64
Total assets in banking sector balance sheet	1169179	1561805	1776919									

Source: *www.nbs.rs*

We can assume that their presence in the Serbian market would have been even larger, withdrawn funds from the headquarters, i.e. mother banks, cheaper and significantly longer term, their credit and loans, more price competitive in a significantly long run too on one hand and more productive and less speculative on the other.

One of the main reasons why the above said is not valid is inadequate F exchange dinar's regime. Inadequate dinar's F regime means short term and more expensive liabilities provided by Italian and other foreign mother banks (HQs) to their daughters in Serbia (subsidiaries). This means a lot less consumer spending, the end of domestic credit expansion and a lot more pain for the national economy. Mother banks' support to their subsidiaries and cross border lending used to be the mother's milk of bank's liabilities and domestic consumption's Main Street.

2. Current exchange rate regime in the Republic of Serbia - Fake Managed Floating -

The managed float exchange rate regime appears as a suitable solution for the emerging market economies. It is a surrogate of pure floating and allows central bank to use different policy measures to discourage short-term movements of the exchange rate, usually on daily bases. Pilbeam states that central bank shall under this regime intervene on exchange market by buying or selling of foreign currency in order to answer excessive daily fluctuations of domestic exchange rate or to stabilize the market in terms of liquidity. (Pilbeam, 1994:251-278)

Under a managed float exchange rate regime the authorities are not to have any announced targeted exchange rate level that needs to be defended but it is to be determined by market forces- not proclaimed, not announced, but not in the shadow too.

Most of the former transitional countries widely use managed float exchange rate regime mainly advised by IMF. Besides positive results that it brings it has shown a number of weaknesses and posed many questions that need to be answered regarding its effectiveness.

The type of managed float currently used in Serbian economy is incorrect because standard managed floating regime assumes, as it is said earlier, that the exchange rate of domestic currency should not target a certain level but avoid significant and uncontrolled fluctuations of domestic exchange rate. The authors are concerned that we are currently having a fixed RSD exchange rate in the shadow, but not regular managed float FX regime. Central monetary authorities do not publish exchange rate in the shadow formally, but it is obvious that they defend a certain level of dinar's F rate which is easily predictable. The targeted levels of FX RSD rate used to be fixed at 80 during this period, 90 for 2008., 100 for this year as being the last line of defense because the overshooting would completely endanger the legitimacy of managed float of RSD concept.

The reasons why the current concept is inadequate are numerous:

1. The exchange rate of RSD is very sensitive and is supported only by the Central Bank of Serbia interventions but it is not a result of healthy economy and export revenues.
2. It is directly dependable on quantity of domestic foreign exchange reserves that are at the disposal of the national central banking authorities, but are hardly renewable resources.
3. FX RSD rate fundamentally depends and is going to depend even more in the future on foreign direct investments and banking reserves that mother banks would supply their Serbian subsidiaries with.
4. The rate is so vulnerable that certain interest groups can destabilize it by speculative interventions on pretty shallow domestic FX market.
5. It can force the Serbian Central Bank to run out domestic foreign reserves from time to time unwillingly and uncontrollably.
6. Domestic FX foreign exchange market is pretty shallow and certain interest groups can destabilize it by speculative interventions.
7. The rate can force the NBS to keep referent interest rate (REPO rate) at the high level and put aside great amount of dinars sterilized and out of crediting process.
8. The NBS has no other mechanisms than interventions on the foreign exchange market to substantially answer depreciation pressures. The NBS can have only a small impact on RSD FX through short term market operations and certain decisions about required foreign reserves.
9. The fluctuating exchange rate causes negative anticipation of private market transactors about the future dinar depreciation.

It is undoubtedly clear to private market transactors that Serbian CB prefers fixed FX RSD in the shadow and it is defending it persistently by interventions from domestic foreign exchange reserves. It is also clear that this FX is not realistic, as it is balanced in the short run and is absolutely uncertain how long the CB will be able to defend the targeted level of FX rate of national currency (fixed FX RSD in the shadow).

Commercial banks have no dilemma about the potential instability of domestic currency thus their own reserves and investments protect of FX risk and deal with them in the short run and speculative way. Also mother banks thanks to instability of RSD and mistrust in its managed floating FX rate are not willing to transfer stable and long term banking reserves in their subsidiaries in Serbia. They deal in the short run and speculative way as well. At the end of this chain, the most reputable international rating agencies rank Serbia as a market suitable for a short term investing (so-called speculative investing), unfortunately not for a long term investing related to a country credit risk. The previously mentioned transactors are rather skeptical about the power of National Bank of Serbia (NBS) to defend FX RSD in the shadow (informally targeted level) in the long run, but they have no dilemma that NB of Serbia will succeed at this in the short run. This belief is supported by the last stand-by arrangement with the IMF[3]. Therefore it should not be expected that international bank headquarters

[3] Confidence of a private sector and banks is at its lowest point in last few years, and central bank unstable and uncertain monetary policy stance regarding the true exchange rate regime causes speculative bank activity and

with subsidiaries present in Serbia will believe in sustainability of the shadow FX RSD stability in the long run, and thus refrain from transferring of long term reserves and funds to their Serbian daughters and granddaughters in the future. Continuous effort of the NBS to keep so called RSD managed float which it obviously is not, as well as its evident inability to keep wanted levels of shadow fixed FX rate in the long run, will not lead reputable international agencies to rank Serbia as a country suitable for investing in the longer run.

3. Negative effects of fixed exchange rate in the 90s

Bearing in mind negative memories of the 90s it is more than obvious that monetary authorities found in dinar floating a sound monetary tool that seemed efficient as a nuclear power plant. The dinar FX rate is still under control, but if monetary authorities run it too hard, it will blow up and we will suffer a financial and FX Chernobyl, the one we already went through in the 90s. Without any doubt the dinar fake floating is radioactive and the task now is to find the proper substitute so it wouldn't detonate again.

During 2000s the floating exchange rate of the national currency has been seen as one of the greatest achievements of the national economic and monetary policy. Most of the time, it has been talked about managed floating of dinar as to get speculating at times about pure floating of the national currency and even of its perfect convertibility. The authors' stand point is that we never had a perfect floating national currency exchange rate on one hand, and that so-called managed floating national currency exchange rate was a wrong approach on the other hand.

As it can be seen from the equation bellow (Rabrenovic, Zivanovic, Simic, 1997) the perfect floating national currency exchange rate can be expressed by following methodological observations. If we disregard the influence of other factors the supply function of the national currency can be expressed as the growing price function p .

$$q' \quad f' \; p \qquad\qquad q' \succ 0, p \succ 0 \; . \tag{1}$$

If q' is differentiable on the arbitrary interval p_1, p_2 then

$$\frac{df'}{dp} \quad 0 \, . \tag{2}$$

If we suppose that the supply and demand functions are known

$$q \quad f \; p \qquad \text{and} \qquad q' \quad f' \; p \; . \tag{3}$$

The balanced exchange rate is determined from the equality of the supply and demand

$$q \quad q' , \tag{4}$$

that is

$$f \; p \quad f' \; p \; , \tag{5}$$

or

$$f \; p \; - f' \; p \quad 0 \, . \tag{6}$$

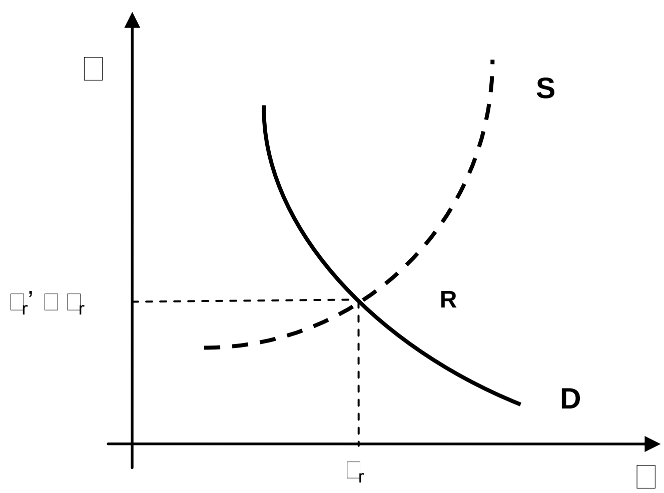
creates large risk of overshooting. Even the help from the conclusion of IMF stand-by arrangement with Serbia will have only short-lived stabilizing effects on currency level, and negative consequence of returning the principle amount with relatively high interest payments in only five years from the date the resources are drawn (grace period 2 years and 3 months). The 3 billion EUR from the whole amount of the stand-by arrangement with Serbia, can be spent in just a few months if "fake managed float" remains an option of the central bank.

The solution of the equation 5 or 6 gives the price p_r for which the supply of the national currency is equal to its demand. At the same time p_r presents the rate of the balance, the rate which "cleans the market".

The graphic condition of the balancing rate $R\ \ p_r, q_r\quad q_r^{'}$ presents the crossing point of the supply curve S and demand curve D :

$$f\ \ p\qquad f'\ \ p\qquad R\ \ p_r, q_r\quad q_r^{'} \qquad (7)$$

Figure 1. Balancing foreign exchange rate



Source: Rabrenovic, Zivanovic, Simic, 1997:46

Unregulated foreign exchange markets are closest to theoretical perfect markets that we have never had, because of the highest level of competition expressed in them. In the conditions of the unregulated (so-called unconducted) foreign exchange markets, the actual exchange rate (*R*) comes closer to the theoretical rate of balance.[4]

Our negative experience related to the period of the 90s is connected to a different FX market type – so called regulated foreign exchange market. In this period we didn't have fixed exchange rate in shadow, but pure fixed exchange rate which was completely unreal and unbalanced, followed by a spectrum of grays and blacks informal, but existing dinar's foreign exchange rates at the domestic F market. Dinar fake floating and its vulnerability and potential instability leads us to believe that 90s scenario and foreign currency shortage followed by fixed exchange rate model and regulated foreign exchange market could be seen again.

The regulated foreign exchange markets are characterized by emphasized presence of central monetary authorities and governments, which authoritatively put under control the inflow and outflow of the foreign currencies, due to their shortage caused by the existing exchange rate. The inflow of the foreign means of payment is registered at the Central Bank and most often concentrated at one place, wherefrom its planned distribution is performed afterwards, by the criteria of the general economy interests. Husted and Melvin notice spectrum of restriction on foreign currency transactions. "These restrictions take many forms, such as government licensing requirements, limited amounts of foreign currency that may be purchased, a limited time after the receipt of foreign currency before it must be sold to the central bank, or even outright prohibitions of foreign-currency use by private concerns." (Husted and Melvin, 1995:346)

[4] The exchange rate which "cleans" the foreign exchange market and balances the foreign finances.

The regulated foreign exchange markets are typical for former socialist economies – transitional economies as well as for the undeveloped countries (Rabrenovic, Zivanovic, Simic, 1997) are of opinion that the main characteristic of such "market" mechanisms is a permanent lagging of the foreign currencies supply after their demand $(S \prec D)$.[5]

Until now we have presented the demand for a foreign currency as

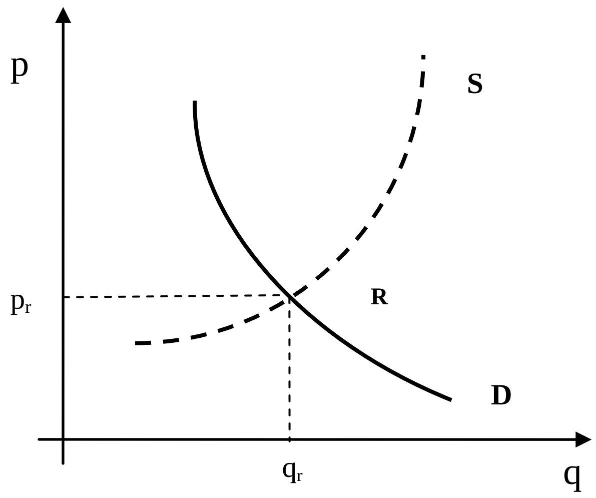
$$q = f(p). \qquad (8)$$

However, we can also present the price of the foreign currency as a demand function

$$p = f'(q). \qquad (9)$$

In this case the balanced currency rate is going to be on the level of p_r (Figure 2.).

Figure 2. Balancing foreign exchange rate



Source: Rabrenovic, Zivanovic, Simic, 1997:48

[5] This phenomenon has a character of the law of "nature" in the mentioned group of national economies. This law is not expressed only in short periods after the introduction of the "new" stabilization programmes which are accompanied by the following economic measures: devaluation of the national currency, denomination of the natural currency, the increased level of financial discipline (control), monetary contraction and etc. In this period the measures are supported by the adequate level of the currency (monetary) reserves. The central bank intervenes in the wide range due to export needs (M). Even citizens can come into a possession of foreign means of payment at commercial banks' counters (most often in cash or traveller's cheques). Commercial banks buy foreign currencies from the Central Bank (as a guarantee of the stabilization programme) for the national currency, which is at that moment rare because of the restrictive monetary policy of the government and the central monetary authorities.

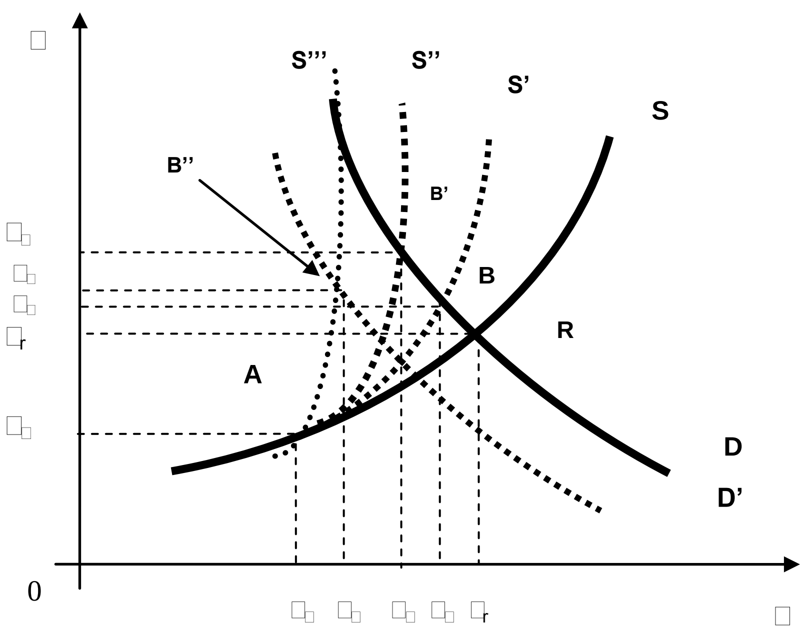
At the time mentioned, the supply and demand for foreign currencies are in equilibrium (S=D). Sometimes the foreign currency supply happens to surpass the demand (S>D). The momentarily intensified supply is due to a shortage of the national currency, citizens exchange the foreign means of payment - the yesterday form of stashed money (household reserves) for the national currency. Most frequently, the corporate sector is forced to do the same, to cede a part of its own (free) foreign means of payment (the deposits in the country and abroad in foreign currencies) to commercial banks, or to cede the means to the Central Bank, in order to get the domestic currency (which is at that moment insufficient) as to sustain its current liquidity.

This period usually lasts from 3 to 6 months, after which the recession symptoms begin to appear for the first time, as a reaction to the persistent FX course in the sphere of the monetary policy. The recession centres are overhauled by mild loosening of the monetary contractions which cause the inflationary sequences which again introduce us to the traditional scenario S<D (the character of the natural law).

The balanced currency rate p_r is a theoretical currency rate which, as a result of the autonomous courses of the supply and demand of the observed currency, is the closest to the exchange rate in unregulated foreign exchange market (although it differs even from it in some degree).

However, this law does not seem to be good at all in regulated foreign exchange markets. State authorities estimate that situation in the domestic foreign exchange market, at the level of the exchange rate p_r, would be in collision with national economic objectives.[6] Wishing to provide internal (domestic) economic balance, the authorities announce the price of the domestic currency achieving the cited objectives (through its fixed currency rate).

Figure □. Creation of Parallel F□ rates in regulated F□ markets



Source: Rabrenovic, Zivanovic, Simic, 1997:48

Most frequently such currency rate is overrated

$$p_1 \prec p_r . \qquad (10)$$

Up to the level q_1 the central bank will intercede at the official exchange rate, but it will not be able to satisfy the total demand for foreign currency $D\ 0, q_r$.

The low price of foreign currency causes the disproportion between the supply and demand in the range $AR\ q_1, q_r$.

As a consequence of the unsatisfied total demand, black (illegal) foreign exchange market begins to work. As the trading in this market includes a risk, there is a special kind of expenses in the form of risk-premium,[7] which is reflected in the reaction of the supply curve S . The reaction consists of the

[6] The national economic objectives: the height of GNP, the maximum degree of employment, the stability of prices, □>*M, etc.*

[7] Black market makers call the risk-premium popularly: "The fear expenses".

lowering of FX supply curve price elasticity El_s, i.e. increase of the foreign currency price at the illegal market segment

$$p_2 \succ p_r \succ p_1 \qquad (11)$$

This case can be taken as a classical example of the counter-productive act of the government, considering that now for a higher price p_2 than the former real one p_r (the level of the theoretical exchange rate $q \quad f^{'} \; r$, Figure 2.) the economy sector gets smaller amount of the foreign currency

$$q_1 \prec q_r. \qquad (12)$$

The final prices of the producers, whose products have a built-in export component, are higher for the amount of the risk premium, if they get foreign currencies in the black market. That affects the increase of the average price level causing inflationary sequences in national economy. If, furthermore, we take into consideration the transactions in the black market that are not taxed, the budget receipts will decrease too. Unfortunately, this is not at all the end of the chain of the negative effects of such government act. Namely, the largest consequences are reflected in draining of the income in sectors favoured by the government, as some sectors get a foreign currency at the price p_1, while the unfavoured sectors buy it in the illegal market at the considerably higher price p_2. All the above causes making of the imperfect price system[8] and distort economic structures in medium and long terms. (Rabrenovic, Zivanovic, Simic, 1997)
If the government decide to eliminate the black market, and consequently make an extra pressure on sellers, it will only result in even less elastic supply curve $S^{''}$:

$$El_{s''} \prec El_{s'} \prec El_s \qquad (13)$$

and higher risk premium

$$RB \prec RB'. \qquad (14)$$

The pressure towards sellers only leads to the higher price $p_{\square}$, increasing the previous error. Although the state controls and punishes the sellers more easily, only with the pressure on buyers (simultaneous pressure)[9] it can make the size of the black foreign exchange market smaller.

In that case the black foreign exchange market falls to the level $p_{\square}$, as a result of the effective demand D decrease. However, the currency rate at the level p_4 is still well above the official currency rate p_1, which becomes more difficult to defend. Speaking of this, by putting pressure on buyers, the government risks removing "the most honest players" in the market - the final consumers of a foreign currency. Usually the final consumers are the manufacturing firms, which deal with illegal business unwillingly, and after severe state measures have been introduced, they most often withdraw.[10] With the absence of their products, the need for the substitutes from abroad in the domestic market arises, and that only widens the currency gap and again stimulates the growth of the black foreign exchange market. (Rabrenovic, Zivanovic, Simic, 1997)

This scenario is already seen not only in our case. Husted and Melvin mention the cases of Mexico and Guatemala (Husted and Melvin, 5: 4). The authors blame the governments. "Obviously government policy creates the black market. Often, the government sets an official exchange rate that deviated widely from that the free market would establish. The demand arises because of legal restriction on buying foreign exchange, and the supply exists because of government – mandated official

[8] So called the price distortion.
[9] The pressure downwards buyers is more difficult and it rarely happens in practice.
[10] The statement is a result of the poll done in export-import firms and manufacturing firms.

exchange rates that offer less than the free market. Ironically, governments defend the need for foreign-exchange restrictions based on conserving scarce foreign exchange for high-priority users. But such restriction work to reduce the amount of foreign exchange that follows to the government as traders turn to the black market instead." (Husted and Melvin, 5: 4).

Dinar managed float regime engineers were more than happy that for a certain period since 2006 to mid 2008, dinar exchange rate was pretty stable and under control. It seemed as the real managed floating, which was under the control of the National Bank of Serbia. Continuously, without asking too many questions about company's ability to repay cross border debts and the NBs ability to keep such a high level of FX reserves forever, they have been keeping desired FX regime.

Despite the resolute dinar's resistance, the NBS is hardly keeping its value, introducing more and more restrictions and reminding us of the 0s by them. Reasons for correction of dinar's value and its FX type are various and will be presented in the next chapter. On the other hand its keeping at this level and its so called managed float type is more resembling of re-introduction of unreal fixed exchange rate of dinar, foreign currency shortage and parallel foreign exchange market segments.

4. Ar n s for nad a of rr n d nar s r and its value

4.1. Interventions of the NBS on foreign exchange market

The first blows on dinar which appeared in the mid 2008 and lasted till the first quarter of 2008, provoked NBS interventions on foreign exchange market in the amount of 1.498 900 000 Euros (nearly 1.5 billion Euros).

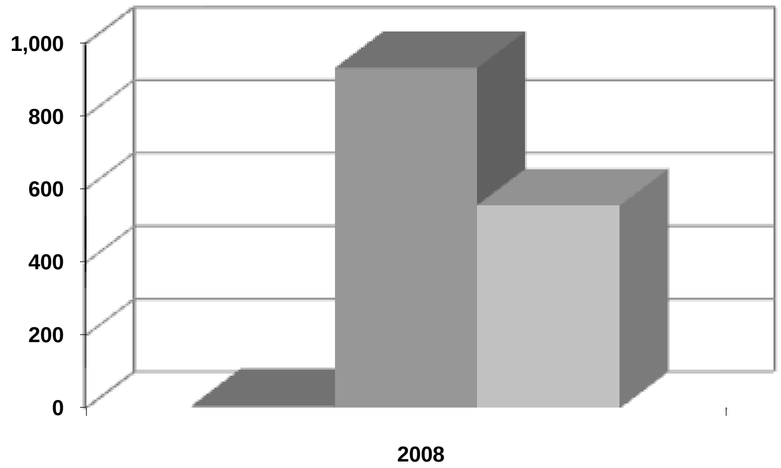
Table 2. NBS interventions on foreign exchange market

Year	Quarter	Amount of interventions
2008	III	9.000.000
	IV	933.500.000
2009	I	556.400.000
TOTAL		1.498.900.000

Source: *www.nbs.rs*

*Figure *

Interventions of the BS on foreign exchange market



Source: *www.nbs.rs*

This was very sensitive time, characterized by enormous pressure on the domestic currency and the NBS had the only solution - to intervene with significant amounts in order to keep targeted level of dinar's exchange rate, fixed in shadow. Central bank had to intervene even with the amounts of over 50 million Euros on a daily basis, to prevent overshooting psychological margin of hundred dinars for Euro, what would be the final end of proclaimed dinar's managed float regime and a definite sign of a wrong monetary policy approach.

4.2. Foreign Reserves level period October 2008 May 2009

Defending interventions caused significant drop in the national foreign reserves level. In the period from October 2008. till May 2009. foreign exchange reserves level decreased from nearly 9.8 billion Euros to 7.9 billion Euros, almost in the amount of 2 billion Euros. Not much was achieved with these interventions that caused the dramatic decline of foreign exchange reserves, having in mind that dinar was still depreciating to the level of around 95 RSD per Euro.

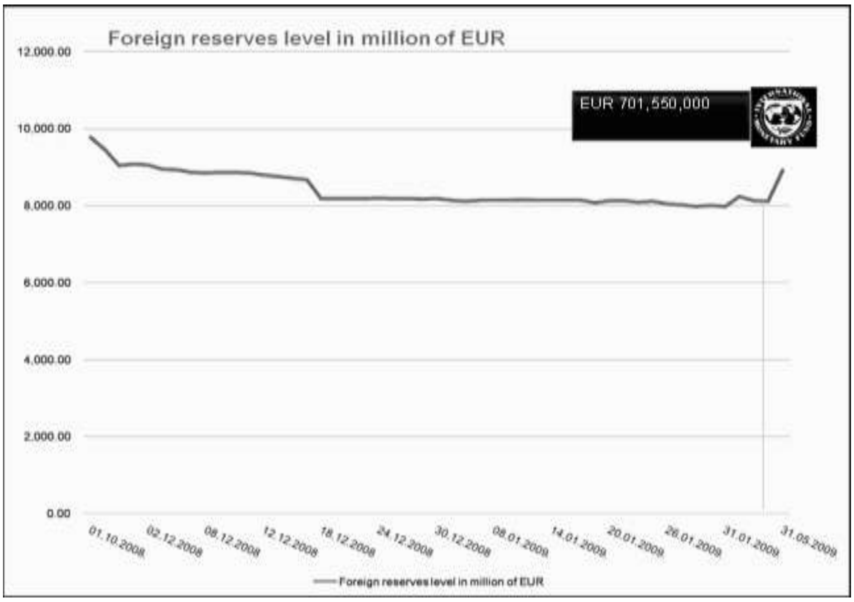
Table 3. Foreign Reserves level period October 2008 May 2009

Date	**Foreign reserves level in million of EUR**	**Date**	**Foreign reserves level in million of EUR**	**Date**	**Foreign reserves level in million of EUR**
01.10.2008.	**9.768,1**	18.12.2008	8.184,2	14.01.2009.	8.139,8
31.10.2008.	9.443,8	19.12.2008	8.179,5	15.01.2009.	8.140,0
30.11.2008	9.040,4	22.12.2008	8.187,7	16.01.2009.	8.136,4
01.12.2008	9.079,6	23.12.2008	8.183,8	19.01.2009.	8.078,8
02.12.2008	9.050,2	24.12.2008	8.189,6	20.01.2009.	8.122,2
03.12.2008	8.934,6	25.12.2008	8.176,9	21.01.2009.	8.123,6
04.12.2008	8.921,5	26.12.2008	8.181,4	22.01.2009.	8.091,2
05.12.2008	8.865,7	29.12.2008	8.168,1	23.01.2009.	8.113,1
08.12.2008	8.847,9	30.12.2008	8.175,7	26.01.2009.	8.051,7
09.12.2008	8.855,7	30.12.2008	8.175,7	27.01.2009.	8.017,8
10.12.2008	8.861,5	31.12.2008	8.148,0	28.01.2009.	7.979,0
11.12.2008	8.849,3	05.01.2009.	8.109,3	29.01.2009.	8.001,4
12.12.2008	8.796,7	06.01.2009.	8.143,4	31.01.2009.	7.980,3
15.12.2008	8.756,1	08.01.2009.	8.144,4	28.02.2009.	8.235,5
16.12.2008	8.709,6	09.01.2009.	8.141,9	30.03.2009.	8.134,3
17.12.2008	8.670,4	12.01.2009.	8.153,3	30.04.2009.	8.110,2
		13.01.2009.	8.143,8	31.05.2009.	8.914,4

Source: *www.nbs.rs*

The noticed growth of domestic foreign reserves in the amount of 701.550.000 EUR on May 19th, 2009. unfortunately, was not the result of a domestic export, nor even the privatization revenue, the push to growth came from the drawdown of the first tranche of pure credit arrangement intended only for a defence of domestic currency.

Figure □. Foreign Reserves level – period October 2008 – May 2009



Source: *www.nbs.rs*

4.3. Exchange Rate Movement (period 2008 2009)

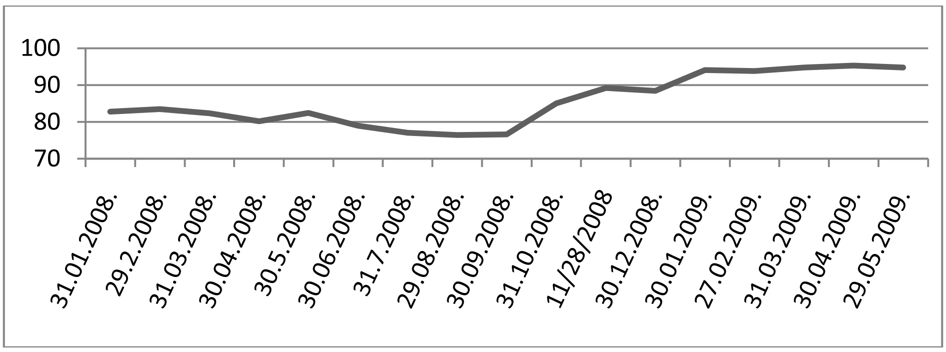
In 2008 wrong monetary policy stance regarding the exchange rate regime, showed its true nature. National Bank of Serbia had a very hard time keeping the stability of dinar exhange rate.

Table 4. Central Exchange Rate RSD/EUR

Date	exchange rate RSD/EUR	Date	exchange rate RSD/EUR
31.01.2008.	82,7715	31.10.2008.	84,9910
29.02.2008.	83,4635	**28.11.2008.**	**89,1953**
31.03.2008.	82,3146	30.12.2008.	88,3849
30.04.2008.	80,1295	30.01.2009.	94,1012
30.05.2008.	82,4302	27.02.2009.	93,8022
30.06.2008.	78,9784	31.03.2009.	94,7778
31.07.2008.	76,9939	**30.04.2009.**	**95,2396**
29.08.2008.	76,4442	29.05.2009.	94,7155
30.09.2008.	**76,5972**		

Source: *www.nbs.rs*

Figure 6. Central Exchange Rate RSD□EUR



Source: *www.nbs.rs*

In the second half of the year and later dinar depreciated heavily despite numerous foreign exchange interventions by the National Bank of Serbia. From the last quarter of 2008 till now, dinar currency depreciated against Euro from the level of 76 to 95 dinars per Euro, which proved our stand point that activities by the National Bank of Serbia in recent period had little or no effect what so ever. The NBS officials claimed they were not defending any particular rate of exchange rate but simply trying to avoid large daily fluctuations (managed float logic). This was simply not true, and everybody in the economy knew that National Bank of Serbia had in mind a certain limit - dinar should not go over. The targeted levels of FX RSD used to be fixed at 80 during 2006 and 2007. 90 for 2008 and 100 for this year as being the last line of defense because the overshooting would completely endanger the legitimacy of managed float of RSD concept.

5. Crawling peg FX standard Adequate solution

The arguments mentioned in the previous chapter and the depreciation of dinar of 27%, like we had in the last couple of months are highly alarming and this is the time to change the current fake FX regime – dinars managed floating. The most suitable solution to keep the exchange rate from overshooting in the upcoming period would be a crawling peg exchange rate regime of RSD to Euro.

Crawling peg is an exchange rate model seen as a hybrid of fixed exchange rate regimes which includes depreciation or appreciation of a current exchange rate of domestic currency in standard time intervals. The crawling peg basic model uses a formula which includes changes when certain conditions are met -inflation current adjustment. It can be thought as a type of a fixed exchange rate regime where the real exchange rate conversion factor of domestic currency against some other hard currency (usually EUR and USD) stays unchanged for a certain period of time when all relevant factors are taken into a consideration. It also can involve establishing a par value around which the rate can vary up to a given percent (band) where that par value is revised regularly according to a formula determined by the central bank authorities. In any form implemented, it surely represents a tool of monetary policy makers which is aimed at diminishing effects of on-going inflation combined with repressed foreign trade and speculative financial system allowing the monetary authorities to keep control over exchange rate influence on general level of prices.

Crawling peg standard is particularly suitable for countries whose economy greatly depends on imported goods and foreign investment thus creating a stable environment for trade and long term investments. It should seek stable or slowly moving exchange rate over time, enhancing greater confidence in domestic currency, eventually influencing lower inflation rate and greater demand for domestic currency.

One of the standard module to conduct a crawling peg regime is such that monetary authority announces future value of exchange rate for some upcoming period and this can be done for the period up to one year having the announced intervals on weekly, monthly or quarterly basis. This is implemented by using different projections associated with macroeconomic indicators so that the future exchange rate parity reflects the economic conditions compared with some other developed economy. The central bank is sending a clear signal of the expected future exchange rate to the market players directly. With consistent and trusted CB's policy of preannounced rate Commercial banks and private market transactors will be turned away from the speculative activities.

Adjusting frequently its level according to a calculated differential of consumer price indexes between the domestic economy and the economy that the national currency is pegged with, is another way of conducting crawling peg.

The third way of using crawling peg is when monetary authority maintains a fixed exchange rate in which they set a margin by which it can go up or down percentage wise against some hard currency. It has stabilizing effect on market but the limits have to be precisely defined and would not allow large depreciations of domestic currency rate. The corridor (band) around a so called par value must be narrowly defined.

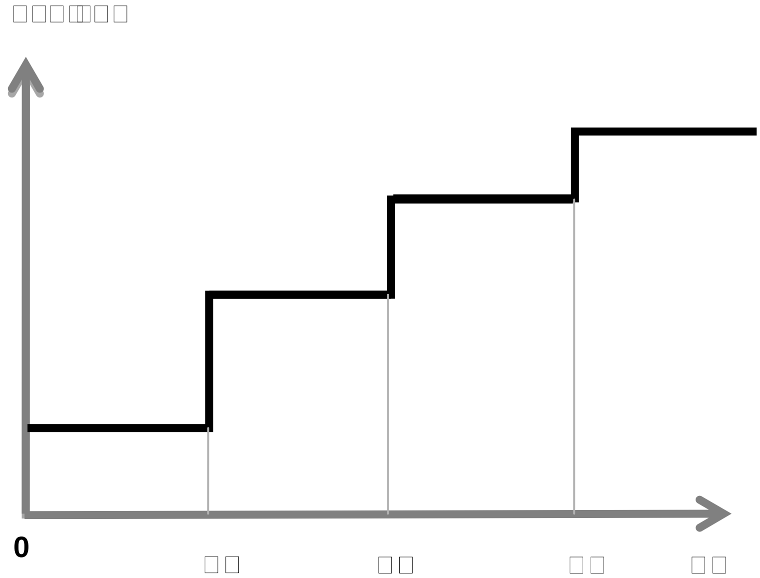
Besides the three models for determining standard module of conducting a crawling peg regime as mentioned above, Williamson made a proposal of other models that could fall in five groups divided by authors. (1) Harrod, Scott and Williamson proposed a decision-variant crawling peg, rather than a formula. (2) Black, Murphy and Modigliani and Askari proposed rather similar formula based on a moving average of a daily market exchange rates over some previous period. The idea was that a strong (weak) currency would be quoted at a rate appreciated (depreciated below) its parity, so that calculating a moving average of market rates to form the new parity would tend to appreciate (depreciate) it gradually. In contrast, Modigliani and Askari proposed to exempt the dollar from the normal rules, and to provide instead that the dollar crawl against the SDR so as to inflation-proof the latter asset; this was part of an ambitious model of a comprehensively redesigned international monetary system presented in their model. The model encompassed the following features*: Maximum rate of crawl (□ p.a.), frequency of crawl, jumps proscribed and countries covered*. (3) Meade and Cooper proposed using reserve change in order to create a presumption of a need to adjust the peg. (4) Willett proposed using the deviation of reserve levels from an internationally agreed norm to create an obligation to adjust the peg. (5) The German Council of Economic Experts proposed using the difference between the target German and actual foreign rates of inflation to determine an upward crawl for the domestic currency,to enable Germany to repel imported inflation (Williamson, 1981:4-8).

Crawling peg regime should not be taken as an ultimate and miracle solution. Savastano discusses the conditions that define actual timing of the regime's breakdown. He stands that the dynamics of the collapse of a crawling peg exchange rate in the presence of an explicit link between the fiscal deficit and domestic credit. He focused on speculative attack on international reserves in the presence of a sustained inconsistency between the country's fiscal and exchange rate policies (Savastano, 2).

Crawling FX standard as a monetary tool has been mainly used in the Latin America countries: Brazil (Fendt, 1981), Argentina (Martirena-Mantel, 1981), Mexico (Ortiz and Solis, 1981) etc, then in Botswana (Limi, 2006). There were some attempts in Turkey where the exchange rate is set by the Central Bank of Turkey every day (Altinkemer, 1990). Of European countries the biggest achievement regarding the crawling peg FX standard has been achieved in Hungary.

The authors' stand point is that the most adequate domestic F regime is a crawling peg module with equal time intervals depreciation preferably in small amounts. The domestic currency (RSD) exchange rate would be pegged to Euro. Equal time intervals would include quarterly RSD depreciations. The depreciation value and its interval would be targeted and announced in advance as an expected differential between current increase of domestic and Euro zone inflation. Possible corrective factor would be the level of domestic foreign exchange reserves, precisely the net asset level of domestic foreign exchange reserves. The advantage of the advanced announcement is in the prevention of RSD speculations. Market transactors would be aware and deeply convinced in the level of the forward exchange rate, the quarter one. Permanent devaluations would in the beginning score bigger value intervals, but with the time and more stable market occasions, the negative anticipation in terms of RSD forward exchange rate would be disappearing. Eliminating psychological effect related to expected RSD FX will cool down the overheated domestic FX market and stabilize the exchange rate in the longer run.

Figure . Crawling Peg Standard



Conclusion

Without any doubt floating exchange rate or managed floating of dinar are not adequate FX regime solutions for domestic currency. The results of keeping fake managed float of dinar have had devastating effects on foreign investment, speculative acitivities of banking sector, low country credit rating, and decline in reserves. Banking sector is mainly focused on speculative activity and not interested in allocating its resouces to corporate financing (through credit and loans activities) bearing in mind high level of FX risk exposure. The commercial banks simply settle for two week repo operations and make satisfying profits by buying those securities under such favorable conditions.

It is obvious that dinar's managed float is not a miracle solution and the NBS would be able to defend dinar's value and its stability only by continuous decreasing of national foreign reserves level and IMF's credit support. After a serious drop of national foreign reserves level in the amount of 2 billion of Euros, we withdrew a first tranche of pure credit arrangement intended only for a defence of domestic currency. The credit arrangement although granted by IMF is not earned and must be paid back with a substantial interest payments until the year 2016 and the question rises: is it not too costly and faulty to rapidly sell "family silver" (F reserves) or withdraw credit lines to protect desired level of dinar's exchange rate and its type?

To stop monetary policy Ludities and further blowing of dinar exchange bubble, the authors suggest to change current FX regime to crawling peg FX standard. The question is not to crawl or to float, the question is to crawl or to financially kneel- that we are I am afraid ready to do.

Our standpoint is that the most adequate domestic FX regime is a crawling peg module with equal time intervals depreciation preferably in small amounts. The domestic currency exchange rate would be pegged to Euro. Equal time intervals would include quarterly depreciations. The depreciation value and its interval would be targeted and announced in advance, as an expected differential between the current increase of domestic and Euro zone inflation. Possible corrective factor would be the level of domestic foreign exchange reserves, to be more precise the net asset level of domestic FX reserves. The advantage of the advanced announcement is in the prevention of dinar's speculations. Private market transactors would be aware and deeply convinced in the level of FX rate- the quarter one. Permanent devaluation would in the beginning score bigger value intervals, but with the time and more stable market occasions, the negative anticipation in terms of RSD forward exchange rate would be dissapering. Eliminating psychological effects related to expected dinar's F will cool down the overheated domestic FX market and stabilize the exchange rate in the longer run. Under a new FX regime, called by its true name crawling peg, targeted exchange rate level will be defended during one quarter. Central bank will be a holder of general trust and the authors belief is that economy will positively react to NBS's projections and that it will recover ever needed financing of the economy.

Increased confidence about movements in exchange rate would bring in general more stable environment which would in turn influence lower inflation and currency depreciation pressures- by eliminating dinar foreign exchange bubble.

We strongly believe that it would help in creating a stable atmosphere for foreign investment, which the whole business enviroment is dependable on, and would definitely stabilize financial and foreigh exchange circumstances and most probably upgrade the country credit risk grade from BB- to wanted BB+ which means that general economic conditions are now suitable not only for speculative and short term investing, but for longer run and productive investments.

Thanks to stability of domestic foreign exchange market, and stable and promising national currency, Italian and other foreign banks would probably supply their Serbian subsidiaries with cheaper and longer term credit support, allowing them credit and financial support of domestic companies with lower interest rates in particularly longer run. From speculative and short run investments, foreign bank subsidiaries will turn their financial sources to productive ones.

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DOING BUSINESS IN SERBIA: CASE OF STRATEGIC PARTNERSHIP BETWEEN FIAT AND ZASTAVA UNDER CIRCUMSTANCES OF GLOBAL TRENDS IN AUTOMOTIVE INDUSTRY*

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Abstract

In this paper we have tried to highlight the main characteristics of doing business in Serbian economy having in mind strategic cooperation between Fiat, the Italian car manufacturer, and Zastava, the only car manufacturer in Serbia. The paper consists of three parts. In the first part the most important transition indicators in Serbia have been analyzed as well as general ambience of doing business. Serbian government have put tremendous efforts in making economic ambience as attractive as possible for prospective foreign investors. Still there are open issues of how successful these efforts have been and what else has to be done. In the second part of this paper, recent global trends in automotive industry have been analyzed and their influence in Serbia and Western Balkans region. Finally, in the third part, the most important aspects of strategic cooperation between Fiat and Zastava have been analyzed, in order to put out the direction into which Serbia government can direct its activities so as to improve general economic ambience for business activities and further attracting of foreign investments.

Key words: *business, strategic management, automotive industry, privatization, restructuring*

1. Analysis of transition indicators and general environment for doing business in Serbia

It is more than eight years since huge political changes took place in Serbia (2000) and processes of transitional changes were intensified (mainly based on principles determined by Washington consensus). During that period Serbian government have put tremendous efforts to improve general economic ambience for business activities. Government officials claim that these efforts were quite successful. In the introduction to this paper we have tried to avoid subjective approach in estimation of the achieved results. Instead, we have decided to use analyses provided by certain renowned international institutions. According to the report by European bank for reconstruction and development the process of reforms in Serbia can be given a passable mark, i.e. 2, 89 on 1 to 4 scale (*EBRD Transition report*, 2009).

Avoiding black and white estimation, total current economic ambience in Serbia, apart from significant improvement, cannot be regarded as successful. Serbian economy faces numerous problems, intensified by negative effects of the world financial crisis. Unfortunately, many of the desired and expected goals of transition have not been achieved yet. Moreover, initial enthusiasm and faith that reforms would provide fast economic advance have been replaced by the lack of energy in implementation of reforms, even disbelief and pessimism regarding success of transitional reforms.

According to certain key areas significant for the process of transition, as estimated by EBRD, achieved results are very different. The best results have been achieved in liberalization of prices, trade and foreign currency exchange rate, privatization of small enterprises, as well as in reform of banking system. On the other hand, the least improvement has been achieved in implementation and adoption

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of the policy of competitiveness, as well as capital market development and non-banking financial institutions.

Table 1. Transition indicators in Serbia according to EBRD

	Privatiza-tion of big enter-prises	Privatiza-tion of small enter-prises	Restructu-ring of enterprises	Liberali-zation of prices	Liberali-zation of trade and foreign currency exchange rate
2001	1,00	3,00	1,00	4,00	2,67
2002	2,00	3,00	2,00	4,00	3,00
2003	2,33	3,00	2,00	4,00	3,00
2004	2,33	3,33	2,00	4,00	3,00
2005	2,67	3,33	2,33	4,00	3,33
2006	2,67	3,67	2,33	4,00	3,33
2007	2,67	3,67	2,33	4,00	3,33
2008	2,67	3,67	2,33	4,00	3,67

	Policy of competi-tiveness	Banks reform and liberaliza-tion of interest rates	Capital market and non-banking finan-cial institutions	Reform of total infra-stru-cture	Average mark
2001	1,00	1,00	1,00	2,00	1,52
2002	1,00	2,33	1,67	2,00	2,33
2003	1,00	2,33	2,00	2,00	2,41
2004	1,00	2,33	2,00	2,00	2,44
2005	1,00	2,67	2,00	2,00	2,59
2006	1,67	2,67	2,00	2,00	2,70
2007	2,00	2,67	2,00	2,00	2,74
2008	2,00	3,00	2,00	2,33	2,89

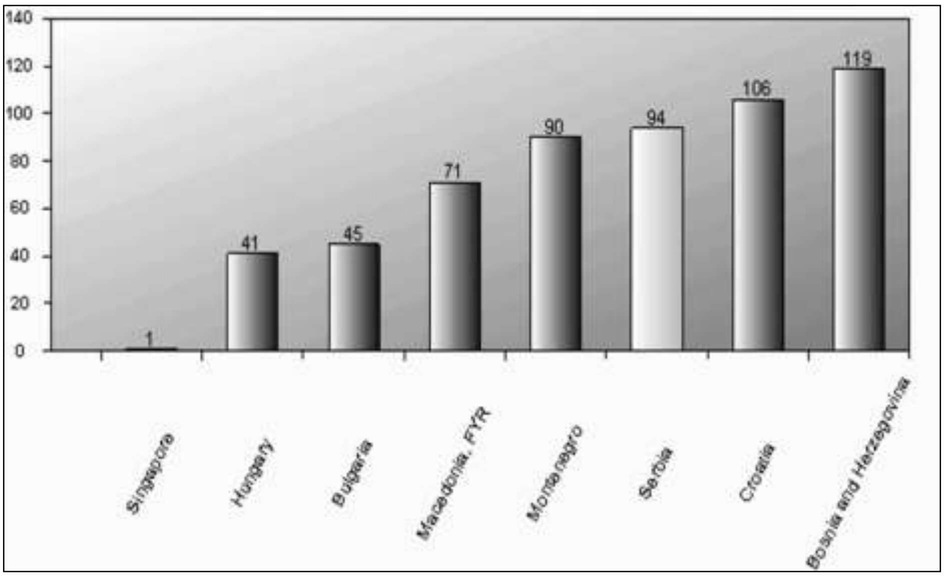
Source: *EBRD Transition report*, 2009

What can be concluded from the table given above is the increase in average mark given to Serbia and that is encouraging for sure. However, the process of transition in Serbia after the year 2000 has developed based on 'neo-liberal' model of reforms, defined under the strong influence of IMF. Economic problems which Serbia encounters today mainly resulted from implementation of this model (huge structural problems, enormous import, modest export in which final products do not dominate, huge deficit of payment balance, etc). Also, they are the consequence of hesitation and slow implementation of necessary economic reforms. Outbreak of global financial and economic crises caused the need to re-question this approach to economic development and seek possible new directions.

In future Serbia has to be more determined so as to complete the process of economic transformation (in order to achieve standards which would provide membership in EU) and create more propulsive economic ambience. In the last few years Serbia lost numerous opportunities, mainly due to political problems (several early elections, recognition of Kosovo independence, cooperation with the Tribunal for war crimes in former Yugoslavia, etc). By the end of 2008 significant consequences of global economic crisis became evident. Searching for new possibilities and resolution of open issues have become one of the main tasks for creation of basis for sustainable economic growth in future.

If simple comparative analysis is made of economic ambience in Serbia and some wider environment, for example Central and East European countries in the process of transition, it can be concluded that current economic and market ambience in Serbia is not so favorable and competitive in comparison to other Central and East European countries. Research by the World Bank, presented in the report called «Doing Business 2009» (*Doing Business, 2009*), in which conditions of doing business were analyzed based on 10 parameters in terms of easiness in doing business (starting from start-up business, provision of licenses for building up, employment, possibilities of loan taking, protection of investors, contracts, and ending with closing up of companies) shows that business ambience in Serbia is ranked 94 out of 181 countries.

Graph 1. Global ranking of Serbia in terms of business conditions



For example, if we compare Serbian economy with the economy of the so-called Visegrad group (Hungary, Slovakia, Czech Republic, Poland), Serbia lags behind in terms of analyzed conditions of doing business and has the worst position (Slovakia – ranked 36, Hungary (41), Czech Republic (75) and Poland (76) – for more details see Table 2.

Current, fairly unfavorable ranking of Serbia in terms of conditions for doing business is conditions by a great number of factors, among which the following can be pointed out:

- Starting up an enterprise and development of business – even though huge success was made, still these processes have been connected with long and complex procedures. Huge improvement was made when Serbian Business Registers Agency was established. Before its foundation, more than 55 days were needed to establish a company in Republic of Serbia. The whole procedure is significantly simplified (it takes 23 days) but still there are 22 different procedures. What is positive in the whole thing is that Serbian authorities are aware of this problem and that further reform of this procedure has been undertaken known as «Guillotine of legislature».

Table 2, Ranking according to conditions for doing business on the list of 181 countries in the world

Economy	Conditions for doing business	Starting up company	License for building	Employment	Registering ownership
Slovakia	36	48	53	83	7
Hungary	41	27	89	84	57
Czech Republic	75	86	86	59	65
Poland	76	145	158	82	84
Serbia	94	106	171	91	97
Economy	**Getting loans**	**Protection of investors**	**Taxes and fees**	**Protection of contract**	**Termination of company**
Slovakia	12	104	126	47	37
Hungary	28	113	111	12	55
Czech Republic	43	88	118	95	113
Poland	28	38	142	68	82
Serbia	28	70	126	96	99

Source: *Doing Business, 2009*

- In order to get various licenses for building, power connection facilities, phone, licenses issued by inspection or other authorities so as to start-up business – companies in Serbia encounter 20 procedures, which fulfillment requires approx. 279 days. In that sense, Serbia considerably lags behind Central and East European countries and this issue, in our opinion, represents on of the biggest problems, mainly for foreign investors. We strongly believe that global economic crisis is the right moment to start reform in this area. However, what worries us most is that not much has been done so far.
- Registering ownership – requires 6 procedures and takes approximately 111 days, which is unacceptably slow.
- When loan granting is concerned, Serbia has solid position and in terms of this indicator has the highest rank among all indicators analyzed by the World Bank experts (28th position). As researchers we have to point out that interest rates for loans granted to economic entities are very high, but that is not the topic of this paper.
- In terms of protection of investors Serbia occupies solid 70th position and is better ranked compared to some neighboring countries such as Macedonia (88), Bosnia and Herzegovina (113) and Croatia (126) but worse than Montenegro (24), Bulgaria and Romania (38)
- For employment of a new employee the company spends 18%, while for termination of employment it spends 25 wages.
- Republic of Serbia belongs to a group of countries with a complex system of taxes and fees – the number of annual fees is 66 times, that is for preparation, calculation and tax payment and other mandatory payments companies spend 279 hours, and the whole system is not transparent enough.
- Liquidation process – termination of enterprise lasts long and costs too much.
- Efficiency of legal system is not at satisfactory level. In order to collect bad debts in Serbia based on commercial contracts it takes 635 days and 36 procedures, and the rate of payment from insolvent companies is 23% average.
- What worries most is that analysts of the World bank in their Report «*Doing Business 2009*» noticed improvement in comparison to their first report in only one area (registering property ownership). For example, during the same period, some neighboring countries such as Former Yugoslav Republic of Macedonia completed reforms in 6 areas, Bosnia and Herzegovina, Bulgaria and Albania in 4, Croatia in 2 areas, etc. In other words, improvements in Serbia are not an issue, but they are slower in comparison to other countries in the neighborhood and in the region.

Given quality indicators of general economic ambience are very indicative if wider economic situation in Serbia is taken into consideration, which greatly depends on foreign direct investments that represent one of the key factors which influence total economic growth. Taking into account these facts, we will point out the importance of arrival of the big Italian car manufacturer – Fiat- in Serbia, which was agreed and carried out in 2008. Understanding of motives and reasons for arrival of Fiat in Serbia may be beneficial to Serbian authorities, economists and analysts to direct their efforts towards those areas where some problems still exist so as to improve economic ambience in Serbia, as well as business performances of all participants and the total economy.

2. Global trends in automotive industry

The field of automotive industry is very important for Serbian economy which in the former Yugoslavia had significant influence on total economic performances. In the second part of 1980s more than 200 000 units went out from Zastava in Kragujevac. They were exported to a huge number of countries, and the most significant job was export of Yugo model to US market. There was vertically integrated production of components, raw materials and spare parts, which made automotive industry one of the most important in former Yugoslavia. However, during 1990s there was a complete destruction of production and equipment, machinery and knowledge became obsolete, which was worsened by NATO bombing of the parts of the factory in 1999. As automotive industry lost its significance, it has to be restored from scratches. Thus, we have to point out the most important global trends in this very important branch of economy.

Although the firs car was invented in France in 1771, modern automobile industry was created by the Americans. «*It started in 1896 when the Duryea brothers from Springfield, Massachusetts produced thirette automobiles*» (*J. Harrison, 200□, pp. C 26□*). By the beginning of the 20th century having applied scientific methods of management Henry Ford introduced elements of standardization, specialization and opened doors to mass production of cars. Competition between *Ford Motor Company* and *General Motors* became a symbol of fight for dominance in automotive industry in the USA during the whole 20th century. In 1970s Japanese manufacturers became stronger, first of all Toyota/Lexus, Honda/Acura, Nissan/Infiniti, Mazda, Mitsubishi, and Subaru. Some years later, at the beginning of 1990s significance was given to cars produced in South Korea – Hyundai, Kia, and Daewoo. Contemporary car industry is the symbol of globalization. New countries are emerging as very significant car producers such as Mexico, Brazil, Malaysia, China, India, Turkey, South Africa (*J. Barnes □ M. Mor□ris, 2008, pp. □2*)

Competition becomes stronger, innovations become pre-requisite for survival, and changes become inevitable part of all organizations in the branch. Apart from technical and technological changes, institutional changes have significant influence which according to some researchers are connected with three types of pressure: regulative, mimetic and normative (*R. Van den Hoed □ Ph. J. Vergragt, 2006, pp. □□)*.

Analysis of any trends in contemporary car industry is not possible without an insight into influence of global financial and economic crisis. Crises in the car industry started in the second half of 2008. The crisis is primarily felt in the United States automobile manufacturing industry and, by extension, Canada, due to *the Automotive Products Trade Agreement*, but other automobile manufacturers, particularly those in Europe and Japan, are also suffering from the crisis.

The world automotive industry started to suffer from negative effects from the environment earlier, in the period 2003-2008, which was connected with extremely high growth in oil prices. This particularly referred to those categories of beneficiaries which were focused on buying large sport utility vehicles (SUVs) and pickup trucks, the main market of the American "Big Three" (*General Motors*, *Ford*, and *Chrysler*). High prices of oil provoked interest for alternative energy sources and innovations in the field of hybrid automobiles. On the other hand, for US automakers the big problem was considerably high wages than their non-unionized counterparts, including salaries, benefits, healthcare, and pensions. In return for labor peace, management granted concessions to its unions that resulted in uncompetitive cost structures and significant legacy costs.

In the second part of 2008 the situation became almost critical at the world market. Due to the influence of negative effects of global financial crisis and related credit crunch placed pressure on the prices of raw materials and caused further fall in demand. In certain countries, particularly the United States, the Big Three have been under heavy criticism since their vehicle offerings were largely fuel inefficient SUVs and light trucks, despite the increase in the price of oil. Accordingly, they suffered both from consumer perception of relatively higher quality models available from abroad - particularly from Japan and to some extent from Europe - and from *transplants*, foreign cars manufactured or assembled in the United States. As of the beginning of 2009, the vehicle companies of the world are being hit hard by the economic slowdown across national boundaries. Car companies from Asia, Europe, North America, and elsewhere have been forced to implement creative marketing strategies to entice reluctant consumers to purchase vehicles, when many firms are experiencing double digit percentage sales declines. Major manufacturers, including the Big Three and Toyota, are offering substantial discounts. Hyundai is even offering to allow customers to return their new cars if they lose.

Conditions of almost the biggest economic crisis ever left deep trace on the world automobile industry. Only in the USA in the field of car and light trucks manufacturing there was a drastic fall from 13.2 million units for the year 2008, down by about 2.9 million from the number of units sold in 2007. In 2009 further fall in sales is expected to more than 11 million of sold cars in USA. Globally, fall in sales in 2008 compared to the year 2007 totaled some 3 million units, from 55 million to 52 million of sold cars and light trucks. To make situation worse, further fall is expected in 2009 for some 4 million, that is total sales of about 48 million units.
(*www.plunkettresearch.com/Industries/AutomobilesTrucks/AutomobileTrends/tabid/89/Default*).

Many big car manufacturers encounter numerous serious problems due to fall in sale:
- Saab, GM and Chrysler – announced bankruptcy (prior to that GM and Chrysler received together $17.4 billion federal aid)
- Toyota and many European automobile manufacturers got significant amount of financial aid by the government
- Peugeot/Citroen announced huge lay offs of employees, but not on the territory of France, which provoked fierce reactions from the European Commission.
- Problems of automotive industry are not only connected with that branch. It is a vertically integrated production which huge number of suppliers of car components depend on. Fall in demand for final product has significant consequences in decrease of production in all successive stages of production of raw materials, spare parts and other car equipment. This problem is particularly evident in the countries of Central and East Europe. The issue of closing up some production plants attracted significant attention of some researchers (*R. Alaez Aller & M. Barneto-Carmona, 2008, pp. 62*).

Two countries which are not expected to have problems globally are Korea and Mexico, "where auto making plants are modern, quality is good (actually quality is world class in Korea) and currency values have plummeted to the extent that cars and parts made in those two nations are now extremely competitive on a global basis" *(www.plunkettresearch.com/Industries/AutomobilesTrucks/AutomobileTrends/tabid/89/Default)*. South Korean makers Hyundai and Kia have established themselves as true, high-quality manufacturers with a growing global customer base. One of the particularly important trends in contemporary car industry is connected to strengthening of production capacities and manufacturers from China. Soon, huge exports of quality cars from this country can be expected.

From historical point of view, the years 2008-2009 will be remembered as completely unusual. Did anyone think a year ago that GM or Chrysler were going to bankrupt? For car industry in Serbia these years would be mean new start. Any crisis has losers and winners. Where in all these trends belongs strategic cooperation between Fiat and Zastava?

3. Fiat buys Zastava strategic cooperation as a chance fro both parties

FIAT is an acronym from the Italian «*Fabbrica Italiana Automobili Torino*». Founded in 1899 by the founder *Giovanni Agnelli*, FIAT nowadays represents global company which has companies located in more than 50 countries in the world and business contacts in more than 190 countries. With 1,990 million of units produced in 2007 Fiat is according to the report of International organization of car manufacturers occupied 11 place in the world (*www.oica.net*). FIAT Group employs more than 180 000 people and entails several businesses - Automobiles **(**produces and sells cars world-wide under the Fiat, Alfa Romeo, Lancia, Fiat Professional (light commercial vehicles) and Abarth brands, as well as luxury cars of Maserati and Ferrari**),** Agricultural and Construction Equipment **(**CNH - Case New Holland is a world leader manufacturing tractors and agricultural machinery through the Case IH, New Holland and Steyr brands, and construction equipment through the Case, New Holland and Kobelco brands) and Trucks and Commercial Vehicles **(**Iveco is internationally recognized in the road transportation sector. It designs, produces and sells a complete range of commercial vehicles under the Iveco brand, buses under the Irisbus brand, and fire-fighting and special purpose vehicles under the Iveco, Astra and Magirus brands).

Fiat Automobiles S.p.A

Fiat group has achieved significant results in the past years. The most important financial indicators for Fiat Group for the period 2006-08 can be seen in the Table 3. Even in the most difficult year of 2008 there was a growth in revenue and trading profit. In terms of revenue structure more than 64% comes from Europe (from Italy 24% and the rest of Europe 40%). According to the type of the source even 49.2% of revenue comes from business with automobiles. (*www.fiatgroup.com/en-us/group/default/Pages/default.aspx*). Good business results are due to very good management in the company.

Table 3. The most important financial indicators for FIAT Group 2006-2008 (million Euro)

	2006	2007	2008
Revenues	51,832	58,529	59,380
Trading Profit	1,951	3.233	3,362

Top management of the company, which consists of Mr. *Sergio Marchionne* (CEO), *Luca di Monte-zemolo* (Chairman) and *John Elkann* (Vice Chairman), succeeded in managing the company avoiding huge dangers and recognizing chances. During 2009 FIAT led very serious negotiations about taking over American Chrysler and German OPEL, Swedish SAAB and British Wauxall, with which it would acquire the status of one of the leading car manufacturers in the world. Having formulated aggressive growth strategy, FIAT has a chance to reduce some of its deficiencies, among which the most prominent are the lack of scale compared to peers, weak performance in Western Europe and weaker margins (DATAMONITOR, 2008, pp. 21).

Success of FIAT has not happened over night. For more than 40 years the prestigious award of the European Car of the Year has been awarded. During that period Fiat Group was awarded twelve times, what is more than any other European car producer. Nine out of 12 of these awards being won by Fiat Automobiles models. Most recently the Fiat Nuova 500 has won the award for European Car of the

Year 2008. Apart from this model the award for the European Car of the Year was given to the following models:

Table 4. Fiat models awarded The European Car of the Year award

- 1967: Fiat 124
- 1970: Fiat 128
- 1972: Fiat 127
- 1984: Fiat Uno
- 1989: Fiat Tipo
- 1995: Fiat Punto
- 1996: Fiat Bravo/Brava
- 2004: Fiat Panda
- 2008: Fiat 500

On the other hand, car manufacturing in Crvena Zastava in Kragujevac started in 1952 when only 5 cars were produced. The next year 25 units of the 750 model were made, known as popular Fi a and 361 units from additional program. Only a couple years later, in 1961 from the Kragujevac car manufacturing plants more than 10 000 cars went out (precisely 10 008 and 9 895 units of model 750 and 113 units of the new model of Zastava 1300/1500, according to Fiat license). The scope of production is bigger than 100 000 units Zastava first had in 1974 when 44 865 cars of Fica were produced, 13 115 famous «tristac» and 53 573 units of new Skala 101 model (redesigned version of FIAT 128). Maximum production Zastava had in the period 1987-89 when more than 200 000 units went out from the assembly line. During these years the «job of the century» was underway. It was the name for the business enterprise of exporting Yugo model to the USA. In USA Zastava exported more than 140 000 units of Yugo. Unfortunately, this job was not successful. Zastava was not given a second chance to learn a lesson out of that failure. Apart from USA, Zastava exported to more than 70 countries. The biggest were Egypt, Poland, UK, Greece, and Hungary.

1990s were the years of civil war in former Yugoslavia, for isolation and sanctions were disastrous for Zastava. From 1992 to 2008 the scope of production went from 4 616 (the least in 1999 when Serbia was bombed by NATO) to 13 355 units in 2004. Apart from the issue of small scope of production, obsolete technology, shortages in finances for research and development, Zastava experienced problems with a huge number of employees, broken relations with raw materials manufacturers and spare parts from the parts of former Yugoslavia, etc.

In 2007 cooperation with Fiat was restored. Namely, in that year assembling of Zastava 10 model started, what is anther name for Kragujevac version of Punto. In 2007 1435 units was assembled, while in 2008 there were twice more – 2 789 units.

As it can be seen, one of the biggest problems Zastava encounters for more than a decade is the low scope of production which opens a wide range of issues. Automotive industry is a very specific one, with huge input barriers and high standards of efficiency. Yet at the beginning of 1980s it was thought that «*minimum efficient scale in the casting of engine blocks is 100,000 units per annum, in the mak□ ing and assembly of the power train (engine and transmission) □00,000 units per annum, and in final assembly 200,000 units per annum*» (*M. Casson, 1986, pp. 110*). Only three years in its history Zastava was above the last mentioned standard, at the end of 1980s. Since then, standards at least doubled. All that led a huge wave of restructuring in the sphere of automotive industry, especially through activities of mergers and acquisitions (M&A).

Negotiations about cooperation between Fiat Group and Zastava, that is Government of the Republic of Serbia lasted for a short period time, which was extremely favorable for both sides. Agreement on strategic partnership which was concluded in mid 2008 was signed by Fiat representatives and Serbian government and meant establishment of the new joint company in which Fiat would have 70% and Serbian government 30% of ownership. For Serbian party it was very important that the Italian party was obliged to invest 700 mill euro in production of 200 000 A class cars by the end of the next year. Also, production of B class vehicles would start, increasing the total production of Zastava to 300 000 cars by the end of 2010. In that way, production in Zastava would increase 20 times by the end of 2009, that is 30 times within three years, compared to 12 350 cars produced last year. It is planned that before production of the two new models in Kragujevac, production of Fiat's model of Punto would be continued, that is Zastava 10 which is the trade mark of the car assembled in Zastava.

Model Zastava 10, i.e. Fiat Punto

Motives of the Serbian Government were the following: to increase production of a domestic automobile so as to reduce high imports of cars (especially second-hand ones) and negative influence on the balance of payment, to reduce budget appropriations in the form of subsidies so as to cover astava’s debts and „secure” social peace and finally, to launch vertically integrated companies of component producers. As one of the elements of the deal, the Serbian Government is obliged to invest 100 mill euro by the end of 2011 and guarantee incentives to the Italian producer in the next ten years such as tax incentives, support to Kragujevac in improvement of infrastructure and free land for enlargement of the capacities of the factory and proclaiming Kragujevac free tax zone. The above mentioned elements can be taken as a recipe for other towns in Serbia and a chance to improve business climate for doing business.

For the Serbian party, that is Zastava, the biggest advantages of this partnership are as follows:

- Increase in the scope of production – only in the first couple of months in 2009 the scope of production in Kragujevac production plants surpassed the total number of cars produced in 2008. Increase in the scope of production should lead to the increase in production efficiency, reduction of prices and the whole range of other positive effects.
- Enlargement of market, increase of exports – which presents one of the most prominent problems of the Serbian economy. Production of a quality car model creates possibilities for export in CEFTA countries, Russia and other markets.
- Reduction of budget subsidies, which brings about immediate benefits to tax payers in Serbia. As Zastava increases revenues and financial performances so would reduce the need for Serbian government subsidies. This was one of the disadvantages of Zastava's business and its existence, since it was not liquidated during the last 15 years and was «saved» by the Government in order to keep social peace.

Advantages for Fiat Group can be summarized as follows:

- Cheap and relatively professional labor that possesses certain technical qualifications.
- Younger workers who can find job in the company with big potential to learn and prosper
- Certain pool of suppliers, with which cooperation should be developed to increase quality in production of components.
- Relatively good infrastructure – railways and vicinity of Belgrade-Nis highway, that is the European corridor 10.
- Favorable fiscal and customs policy – tax on corporate profit in Serbia is among the lowest in the region (10%).
- State incentives for further investments.
- Some of the mutual dangers that both sides should take into account are the following:

– Unfavorable economic situation in Italy, Europe and in the world, where huge decrease in production and sale of cars can be expected in 2009
– Relatively high costs of production – in Kragujevac cars have still been assembled. Parts come from Italy and transportation costs are relatively high, which significantly reduces profit margin and earning power of the company.
– Small scope of production – there is no company in Europe which produces less than 50 000 units. With projected 15000 cars, production in Kragujevac cannot be too profitable.
– Punto, the model which is to be assembled is obsolete and is not sold any more in many European countries.
– Cultural differences and conflicts between the Italian and Serbian management style.

4. Instead of a conclusion

In the first part of this paper we have had a chance to see that despite tremendous efforts made by the Serbian Government, according to renowned international organizations (World Bank, EBRD) business ambience for doing business in Serbia still lags behind neighboring countries and in a wider environment of Central and East European countries (concretely V4 group). Thus, the arrival of the big Italian car manufacturer of Fiat group in Serbia is a very important business event. It is particularly important in the light of global trends in automotive industry, which suffers from huge economic crisis and the trends of consolidation that preceded. Under such circumstances, many big producers disappeared, power is re-grouped and re-distributed. For Serbia, cooperation with Fiat is a big chance to restore long troubled automotive industry, as well as a whole range of vertically integrated component producers. Also, this cooperation is a chance to make additional efforts towards improvement of business conditions and attractiveness of business ambience for new foreign direct investments (FDI).

Both parties have to be aware of the dangers and weaknesses which can appear in this strategic partnership. However, it also creates additional opportunities and chances in future, when the big economic crisis has ended. Serbian party gets a chance to find itself on the profiteer side in the crisis and occupy significant place in realization of strategic plans of growth of Fiat Group. Thus, a recipe for successful cooperation between Fiat and Government of the Republic of Serbia can be a «seed» for making additional efforts towards improvement of business ambience in Serbia providing a chance for Serbia to occupy somewhat better position in the reports of the international organizations.

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IMPLEMENTATION OF SEPA ELEMENTS IN SERBIA AND THE EFFECTS ON SMEs SECTOR

Emilija Vuksanović[1]*, Aleksandra Bradić-Martinović*[2]

Abstract

The European Union is in the process of creating integrated payment system in the euro zone within the SEPA project. This paper discussed the importance of the implementation of certain elements of this system to creating a more favorable business environment of SMEs in Serbia. The first part is dedicated to the analysis of objectives, characteristics, advantages and perspectives of the SEPA concept. Second part deals with analysis of the institutional foundations of the existing payment systems in Serbia. In this particular part there is a review of achieved level of compatibility of infrastructure and instruments with the European system, and the importance of the actual project implementation in the SEPA direct debit basis focused in the improving business environment of SMEs.

Key words: *SEPA, payment system, direct debit, direct credit, SME sector*

Introduction

The need for setting up an integral payment system in the Euro-area (**Single Euro Payment Area - SEPA**) emerged from the negative effects of incompatibility of individual national payment systems on the competitiveness of the European economy, after the introduction of the euro as a single currency. Regarding that national payment systems of European countries maintain specific solutions designed for the needs of their users, there is a significant difference in terms of technology, procedures, standards, types of services, the bank fees and the content used in the area of interbanking clearing and payments process. In such circumstances, companies had to have separate accounts for business in different countries, and citizens were not able to complete cross-border payment or purchase of goods and services with only one account.

To solve the deficiencies, as a first step, EU adopted Directive (2001) with the intent of the **harmonization of fees for payments services**. With regulation No. 2560/2001, the EU has introduced new rules for calculating fees for cross-border payments between EU member states. The rules are applied to all banks in the EU countries as well as to retail and corporate customers. Purpose of the new set of rules was: to enable companies to **transfer money fast, safely and cheaply** from one end of the EU to the other; to **harmonized the fees for domestic and cross-border payments** within the EU and to make it possible for the banks to **process payments automatically**, without manual processing. However, the key problem was not solved. Despite the introduction of **Trans-European Automated Real-time Gross Settlement Express Transfer System TARGET,** various instruments and standards still existed, so companies had to keep different accounts for business in different countries. On the other side, citizens were faced with significantly higher fees for cross-border payments and for collecting cash, comparing to the national fees. Therefore, the largest European banks and financial institutions set up a professional body - **The European Payments Council** http://www.europeanpaymentscouncil.eu), whose task was to establish a unified, efficient payment system in Euro-zone. Then, **The Council of Ministers for Economic and Financial Affairs - ECOFIN Council** formulated the **Payment Services Directive.**

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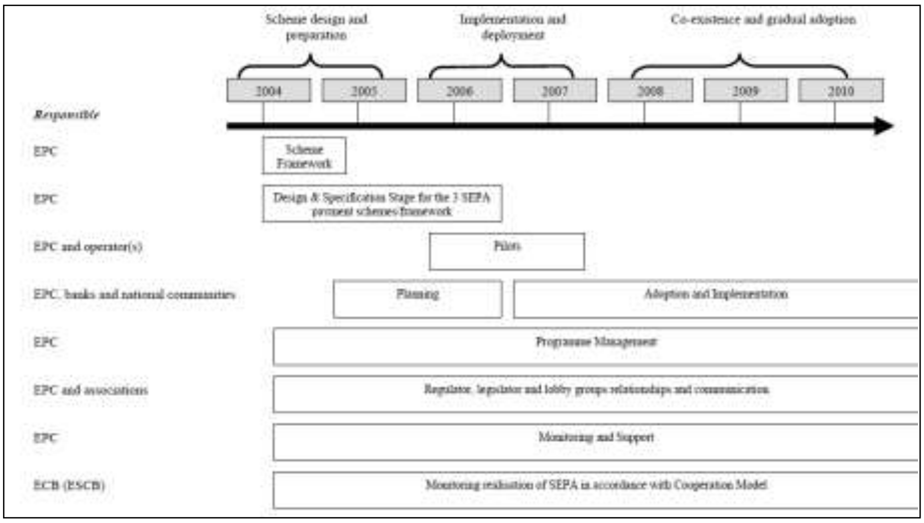
Graph1. Phases of SEPA implementation



Source[3]

The result of these activities was the project of establishing a unified system of payments in the euro region - SEPA, which would solve all mentioned disadvantages of existing payment system.

The process of implementation of SEPA project has organized in several phases, during the period 2004-2011.

I. **The first phase - Design and preparation** (January 2004 - June 2006) contained creation and design of payment system.
II. **The second phase Implementation and deployment** (mid. 2006 – 31st December 2007) was dedicated to the process of introduction, learning about and testing new SEPA instruments.
III. **The third phase Co-existence and gradual adoption** (January 2008. – 31st December 2010) is envisaged as a transition phase toward a new system.
IV. **The fourth phase** (2011) should be only the implementation phase of SEPA payment system.

1. SEPA and the competitiveness of EU economy

SEPA payment system is primarily designed for the retail payments i.e. small and micro payments, which amount is below 50 000 euro. This system is **integral** (covering the entire Euro-zone), **comprehensive** (applied to all payments) and **imperatival system** (because it commits all participants to carry out what is written in Directive). Its application involves the use of a single currency (euro), the use of unique standards and business practices, the use of a unique set of payment instruments, the establishment of effective infrastructure, mutually legal framework with clear regulations and ensures favorable prices of payment transactions.

Construction of unique payment infrastructure requires the introduction of uniform rules and standards for SEPA transactions. As SEPA payment system incorporates different channels, mechanisms and instruments, each of its parts are based on the principles that are **partly mutual and partly specific**. Common features that each of the SEPA subsystems contain is related to the effective implementation of all payments and specific characteristics are related only to certain subsystems i.e. segments. On the other hand, specific standards need to ensure functionality of each subsystem, as a part of a network. Defined standards are presented in the form of a single scheme and published as **Rules books** for each different segment of payment. SEPA common rules are related to credit transfers/payment (**SEPA**

[3] http://www.europeanpaymentscouncil.eu/documents/Roadmap%20public%20version%204th%20April%20amended%20March%2008.pdf

Credit Transfer - SCT) and direct debit/charge (**SEPA Direct Debit - SDD**). The SCT was implemented until January 2008 and the implementation of SDD will start during the 2009.

A unique scheme for credit transfers, **SEPA Credit Transfer - SCT**[4] provides a set of rules and procedures for credit transfers from account to account. These procedures include the situation when clients make payments over the available amount (within a specified value and time limit) and use a credit card as a legal payment instrument. Rules books provide a unique level of service and time frame in which financial institutions must perform this operation.

A unique scheme for direct debit, **SEPA Direct Debit - SDD**[5] provides a set of rules and procedures for the approval and recording of the money transfer from the account of a buyer to the account of the seller of goods or services, or to the account of another recipient. In this segment, it is a debit account that allows bank clients to make payments only to the amount actually available, without the exceeding. In this case, clients also use traditional payment card as an instrument. Terms of direct payments (SDD mechanism) determine the level of service and the shortest time frame in which financial institutions must be able to execute payment transaction. SDD exists in two forms (models):

1) When the debtor gives direct instruction to the vendor to charge his account and
2) When the debtor gives instruction to his bank to charge his account.

The global domain of SEPA project includes SEPA Scheme (common rules for SCT and SDD transactions), SEPA framework (for credit cards, cash and a mechanism for clearing and settlement) and the SEPA infrastructure (the technological standards, technical infrastructure and legal framework).

It is undoubtedly that the system will work in the future only as an **electronic transfer.** Also, is expected to be open for the development of additional services of payment system such as ***e-invoicing*** and ***e-reconciliation***. The first type of additional services (*e-invoicing*) refers to the ability for sending electronic invoices direct to the customer's bank by the seller and their automatic billing after bank's confirmation, on the basis of instructions from the seller that are already included in the invoice itself. Other additional service (*e-reconciliation*) refers to electronic settlement of debtor's and creditor's accounts, in specified time, for which the participants agree. It is also expected that the integration of payment systems will open a space for the new payment technologies, but some of them are not predictable yet.

General benefits of introducing a single payment system in the Euro-zone should be reflected in the **increase of the competitiveness of the European economy by providing a simple, efficient and low-cost payment system**. If, on the other hand, we look at the positive effects of the individual participants (consumers, trade sector, companies and banks) they differ significantly.
For **consumers** basic benefits should be the possibilities to have only one bank account for all payments in the entire zone and less complicated use of payment cards with lower fees.

Traders (merchants) will have benefits in the area of payment cards. Lower costs and higher speed of transactions are some of them, but probably the most important is the fact that the only one institution will process all payments, regardless of credit card issuer. In the previous period, the major problem of traders, in terms of credit cards, was that they must sign contracts with each individual issuer. The number of issuers is very large and they are located in different countries, so the payment fees they charge are varying from one to another. In accordance to this change, POS terminals that are used for processing must be able to support all types of payment cards.

Banks and institutions that are engaged in the field of payment system should feel the positive effects of the SEPA system in various aspects. In the integrated payment area banks get the opportunity to offer their services in the whole Euro-zone. This will affect the mobility of banks and the increase of their mutual competitive fight. Individual banks will have a larger possibility to cover a wider geographic area, with a better quality of service and lower prices. As a result, the business activities on the macro level will be more harmonized.

4 http://www.europeanpaymentscouncil.eu/knowledge_bank_detail.cfm?documents_id=136
5 http://www.europeanpaymentscouncil.eu/knowledge_bank_detail.cfm?documents_id=219

Companies should improve their efficiency and effectiveness based on the multiple ways and mechanisms to simplify management of their payments. The key change is related to introduction of a **single account for all inflows and outflows**, regardless of relations between different countries. This would eliminate the disadvantages of previous solutions in which the companies had to operate through a separate account for the domicile and foreign payments and through a separate account in case they have a foreign office. Higher level of economic and efficiency would be realized in the development of additional payment system services, that we already mentioned *e-invoicing* and *e-reconciliation*. According to some estimation, transition from cash to electronic payment will provide savings about 28 billion euro per year, while the transition with *e-invoicing* will provide additional savings that could be ranged between 50 and 100 billion euro (9, p.15).

2. General characteristics of the payment system in Serbia

During the last few years Serbia was carried out a series of reforms in the economic and financial sector, where the need of reforming the payment system was a prerequisite for further development. Through several projects, system was fundamentally reformed in line with global trends of implementation of higher quality instruments, procedures and infrastructure in the payment systems, under the influence of market competition and technological progress.

Today, Serbia has a modern and efficient payment system that is based on international standards and best practice of EU countries. Relevant international institutions (IMF, IBRD, ECB) testify about the results that Serbia achieved in this area. Mission of **Financial Sector Assessment Program FSAP** in March 2006 has evaluated payment system in Serbia with highest scores in all the relevant criteria.

The aim of the reform of payment system in Serbia was to provide:

1) Adjustment of our national payment infrastructure to European payment infrastructure;
2) Creation of basic conditions for the development of financial markets and banking business, in accordance with the content of e-banking and
3) Effective fight against the gray economy.

Existing activities that are conducted by a special importance were:

1) Abolition of the existing system in financial transactions which were monopoly,
2) Introduction of systems for securities trading, and
3) Introduction of payment cards in the system of retail, non-cash payments.

Abolition of monopolistic system in the payment area is certainly a significant change. The basic institutional assumptions for the implementation of these changes was made with new **Law of Payment Operations** (*Zakon o platnom prometu*), which anticipated transfer of payments from ZOP (Zavod za obra un i pla anja) to commercial banks (as of January , 200). This law also prescribed the conditions of technical and technological capability of banks to carry out these tasks, to use electronic payment orders, electronic transfer of funds and the new clearing system.

This institutional change abolished the difference in the organization of payment transactions in the country and abroad. In that way, Serbia eliminate the most limiting factor for the merging of national and international payment system, particularly in the field of unification of instruments, technologies and organizations (in the institutional and instrumental sense). A foreign practice, a new type of segmentation was established on the basis of economic characteristics of transactions – (1) Gross value transaction and (2) Small value transactions.

Central Bank took over the function of operational involvement in the inter-banking clearing. Model is selected in accordance with the trends and practices of developed countries and transition countries. In the process of creating **settlement points** between the banks, Serbia accepted the combined use of **net billing** (with a greater number of inter-banking accounts during the days/three) **for small payments** and **RTGS for large payments**, which works on the waiting list principles. In a technical sense, they are configured as one system that works on a single platform, with the operator and owner of the Central Bank of Serbia (NBS). Later, in 2005 Serbia introduced the possibility for banks to perform small payments in the RTGS, under the same costs as to the clearing payments.

Inter-bank clearing is carried out in the checks clearing system by the Banks association of Serbia, while the performance of obligations by net positions is realized through the RTGS system of National Bank of Serbia.

Technical and technological solutions for the functioning of the RTGS system made in accordance with international standards. Based on the alternative possibilities of connecting banks over three independent lines (SWIFT, a private network and the Internet), in case of system failure, it is possible to switch very quickly from the system out of the line to the backup system, sending messages in the SWIFT or XML format and ensuring security of data, using pairs of private and public keys.

Clearing of international payments, based on the principles of multilateral net calculation, was introduced in 2007. It is performed for the account of private and legal persons whose banks have headquarters in Serbia and in the territory of the state with which the National Bank of Serbia made an agreement on carrying out the calculation of net international payments. Participants in the clearing process are central banks that are signatories of the agreement and the bank with its central bank signed agreement based on participation in international payments. At the moment, this agreement is signed with the Central Bank of Bosnia and Herzegovina and Montenegro. It allows further lowering the costs of payment transactions, increase efficiency, establish singularity with foreign exchange payments in the country and facilitate cooperation with countries in the region and providing support for free trade.

3. Clearing of international payment and European integration

Clearing mechanism of international payments in foreign currency is now executing by the NBS, for the first time in history. The main reasons for this solution lie in the possibility that it provides a further increase of efficiency of payment systems, and indirectly the entire economy. In that sense, this mechanism enables further lowering costs of payment transactions, establishing the identity of international payment, foreign exchange payments in the country, raising the efficiency of payment transactions, providing additional support for cooperation with other countries in the region and free trade in general (CEFTA) and the contribution to the preparation for European integration (SEPA).

Starting from the assumption that the standards and rules that SEPA brings in the nearest future will become a matrix, which almost all European countries will seek to adapt, the NBS has acceded to making regulations which ensure the establishment of clearing with the foreign exchange and payment transactions by direct debit. The NBS made the Decision for inter-clearing payment in foreign currency[6], Operational rules for inter-clearing payment in foreign currency[7] and the Decision on carrying out payments by direct debit[8].

This legislation established the mechanisms that will facilitate easier connectivity and functioning of the payment system in our country with countries in the environment, and in the future to pave the way for swift connection of domestic foreign currency payment system with those who will work in the EU.

The overall mechanism of communication function in accordance with SWIFT standards according to which the use of two types of accounts as follows: MT-103 messages for the transfer of funds for the account of the user, and MT-102 messages that contain a group of payment for the account of the user. Orders execution is based on the method of approval limits and waiting lists. Participant may request from their central banks to increase or decrease the limit, which are granted depending on the conditions to be fulfilled. Sent message (how to meet the requirements for participation in the clearing system) is recorded in the bank account within the limit. If a negative position exceeds approved limits, a message goes to the wait. At the end of the cycle multilateral net position are calculated and the Central Bank get the information of net position of their banks.

[6] Odluka o me ubankarskom kliringu pla anja u devizama
[7] Operativna pravila za me ubankarski kliring pla anja u devizama
[8] Odluka o obavljanju platnog prometa po osnovu direktnih zadu enja

Alignment between the central banks is done through the account of the banks in the first-class international bank (in this case to the Deutsche Bank). Central banks are granting and charging bank accounts for their net position from the clearing, a bill is considered to be finite when each bank receives the billing statement of your account for clearing. This agreement is signed with the Central Bank of Bosnia and Herzegovina and Montenegro.

4. Direct debit and SMEs in Serbia

Major incompatibility with the principles of SEPA concept, at this moment in Serbia, exists in the area of operational function of direct payment. In order to eliminate these shortcomings, the NBS and Association of Serbian Banks were decided to implement SEPA concept in the field of direct debit. Institutional basis for implementation of that concept is Decision on carrying out payments by direct debit, prepared by the NBS in 2007.

Although the Law provides the execution of direct debit transactions (Art. 23 and 24) actually Serbia use the system of involuntary payment (Art. 47-49), which is not in accordance with the EU due to non-transparency. The existing system allows I, II and III order of priorities, according to which primacy belongs to the debt to the state, until the claims of business entities are in the III right priorities. Realization of transfer charges on the basis of I and II order of priorities will be made only through a process of enforced payment. Banks do not have insight into the basis of payment and a debtor does not have possibility to pay off a debt in the cheaper way. The level of control is lower at charging I and II degree of priority than III (in the case of I and II relations are between the applicant-enforced service charge, and in III applicant-bank service-charges enforced). With such a solution it is not possible for banks provide to their customers complete services in order of III priorities for client-creditor basis for billing and account receivable must take to the bank of your debtors (can not work to complete in your bank).

The basic principles of direct debit system in Serbia are as follows:

1) The ability of business customers to initiate the charge of the accounts of their debtor in their own bank;
2) Standardization of performance account debit in accordance with the SEPA rules;
3) Increasing of security in the implementation of base charges on the basis of a single registry of mandates;
4) Enabling the establishment of quality relationships between business entities;
5) Implementation by phases, connected with other services of payment system (Compulsory toll);
6) The possibility of connecting the authorities in the clearing system and
7) Cheaper implementation of the transfer charges.

It is expected that the introduction of inter-bank clearing system by debit accounts have significant positive effects on SMEs, either directly or indirectly, through the influence of the banking institutions, the state and authorities.

In the functioning of inter-bank clearing system, debit accounts by economic entities will be able to keep in different way and in that case to regulate better their mutual relations and to have greater security and lower cost of financial transactions.

1) It is believed that the implementation of a single registry, base charge or so called mandate, would provide an essential prerequisite for the verification of financial discipline of each business entity before the establishment of business relations.
2) Enabling charging of tax, duty and judicial claims by direct debit system would allow a significant decrease in the price of these transactions compared of their implementation of the system of enforced payment. According to current indicators, tariff charges, which is forced 3,000.00 dinars on the basis of legal persons and 1,300.00 dinars by entrepreneurs to be reduced to 80.00 per account in the system by inter-banking clearing system of debit accounts (see. 7, pp. 74).

Replacement of the enforced system with a system of direct debit is a further step in the development of market infrastructure for the payments and an important element in the realization of the prerequisites for inclusion of the banking system of Serbia in the single European payment area. Banking institutions, with the application of the methodology and standards of international payments, will be able to provide the necessary preconditions for the expansion of their offers and servicing their customers.

Conclusion

Payment system of Serbia is adapted to trends in the world, especially in the EU's process of legislative, technical and technological and professional and organizational significance. Instruments of payment transactions in Serbia containing all necessary data defined SEPA rules, credit transfer is also adaptable to a large extent SEPA rules and framework of the functioning of credit card is compliant with the possibility of functioning of one card for the entire zone. The latest step is the establishment of efficient and effective easily clearing mechanism of international payments in foreign currency through the NBS. Process of the elimination of incompatibility with the principles of SEPA concept in the domain of the functioning of the operating system of direct charge/debit is in progress.

When we try to estimate importance of the implementation of SEPA elements in Serbia and particularly in SMEs sector, it is important to bear in mind that, beside the need of establishing compatibility of payment systems, it is very important to change the business environment for SMEs. This additional dimension of influence stems from the characteristics of SEPA, i.e. the primary focusing on small and micro-payment and the establishment of a unified payment systems in the function of the increase in the competitiveness of the economy.

These goals and characteristics of SEPA concept determine its significance and prospects of development in terms of the current global financial crisis. In today's turbulent financial conditions SEPA gaining importance and remains a top priority because of its effect on efficiency and economy of operations. These effects will certainly be for Serbia in the coming period of exceptional importance, regardless of the pace of its approximation of the EU.

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FOREIGN BANK PENETRATION: BENEFITS AND HAZARDS FROM FOREIGN BANKS ENTRY TO TRANSITION COUNTRIES

Gradimir Kožetinac[1]

Abstract

One of the most striking developments in the banking sector in transition and emerging market economies has been the sharp increase of foreign banks entry during the last decade. Foreign owned banks have become major players in the financial system of these countries. However, foreign banks presence and the level of financial development in general vary considerably among the transition economies. Generally speaking, countries exert varying degrees of controls over foreign bank entry into their financial systems. This is due to their different perceptions of the pros and cons of foreign bank penetration. The pros of foreign banks entry include better resource allocation, higher competition and efficiency, lower probability of financial crisis, and enhanced public confidence in the banking sector. Critics of foreign banks entry have pointed to the risks for the stability of the local financial system, emphasising the danger of creating a less stable supply of bank credit, and loss of domestic banks' profitability.

***Key words**: bank, domestic financial sector, foreign bank entry, transition economies, financial stability*

Introduction and context

In the emerging economies and especially in the countries of South East Europe (SEE) and Central and Eastern Europe (CEE), the banking activity increased rapidly from the beginning of the 1990s. After carrying out the financial liberalization and lessening the limits for the foreign banks entry, a number of foreign banks entered the banking markets in those countries. Presently foreign banks greatly influence the banking sector in the transition economies. Foreign banks already possess more than 50 per cent of the equity capital of the banks in CEE. In many countries more than 80 per cent of the banking market is under the foreign banks control. The largest investors in the banking (financial) FDI of SEE and CEE countries are the Austrian, Italian and Greek banks.

However, the presence of foreign banks largely differs in the transition economies. So during the last decade foreign banks penetrated into some of CEE countries, but the degrees of their penetration differed. Some countries regarded the foreign strategic investors in the banking system as a means to quickly improve the quality of financial intermediation, while others chose to stay relatively closed for the foreign banks activities. The critics of the foreign banks entry have for instance pointed to the risks for the stability of the local financial system, emphasizing the danger of creating a less stable supply of bank credit.

Table 1. Banking Sector of Selected Transition Economies in Early Transition, 1995

Central Eastern Europe (CEE) and Russia

	Number of Banks (Foreign Owned Banks)	Asset Share of Foreign Banks, %	Credit/GDP, %	Nonperforming Loans, % of total	EBRD Index
Czech Republic	55 (23)	15.9	46.7	26.6	3.0
Hungary	43 (21)	41.8	22.7	12.1	3.0
Poland	87 (18)	4.2	12.7	23.9	3.0
Slovakia	33 (18)	32.7	26.3	41.3	2.7
Russia	2,297 (21)	<1	8.7	12.3	2.0

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South Eastern Europe (SEE)

	Number of Banks (Foreign Owned Banks)	Asset Share of Foreign Banks, %	Credit/GDP, %	Nonperforming Loans, % of total	EBRD Index
Bulgaria	41 (3)	<1	21.1	12.5	2.0
Croatia	54 (1)	<1	22.9	12.9	2.7
Romania	24 (1)	<1	7.8	37.9	3.0
Serbia	112 (3)	<1	9.2*	12.0	1.0
Slovenia	39 (6)	3.8	27.3	9.3	3.0

Source: *Bonin, Hasan, and □achtel* (2008)

□*otes:* * indicates data for 1996. The number of banks with the number of foreign-owned banks in parentheses is taken from the country tables in EBRD Transition Report, various issues. FOB is the asset share of foreign-owned banks in total banking assets from Barisitz (2007), except for Slovenia. Slovenian data are from Bonin (2004). Credit/GDP is domestic credit to the private sector at year end from Barisitz, except for Slovenia. Slovenian data are from EBRD Transition Report, 2003. Non-performing loans as a percent of total loans at year end from Barisitz, except for Slovenia. Slovenian data are from EBRD Transition Report, 2003. EBRD Index is the EBRD index of reform of banking sector reform from EBRD Transition Report, 2003; it takes values between 1.0 and 4.0+.

Table 2. Banking Sector of Selected Transition Economies in Later Transition, 1999

Central Eastern Europe (CEE) and Russia

	Ownership Asset Shares		Intermediation		EBRD Index
	State-owned	Foreign-owned	Deposits/GDP	Loans/GDP	
Czech Republic	41.2	27.1	66.1	44.6	3.3 (+)
Hungary	7.8	65.3	36.4	24.6	4.0 (+)
Poland	23.9	69.5	35.4	27.1	3.3 (+)
Slovakia	50.7	24.6	57.1	48.4	2.7 (0)
Russia	41.9 (1998)	10.6*	10.2 (2000)	13.1 (2000)	1.7 (-)

South Eastern Europe (SEE)

	Ownership Asset Shares		Intermediation		EBRD Index
	State-owned	Foreign-owned	Deposits/GDP	Loans/GDP	
Bulgaria	50.5	44.7	21.3	10.7	2.7 (+)
Croatia	39.8	39.9	34.0	35.7	3.0 (+)
Romania	50.3	47.8	20.5	10.6	2.7 (-)
Serbia	90.9#	0.5#	9.7	29.6	1.0 (0)
Slovenia	42.2	4.9	32.0##	35.8	3.3 (+)

Source: *Bonin, Hasan, and □achtel (2008)*

*□otes: * indicates share in registered statutory capital. □ indicates data for 2000 and state□owned includes social ownership. □□ indicates data for 2000 and for primary depo□sits only. Ownership is the asset share of state□owned and foreign□owned banks, respectively, in total banking assets from Barisitz, except for Slovenia. Slove□nian data are from EBRD Transition Report, 200□ Deposits of and credit to the private sector at year end are in percents of GDP from Barisitz (200□), except for Slovenia where data for deposits are from Bonin (200□) and data for credits are from EBRD Transition Report, 200□ EBRD Index is the EBRD index of banking sector reform from EBRD Transition Report, 200□□it takes values between 1.0 and □0□. Also, (□) indicates an in□crease in the index from 199□, (0) indicates no change, and (□) indicates a decrease in the index from 199□.*

Table 3. Banking Market Characteristics of Selected Transition Economies in 2005

Central Eastern Europe (CEE) and Russia

	Ownership		Intermediation Ratio to GDP				Concentration		EBRD Index
	State	Foreign	Deposits	Loans	HH loans	Mortgages	3-firm	5-firm	
Czech R.	2.5	94.5	55.9*	27.3*	13.9	7.9	65.4	75.6	4.0 (+)
Hungary	7.0	84.5	40.1	44.8	15.7	11.6	41.9	56.6	4.0 (0)
Poland	21.5	74.2	34.6*	27.4*	12.6	5.1	33.4	45.3	3.7 (+)
Slovakia	1.1	97.3	47.7*	32.5*	13.0	3.6	47.7	66.3	3.7 (+)
Russia	38.1	11.2**	17.7	25.7	4.9	0.2	37.0	41.7	2.7 (+)

South Eastern Europe (SEE)

	Ownership		Intermediation Ratio to GDP				Concentration		EBRD Index
	State	Foreign	Deposits	Loans	HH loans	Mortgages	3-firm	5-firm	
Bulgaria	1.7	72.8	36.0*	34.9*	14.7	4.8	32.8	49.9	3.7 (+)
Croatia	3.4	91.2	59.8*	55.8*	34.3	12.0	55.3	75.3	4.0 (+)
Romania	6.5	59.2	26.1	20.9	7.3	0.6	48.3	59.8	3.0 (+)
Serbia	23.9	66.0	25.1	25.0	7.6	1.4	37.3	53.2	2.7 (+)
Slovenia	12.0	22.6	n/a	56.4	14.5	3.6	50.4	73.3	3.3 (0)

Source: *Bonin, Hasan, and Wachtel (2008)*

*Notes: *indicates data for 200[illegible]. **indicates share in registered statutory capital. Ownership is the asset share of state-owned and foreign-owned banks, respectively, in total banking assets from Barisitz, except for Slovenia. Slovenian data are from EBRD Transition Report, 2006. Deposits of and credit to the private sector at year end are in percents of GDP from Barisitz, except for Slovenia. Slovenian data for deposits are from Bonin (200[illegible]) and data for credits are from EBRD Transition Report, 2006. HH/GDP is the ratio of total outstanding bank credit to households at year end to GDP from EBRD Transition Report, 2006. Mortgage is the ratio of mortgage lending to households at year end to GDP from EBRD Transition Report, 2006. Concentration measures are computed as market shares of the top number of banks indicated and from Barisitz, except for Slovenia. Slovenian data are for 2000 from Bonin (200[illegible]). EBRD Index is the EBRD index of banking sector reform from EBRD Transition Report, 200[illegible]; it takes values between 1.0 and [illegible]. Also, (+) indicates an increase in the index from 1999, (0) indicates no change, and (-) indicates a decrease in the index from 1999.*

Table 4. The main banks with subsidiaries or control packages of shares in the CEE states

Name	The country of origin	Number of CEE states, where the bank has subsidiaries
HYPOVEREINBANK (HVB)* RAIFFEISENBANK (RZB)	Germany-Austria Austria	More than 10
BANCA INTESA ERSTE Bank Citibank Dresdner Bank	Italia Austria USA Germany	From 5 to 10
National Bank of Greece KBC SOCIÉTÉ GÉNÉRALE BANK BNP Paribas	Greece Belgium France France	From 3 to 5

Source: *European Bank for Reconstruction and Development, EBRD Transition Report, various issues; Bank's Annual Report (2006, 200[illegible]).*

* *UNI CREDIT BANK and HVB merged in 200[illegible].*

The research referring to the role of foreign banks in the transition economies is an ongoing process and its origins stem from a relatively recent past. In most studies being realized and referring to the foreign banks entry effects in the transition economies it appeared that such an entry mainly had a positive effect in the less developed countries. However, in some cases opposite effects resulted.
Generally speaking, the countries exert various degrees of control of the foreign banks entry into their financial systems. Foreign banks take a cognizance of those controls in their decisions whether or not to penetrate. This paper's objective is to theoretically expose the arguments for and against the foreign participation in (emerging market) banking systems. The pros (merits) of the foreign banks penetration cause the bank regulatory authorities to ease the restrictions to the foreign banks entry, while the cons (demerits) cause the bank regulatory authorities to tighten the restrictions of the foreign banks entry. The reminder of the paper is organized in the following manner. In section 2 the positive effects are outlined related to the foreign banks entry into the less developed banking systems. In next section the negative effects of the foreign banks penetration into those banking systems is outlined. Section 4 concludes the paper.

1. Positive effects of foreign banks entry into local banking markets

The restrictions of the foreign banks entry in the countries all over the world were considerably lessened following the wave of financial liberalization in the 1990s. The reasons of those restrictions reducing should be searched in the appropriate benefits provided by the foreign banks presence in the scope of a country's banking system. Some authors, as Walter and Gray ( ), Gelb and Sagari (1990) and Levine (1996) researched potential benefits of the foreign banks entry for the domestic economy through a better allocation of resources in its scope and a higher efficiency of this economy's functioning in general. Peek and Rosengren (2000) found out the following benefits from the foreign banks presence in the host country's banking system[2]:

- Improved efficiency of the banking system through transferring technology and know-how and using the effects of scale economies;
- Better integration of the host country's financial market with the international capital markets – enabling a broader approach to international capital;
- Higher degree of diversification of the banking system assets – improving the quality and availability of financial services on the domestic market by increasing the banks competition and applying the modern banking skills and technology;
- Provision of a new source of funds for the troubled banks recapitalization;
- Providing a "safe haven" in a troubled country, getting an opportunity to reduce funds flowing off shore;
- Larger presence of ratings agencies and auditors – through such an improvement of the bank regulation and supervision, and the legal system strengthening in the host country.

First, foreign banks provide an important channel for the foreign capital inflows aimed to finance the host country's economic activities. If foreign funds are a complement and not a substitute of the domestic sources of funds, each inflow contributes to a net expansion of available funds in an economy. Such a net expansion of available funds can be a strong support of the country's economic growth.

Second, the foreign banks penetration can possibly lead to positive spillover effects. First, foreign banks can introduce new financial services. Following the introduction of new services by those banks, the domestic banks will be obliged to develop such (new) services as well, thus improving the efficiency of the domestic financial system's financial intermediation. Besides, foreign banks may introduce modern and more efficient banking techniques, being new to the domestic banks. Such techniques will be imitated and applied by the local banks. The capability to imitate and accept the technology transfer is known as "absorptive capacity". Those countries being able to imitate more and having a more intensive level of local research and development (R&D) receive more high-quality technological FDI.

[2] Also, in their opinion those benefits were responsible for lessening the restrictions of the host country's regulatory authorities to the foreign banks entry into their financial systems.

Foreign banks can assist in advancing the domestic banks management, particularly if a foreign bank directly participates in a domestic bank management (for example in case of a joint-venture or a take-over). These banks can increase the quality of the human capital in the domestic work in their foreign branches, the domestic employees/ bankers get an opportunity to learn from banking system in several ways. First, if foreign banks *import* high-skilled bank managers to skilled managers from the foreign bank. Furthermore, foreign banks can invest in training of domestic employees. Such an increase of the disposable human capital in the domestic banking system contributes to more efficient domestic banking practices, leading to reducing the expenses of functioning of the total banking sector of the country.

The foreign bank penetration into the domestic bank banking system leads to improving the banking regulation and supervision. Namely, foreign banks can ask the regulatory authorities in the host countries to improve the systems of regulation and supervision. Naturally, this may lead to improving the quality of the banking operations in the local banks.

All those spill-over effects can contribute to a more efficient practice of the domestic banking, as well as to reducing overall costs of the banking system's functioning. Still, such cost reduction is possible to be realized only in the long run. In order to introduce new services, advance the quality of existing services and operations and to carry out new bank management techniques, in this initial stage the banks are expected to be burdened by additional costs. The reduction of overall costs of the banking system functioning on the spillover effects basis is expected later.

Third, the foreign banks presence contributes to strengthening competition on the host country's banking market and may stimulate the domestic banks to reduce their business activities costs, to increase their efficiency and improve the quality of their financial services. All those activities should be performed by domestic banks in order to retain their market shares. The competition effect can work in two ways: either domestic banks have high absorptive capacity and become more effective (catch-up effect), or if the technology gap is too high domestic banks are unable to compete with foreign banks and foreign banks will easily increase their market shares (market-stealing effect). The technology transfer and local firms' reaction to foreign banks' entry therefore depend on the development of the financial sector.

The foreign banks penetration into a banking system is negatively associated with net interest margins, and *vice versa*. Namely, by restricting the foreign banks entry the gap is enlarged between interest received and income paid as a fraction of interest earning assets – a situation reflecting a greater competition and efficiency in the banking sector.

Four, foreign ownership of banks is believed to increase the total banking system soundness, particularly when the banks are part of well-regulated financial systems. Namely, foreign banks are expected to provide, through their parent banks, a greater access to capital and liquidity. In a much broader sense, the presence of foreign banks is expected to contribute to strengthening the financial system in the host country by supporting higher standards in auditing, accounting and disclosure, credit risk underwriting, and supervision.

Among the economists it is widely believed that foreign ownership of banks provides a financial stability in times of financial crises as well. Such an attitude was confirmed by empirical research. Demirgüç-Kunt and Detragiache (1998) found out that, ceteris paribus, the presence of foreign banks in a country is associated to a lower probability of the financial crisis eruption in its economic system. Barth et al. (2002) found out that the banking crises and the restrictions for the foreign banks entry to the domestic markets are positively correlated. If an attempt is made towards relieving such restrictions, the possibility of a banking crisis presence will be reduced. Accordingly, the foreign banks penetration can highly improve the financial stability in the host country and reduce the business cycle's volatility.[3] It is particularly the case in the emerging economies and the countries in transition. If the banks are in foreign ownership and able to forestall the shocks of liquidity, due to the support of their highly capitalized parents, it follows that the country with an internationalized banking sector may be

[3] The foreign banks presence in a country contributes to increasing the public (domestic and foreign) confidence in its banking sector.

partially isolated from bank runs. Levy-Yeyati and Micco (2003) believe in such possible achievement independently from the risky behavior level of their foreign-owned bank institutions.

Foreign banks are able to provide larger and much more stable credit flows than their domestic counterparts. However, Jeon et al. (2006) state that foreign banks provide a source of stability only if their operations are less sensitive to the host country's market conditions in relation to the local banking firms.

Goldberg et al. (2000) investigated the lending behavior of foreign and domestic banks in Argentina and Mexico in the mid 1990s. They concluded that foreign banks had a higher loan growth (with smaller volatility of such growth), when compared to all domestic owned banks. They also found out strong similarities in the portfolio composition of lending and regarding the volatility of lending in the privately-owned foreign and domestic banks both in Argentina and Mexico. Goldberg and his associates wanted to point out that the bank's health and not its ownership *per se* is a critical element in the growth and volatility of bank credit.

The broadest research on the efficiency and competitive effects of the foreign banks entry into a country's banking sector was carried out by Claessens and his associates (Claessens et al., 200). After using a large set of data containing accounting information on domestic banks in 80 countries from 1988 to 1995, they found out that a larger presence of foreign banks is related to the reductions in profitability, non-interest income and overall expenses of domestic banks. They concluded that the foreign bank entry increases the efficiency and improves the domestic banks functioning. They did not investigate whether the effects of the foreign bank entry to the domestic banks behavior depends on the host country's economic development level.

The spill-over effects, as explained before, can be more important to the less developed countries, having as a rule less developed financial systems (King and Levine, l993). Accordingly, there could be more room for improving the domestic banking practices when foreign banks enter a given market. Certainly, in the long run a positive influence may be exerted to the domestic banking system's functioning. In the short term, however, costs may increase and these cost increases may be larger the lower the level of economic development.

The pressure of competition on the domestic banks provoked by the foreign banks entry can be weaker in the economically less developed countries with underdeveloped financial systems. Due to a lower development of the domestic financial markets in such countries, foreign banks can be interested of servicing just a part of demand for financial services, as for example export financing, financial leasing, and to serve just some groups of clients, like foreign-owned multinationals, and/or large export-oriented domestic enterprises. Financial services for other groups of clients can be less desirable, possibly due to higher risks and/or high levels of information and transaction costs. Thus the competitive pressure on the domestic banks can be lessened, if such banks are mainly oriented to the second group of clients – i.e. consumer credits, credits to small and medium enterprises, etc. If the competitive pressure is lower, domestic banks are able to impose, in the short run, increased costs to their clients due to spill-over effects. This may even lead to higher margins on financial services (i.e. when interest rates charged are raised more than the increase of the interest rates paid).

2. Negative effects and risks of foreign bank entry into local banking markets

Although the above mentioned arguments may be more or less convincing, there are also arguments against opening up the domestic banking system to foreign banks. The empirical research carried out (in this area) during the last ten years pointed that the foreign banks penetration leads to negative consequences as well. Those are competitive pressures leading to losing the domestic banks' market share and profitability, instability of the domestic deposit base (especially during times of systemic crises)[4] and a reduced domestic financial systems ability to respond to strong internal and external shocks (Cull and Clarke, 1998). A possible reason why the domestic financial instability may be increased is

[4] The foreign banks presence increases the volatility of the domestic financial markets.

that foreign banks are able to transfer their money resources very rapidly from one market to another in accordance to the changes of the perceived risk-adjusted returns on those markets – probably as a result of sudden changes in expectations. The foreign capital channel, provided with foreign banks, contributes to not only the stimulation of the inflow of capital in good times, but also a rapid outflow of foreign capital in case of a financial crisis.[5] Since in the economic environment of a country, foreign banks appear as more solid and more stable institutions compared to domestic ones, they are in the position to attract the "best" domestic clients-borrowers (higher-profit and lower-risk borrowers). Domestic banks are pushed back in a more precarious position of lending to less credit –worthy borrowers. Consequently, the domestic banks pretax profitability on the markets with a high participation of foreign banks is considerably lower than in markets with low foreign banks presence.

The critics of the foreign bank participation in the domestic banking sector pointed to possible risks to the financial system's stability, emphasizing the danger of a more volatile credit supply (Stiglitz, 2002; De Haas and Van Lelyveld, 2006). The host country gets a broader credit supply when foreign banks enter into its banking system. But since those banks are more sensitive to their home country market conditions, their loans may be volatile although there was no change in the host country's macroeconomic conditions.[6]

The thesis that the foreign banks entry may not provide an increased stability of the domestic banking system is supported by many economists, and also by Agénor (2001). The starting point of such an attitude is that the presence of foreign banks in some countries is not contributing, per se, that the systemic banking crises appear weaker when they occur than they really are in practice. If an economy undergoes a deep and prolonged recession, leading to a massive increase rates of default in payment and an increase in nonperforming loans, foreign banks may decide to abandon such an economy. It is quite possible, in Agénor's opinion, that after a while foreign banks suddenly withdraw from a country in case they fail to achieve a sufficient stability and profitability of their operations.

Foreign bank participation could lead to instability of the domestic deposit base, especially during financial crises. During the episodes of financial turmoil, in the behavior of economic subjects usually a phenomenon appears possible to be denoted as *a flight to quality.* Namely, in such a situation the economic subjects rather leave their money surpluses in the deposit in banks being mainly in foreign ownership (thus increasing their deposit potential), than in "purely" domestic ones. The "flight to quality" phenomenon appeared widespread during the Asian financial crisis (7-1998). It was noted that in Korea, Thailand and Indonesia, the economic subjects-depositors largely shifted their free funds from finance companies and small banks towards larger banks, especially towards foreign financial institutions.

Another often heard argument is that foreign banks will not stay "loyal" to the host country during an economic downturn in the sense that they will not provide additional (or possibly less) credit during such hard times. It appears that in such times the foreign banks only provide credit to the large and often foreign owned (multi-national) firms, leaving the bad corporate credit risks as well as the retail market and the related payment services to domestic banks. The empirical experience in different countries during the period of crisis supports the conclusion that in such circumstances there is a greater risk that the foreign banks operations lead to a stronger credit rationing to small firms and a greater concentration in the allocation of credit to larger and stronger ones. In contrast to foreign banks, the domestic ones will be more patriotic and sympathetic to the cause of small firms. If foreign banks do indeed follow the strategy of concentrating their lending operations only to the most creditworthy corporate borrowers, their presence will be less likely to contribute to an overall increase in efficiency in the financial sector.

The entry of foreign banks into a country's banking system can expose the domestic banks to a pressure to merge with the coming up (foreign) banks as to remain competitive on the domestic banking market. Accordingly, due to the process of concentration in the banking sector following mergers and acquisitions of domestic banks, the banks being "too big to fail" may be created in the host country.

[5] However, the empirical proofs for such an outcome are relatively limited.

[6] Those effects level depends on the organisational nature of foreign banks in the host country – whether they are branches or subsidiaries.

The failure of a big bank in any country leads to very unfavorable consequences, seriously endangering the financial market functioning.[7] The creation and operation of the banks – giants, usually brings increased moral hazard problems. In the scope of the banking sector the monopoly powers are created, finally reducing the total efficiency of the sector. Naturally, those potential problems can be relieved (and even eliminated) through strengthening the prudential supervision or by applying strongly controlled mergers of banks in the domestic banking sector.

Conclusion

The financial reforms carried out in the transition countries essentially changed the banking sectors of their economies. The governments of various countries applied different approaches to the reform and the banking systems strengthening. However, it applies also to the results of the process. One of those results is the foreign banks penetration into the domestic financial system. During the last fifteen years foreign banks penetrated into a number of the transition countries (and into the emerging economies in general), but in different levels. Some countries regarded foreign strategic investors in their banking system as a means to quickly improve the quality of financial intermediation, whereas others chose to remain relatively closed to the foreign banks activity. The critics of the foreign bank entry have for instance pointed to the risks for the stability of the local financial system, emphasizing the danger of creating a less stable supply of bank credit. This paper has analyzed the main effects (positive and negative) of the foreign banks entry into the transition banking sector.

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[7] For that reason monetary authorities throughout the world fear of facing such a situation.

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BUSINESS OPERATIONS RISKS AND FINANCIAL POWER*

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Abstract

Risk occurs in any business operation or any other activity. We encounter risk day-in-day-out. In business operations of an enterprise, business and financial risk play the primary role. Risk analysis entails business and financial receipts and expenses, that is financial result from regular business operations. In this analysis business expenses are divided on variable and fixed component. Business risk and business leverage reflect business operations efficiency of an enterprise with fixed expenditures. Any investment of capital bears certain amount of risk, because costs are incurred regardless of the intensity of capital employment. Financial risk and financial leverage reflect risk of achieving gross financial result. Total risk factor or compound leverage is the result of multiplying factor of business risk and factor of financial risk. How high the factor of total risk would be depends on how high the factors of business risk and financial risk are. It means that if an enterprise manages to reduce factors of business and financial risk, it will automatically reduce the factor of total risk. Analysis of financial power entails fixed liabilities calculation and coverage, which most often refers to covering interest, fixed charges and preferential dividend. The wider coverage of these charges is, the greater financial power would be, and vice versa. In this paper risk analysis and financial power are presented through financial reporting of DI Company during the period 200[illegible]-200[illegible]. For the purpose of analysis, apart from absolute numbers, the relative ones have been used, too, for they make the analysis easier.

***Key terms**: business operations, enterprise, business risk, financial risk, total risk, assets, liabilities, coverage spread, financial power.*

1. Business operations risk analysis

Business operations risk analysis entails business and financial receipts and business and financial expenses, financial result from regular business operations. In this analysis business expenses are divided on variable and fixed component, which may cause additional problem. This problem does not occur in companies which calculate costs according to the system of variable costs calculation, because in that case costs have already been divided on variable and fixed ones. If a company uses another way of calculating costs, the starting point is represented by final production costs, divided on variable and fixed component. Proportionally to the amount of variable and fixed costs of final production, expenditures are divided on variable and fixed components in profit and loss account. Such division of production costs on variable and fixed costs can be done using the method of direct (subjective) determining, mathematical methods or graphical methods.

The method which approximates fixed costs best should be used in the analysis. The main criteria for such decision are amortisation costs. There is no doubt that amortisation costs are fixed costs, but fixed costs appear in overhead costs too, so that they have to be higher than amortisation costs. It can be concluded that acceptable methods of dividing costs on variable and fixed ones, are actually those which reject fixed costs above the costs of amortisation and below the sum of costs of amortisation and overhead costs, because overhead costs entail variable component, as well. For the sake of analysis, costs of financing should be singled out from fixed costs and given separately.

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In this analysis, direct (subjective) method has been used regarding division of costs on variable and fixed component, according to which variable expenses entail the following: costs of material, fuel, power, production services and purchase price of goods sold, as well as 40% of gross salaries, while fixed and mostly fixed expenses entail amortisation costs, reservation costs, mainly fixed costs and 60% gross salaries. Apart from these costs, net expenses of financing have been used in the analysis, as a difference between financing expenses and financing returns.

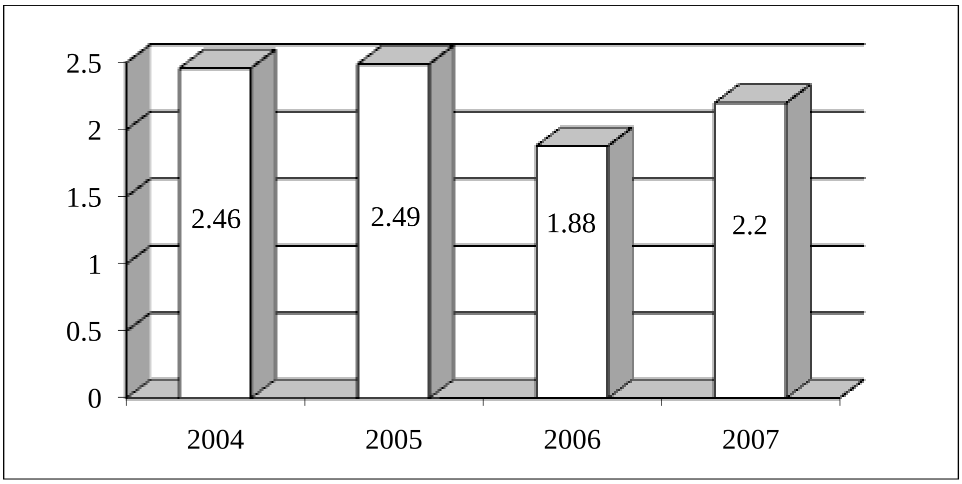
2. Business risk analysis

Business risk, or business leverage, reflects business operations efficiency of a company with fixed business operations expenses. Any investment of capital bears a certain amount of risk, for costs are incurred regardless of the intensity of the capital employment. Such cost is a fixed cost and is incurred when invested means are idle. For example, such costs are amortisation costs as well as fixed costs referring to organisation of a company. These costs are also called period costs. They have to be covered. On the contrary, loss would appear, as a negative difference between the coverage spread and period costs.

Business risk factor is calculated as the ratio between coverage spread and business result. It shows how fast the business result changes in comparison to coverage spread. For example, if the factor of business risk is 3, any change in coverage spread from 10% will cause the change in business result by 30%. It can be concluded that lower factor of business risk is more acceptable for the company, because it is less possible to reduce business result below the level which may lead to negative gross result, that is entering loss zone. Thus, the enterprise should encourage factors which reduce business risk, and these entail the following:

- Amount of selling price - the bigger selling price is, the bigger coverage spread would be, thus reducing the business risk factor,
- Scope of production and sale – the bigger it is, the higher coverage spread would be, thus reducing the business risk factor,
- Direct material usage, power usage, services and direct labour usage per a product unit – the lesser this usage is, the lesser variable costs are; coverage spread is higher thus reducing the business risk factor,
- The amount invested in capital assets – the smaller amount the enterprise invests in capital assets, the lesser fixed expenses on amortisation would be, thus improving business results and reducing the business factor risk, and
- The amount of other fixed costs – similar to the above, the lower these costs are, the better business result the company achieves, thus reducing the business risk factor.

Figure 1.Business risk factor



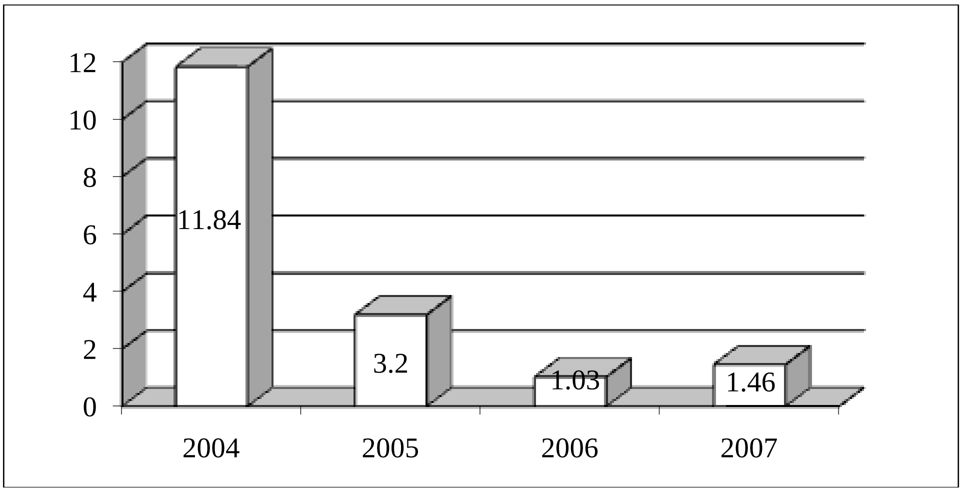
The enterprise had negative business result in the first year, so business risk is not calculated. During the following years, situation is improved and the data shows that the enterprise has a good position due to low business risk factors.

3. Financial risk analysis

Financial risk or financial leverage is a risk of achieving gross financial result, by which gross financial result is a difference between business result and net expenditures of financing. Factor of financial risk is calculated as the ratio of business result and gross financial result (financial result from regular business operations) and shows how fast gross financial results change with any change of percentage in business result.

For example, if factor of business risk is 2, reducing business result by 12%, gross financial result would decrease by 24%. Any company tends to eliminate the influence of financial risk on achieving gross financial result. It is only possible if the company is fully financed from its own sources. Then, companies do not incur costs of financing and business result equals gross financial result. Since borrowed sources of financing which incur financing costs can hardly be avoided in practice, companies try to reduce business risk factors in various ways. Risk can be reduced by increasing business gain. According to that, it can be concluded that the amount of financial risk depends on the amount of business result on one hand, and the amount of net expenditures of financing on the other.

Figure 2.Financial risk factor



The level of business result and factors which may influence business risk were analysed in the previous section, while the amount of net expenditures of financing depends on the following:

- Amount of borrowed sources of financing on which interest is charged – the lower the amount of their own capital and spontaneous sources is, the higher amount of borrowed sources would be, thus increasing expenditures based on financing, as well as the factor of financial risk.
- Interest rate – the higher interest rate, the bigger expenditures of financing, as well as the factor of financial risk
- Amount invested in assets – the bigger this amount is, the higher amount of borrowed sources on which interest is charged would be
- Amounts placed as financial and commodity loans – the higher amounts of money are placed, the bigger financing returns would be, while net expenditures of financing would decrease thus reducing the factor of financial risk
- Amounts of interest rate on amounts placed – higher interest rate ensures higher returns from financing and lower net expenditures of financing.

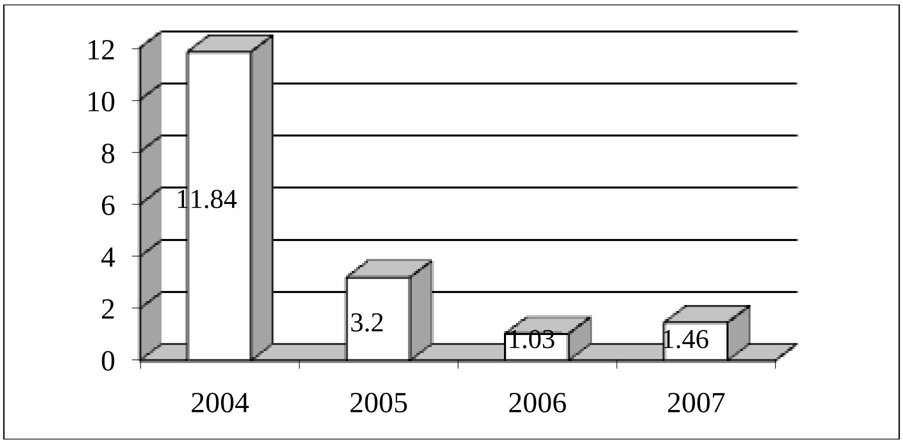
In 2003 the company achieved negative business result as well as negative result from regular business operations, so the factor of financial risk is not calculated. In the following years the company achieved positive gross financial result and reached the most favourable position in 2006 when the factor of business risk amounted to 1.03, due to low net expenditures of financing (Figure 2). The unfavourable situation occurred in 2004 when the factor of financial risk amounted to 11.84, which means that the reduction of business result by 10% would cause decrease of gross financial result by 118.4%. Figure 2 clearly shows the tendency of the decline in financial risk. In 2007 there was a slight increase and the factor of financial risk amounted to 1.46.

4. Total risk analysis

Total risk factor or compound leverage is calculated by multiplying factor of business risk and factor of financial risk, and it can be expressed as a ratio between the coverage spread and gross financial result. It shows how fast gross financial result changes with any change in coverage spread. As it is the case with other factors, the factor of total risk should be lower, so as to reduce the risk of the achieved results. At the same time, the amount of total risk factor depends on the amount of f business risk factor and the amount of financial risk factor. It means that if the company manages to reduce the factors of business and financial risk, it will automatically reduce the factor of total risk. Complexity of this risk originates from its dependence on these two factors.

However, if the company is capitally intensive, it means that it has huge investments in capital assets, so it cannot reduce high fixed expenditures based on amortisation. That increases the factor of business risk, thus increasing factor of total risk. Resolution of this problem can be found in moving the liabilities structure in favour of the company's own capital, so there would be no need for borrowing money. Expenses of financing would reduce, thus reducing the factor of financial risk as well. With the given amount of business risk, the total risk factor would be lower.

Figure Financial risk factor



If we look into the first year of the analysed period when the company achieved negative business and gross financial result, the data show that the company, from the point of view of total risk, was under favourable condition in 2006 when the factor amounted to 1.93. The unfavourable conditions occurred in 2004 when it amounted to 29.10 (Figure 3). Apart from that, the factor of total risk was in a constant decline during the period, except for the year 2007 when there was an increase in comparison with the year 2006 which was caused by the rise in factors of business and financial risk during the same year.

5. Break-even point analysis

Break-even point is the point in which returns are equal to expenses, that is the point in which financial result is neutral and equal to null. In the analysis of the observed enterprise, there were two break-even points: the point of neutral business financial result and the point of neutral gross financial result.

6. Point of neutral business financial result

The point of neutral business financial result is the point in which business returns are equal to fixed and mostly fixed expenses and a part of variable costs which is entailed in returns which ensure neutral business result. Business returns required for neutral business result in relation to achieved business returns multiplied by one hundred, give percentage of business returns used for achievement of neutral business result. At the same time, if positive business result is achieved, percentage of using business returns for achieving neutral business result would be lower than 100%. The farther from 100 that per cent is, the more favourable situation in the company we have, because the risk of achieving business result is lower, and vice versa. The analysis would be completed by introducing the elasticity rate in achieving neutral business result which is calculated in the following way:

$$\text{Rate of elasticity in achieving neutral business result} = \frac{\text{Business returns} - \text{Business returns required for achieving neutral business result}}{\text{Business returns}} \times 100$$

The rate shows how much business returns can be reduced, so that business result falls to null. The higher rate we have, the less probable it is that the company would suffer business loss. If the company achieves negative business result, the rate would be negative and would show how much achieved business returns are lower in per cent than business return which rejects neutral business result. The higher negative elasticity rate is, the deeper into loss zone the company goes, and vice versa.

In the first year of the analysed period, the company achieved negative business result, so the percentage of using business returns for achieving neutral business result in that year only, amounted to more than 100%. Elasticity rate of neutral business result in that year is negative and shows that achieved business returns are lower than business returns required for neutral business result by 19.39%. The company was in the most favourable situation in 2006 when the percentage of using business returns for achieving neutral business result amounted to 46.89% and elasticity rate amounted to 53.11%. In the remaining years of the analysed period, percentage of using business returns fluctuated slightly.

7. Point of neutral gross financial result

That is the point in which business returns are equal to fixed and mostly fixed expenses, net expenses of financing and a part of variable costs which is entailed in returns which ensure neutral gross financial result. In order to get percentage of using business returns for achieving neutral gross financial result, it is necessary to put business returns required for achieving gross financial result into relation with the achieved business returns and multiply that by 100. If positive gross financial result is achieved, the percentage of using business returns for achieving neutral gross financial result would always be lower than 100. The situation is more favourable if that percentage is far from 100, because in that case the risk of achieving neutral business result is lower. Along with the elasticity rate of achieving neutral business result, the elasticity rate in achieving gross financial result shows how many times business returns can be reduced so as to bring gross financial result to null. The higher elasticity rate is, the less probable it is that the company would achieve negative gross financial result, and vice versa.

During the course of the year 2003, the company achieved negative result from regular business operations, so per cent of using business returns for neutral gross financial result is by 28.22% above 100%, which indicates negative elasticity rate. In the following years, situation was improved. Percentage of using business returns for achieving neutral gross financial result declined and in 2006 it amounted to 48.23%. It was then that the company was in the best position, which is indicated by the elasticity rate of gross financial result which amounted to 51.77%. In the following year there was a slight decrease in the elasticity rate, 31.06%, that is the increase in percentage of using business returns for neutral gross financial result which amounted to 68.94%.

8. Financial power analysis

Financial power analysis refers to determining coverage of fixed liabilities, which mostly refers to coverage of interest rate cost, fixed costs and preferential dividend.

***Covering interest rates costs**,* that is costs of financing is calculated as the ratio between business gain and interest rates costs. Business gain is the difference between returns and sum of variable and fixed expenses, excluding costs of financing. The ratio shows how many times business gain is higher than the costs form interest rates. The bigger this ratio is, the higher coverage of interest rates would be along with the financial power, and vice versa. Given formula clearly shows that covering of interest rates costs depends on two variables: amount of business gain and amount of interest rate costs. In the analysis of business risk it was obvious that the amount of business gain depends on the coverage spread, which is connected with the parity of sale and purchase prices, productivity, scope of production and sale, amount of fixed and mostly fixed expenses without expenses from financing, etc. On the other hand, the amount of interest rates costs depends on the ratio of the total amount of debt and total assets as well as on how high interest rates are. With given interest rates, balance power would be bigger if the ratio between total debt and total assets is lower, because in that case the costs of interest rates would be lower, and their covering greater. Greater covering is a guarantee that the company will pay interest. It also brings bigger gross yield on the total result. Covering of interest rates costs is given in the following table:

Table 1. Interest rates costs covering
(in thousand dinars)

No	Position/year	2004	2005	2006	2007
1	Business gain	10529	16269	23365	28622
2	Interest rates costs	3865	6101	6797	7171
3	**Covering of interest rates costs (1/2)**	2,72	2,67	3,44	3,99

For the year 2003 covering of interest rates costs is not calculated, for as we know, the company achieved negative business result in that year. In the following years, the data indicate the guarantee that the company would pay interest. The best situation was in 2007 when covering was 3.99 which means that the situation improved year-in-year-out.

Covering fixed expenses is calculated as the ratio between business gain increased by the lease costs and fixed expenses which entail costs of interest rates, due principal of the long-term debt and lease costs, assuming that tax on financial result is not included in fixed liabilities. This result shows how many times business gain enlarged by adding lease costs. It is bigger than fixed liabilities. If that ratio is bigger, the financial power is bigger, too. The ratio is determined by two variables: the amount of business gain increased by lease costs and amount of fixed expenses (interest rates costs, due principals of long-term debts and lease costs).

The amount of due principal from long-term debt depends on the ratio between long-term debt and total capital, and the amount of lease cost depends on whether the enterprise uses leased business premises and equipment and how much it pays for the lease. If presented pattern for covering fixed expenditures included tax on financial result and if that result was 1 and more than 1, due principal of the long-term debt would be substituted by using the company's own capital, provided that in the division of net gain it would accumulate for their own capital at least the amount of the due principal of the long-term debt. Due to the lack of necessary data, covering of fixed expenses will not be calculated in this paper.

Covering preferential dividend. That is liability of the company towards the holders of preferential shares whom fixed dividend belongs to. The ratio between business gain, enlarged for the amount of lease costs and fixed expenses and fixed dividend enlarged for the tax on financial result makes a basis for calculation of preferential dividend covering. Having been included in tax base in calculating tax from financial result, the fixed dividend is increased by the amount of tax on financial result. Preferential dividend is determined on the basis of accounting data which refer to nominal value of preferential shares and fixed dividend rate.

However, having in mind that preferential dividend is not the only fixed liability of the company, denominator has to include other fixed liabilities as well. Based on that relation, it is possible to understand how many times business gain enlarged for the lease costs is higher than the interest rates costs, lease costs, due principal of the long-term debt and preferential dividend enlarged for the amount of tax on financial result. The bigger this ratio is, the higher financial power would be, and vice versa. Having in mind that the included tax on financial result represents a part of tax, covering of total fixed expenses should be determined in order to provide covering of the remaining part of tax on financial result. Denominator includes total tax on financial result, so the preferential dividend is enlarged by the tax on financial result which belongs to it. The company provides covering of fixed expenses if the result of this ratio is 1 or more than 1. If the result is more than 1, the covering is bigger, thus increasing the financial power for paying total fixed liabilities and vice versa. The company is registered as a limited liability company and has no liability based on fixed dividend.

Conclusion

All procedures necessary for achieving the aim of this analysis have been undertaken, that is assessing risk of business operations and financial power of the company. All applied procedures improved information transfer and benefits of the disposable information, which were used to make deeper insight into risks and financial power of the company in the observed period. The following conclusions speak in favour of that:

Having analysed business operations risk and breakeven point, the following indicators were identified: business risk factor, financial risk factor, total risk factor, point of neutral business result and the point of neutral gross financial result. Risks were not assessed in the first year for negative business result was achieved. The company was in the most favourable position in 2006 when the business risk factor amounted to 1.88 which means that any change in the coverage spread by 10% would bring about changes in the business result by 18.8%. In 2005 business risk factor was 2.49 and it was then that the company was in the least favourable position. As for the financial risk, the best situation was in 2006, too, when it amounted to 1.03, due to low expenses of financing. During the first years of the observed period, the company encountered high financial risk, but it was evident that the situation got improved and had a declining tendency. Total risk factor as a result of multiplying business and financial risk factor has the same tendency as the previously described two factors. As for the neutral business result, the company was in the least favourable situation in 2003. Then the company achieved negative business result and percentage of using business result for realisation of neutral business result surpassed 100%. The best situation was in 2006 when percentage of using business result for realisation of neutral business result was the lowest, while the elasticity rate was the highest, which reduced the risk of entering the loss zone. The same situation is evident in the analysis of neutral gross result. The best situation was experienced in 2006 when the elasticity rate was 51.77%. That means that the gain can be reduced for that amount so as to reduce gross result to null.

Analysing financial power from the point of view of covering expenses, it is evident that the company will pay interest, with the exclusion of the first year when the company suffered business loss. The best situation was in 2007 when the business result was proportionally increased in comparison to the increase of interest rates costs. Covering of fixed charges and preferential dividend were not calculated due to the lack of necessary data, that is due principal of long-term debts and the company is not obliged on dividend for it is not a joint stock company.

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FINANCING SMEs IN SERBIA[*]

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Abstract

The sector of small and medium□sized enterprises (SME) has an extremely important role for the Serbian economic development. This sector accounts for 99.□□ of business entities, and it accounts for 2□□of over□all employed population, generates over 2□□ of aggregate profits, and over □0□ of exports and 60□ of imports of the Serbian economy. Further development of this sector greatly depends on the support which entrepreneurs and small and medium□sized enterprises get from the financial sector. Although Serbian financial sector has been noticeable improved in several last years, where the most significant development has been within banking sector, the necessary support for the SMEs is still on the law level. The commer□cial bank loans are very expensive and unaffordable for the majority of interested entities. The financial support for the SMEs provided by the state agencies and organizations has increased in the past period, but still do not meet all the needs of the SME sector. How an entrepreneur or small and medium□sized en□terprise could get financial source and what is its price, is the issue examined within this paper.

Key words: *SME sector, financing sector, state financial support, Serbia*

Introduction

Small and medium-sized enterprises are extremely important for European economies where they have a dominant position. From a total number of about twenty millions enterprises in European Union in 2007, 99% were small and medium-sized. Furthermore, SME participated in about 60% of GDP and employed approximately two third of the total number of employees in the EU private sector[4]. In order to create a favorable business environment and to improve the competitiveness in SME sector, the EU countries adopted a number of regulation and stimulation measures, which are based on principles defined in Small Business Act for Europe[5].

The majority of transitional economies, understanding the importance of SME's and streaming to join the EU, have formulated their national SME development policies and created the programs and strategies for this sector. The transition countries pay significant attention to SMEs, since the development of this sector is highly important for the success of the overall economic reforms directed to market economy creation. In fact, the comparative advantage of SME is its flexibility, its fast adaptation to changes and they are also appropriate for satisfying the fluctuate market demands. Additionally, the low fixed costs present important baseline and comparative advantage of these enterprises. Simultaneously, the great number of these firms is characterized by innovativeness, entrepreneurship initiative and creativity, which is of remarkable significance for the accelerating technological development. And last, but not the least, the SME sector is indispensable for the new job vacancies creation (which is of considerate importance for Serbia that has approximately 18% unemployment rate).

The importance of SME development is highly respected in Serbia, as well as. In comparison to international standards, as well as in comparison to the institutional framework in some neighborhood countries, the overall economic environment and institutional framework for SME support in Serbia is not developed enough. Namely, the SME sector in Serbia is facing the massive challenges in their

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[4] "Statistics in focus", EUROSTAT 31/2008, 2008

[5] "A Small Business Act" for Europe June 2008

activities, including[6]: the lack of financial recourses, legislation (low regulations), and market information, then harmonized standards, information on technologies, human capital, etc.

One of the key issues and limitations for faster SME development in Serbia are the lack of financial resources and the adequate support from the financial institutions. Concerning the mentioned facts and based on empirical data and comparative analyses, our research is focused on the relation between SME and financial sector in Serbia, that is, the analyses of fundamental obstacles and guidelines for enhancing the interaction between the SME and financial sector.

1. SME sector development in Serbia

SME sector is becoming more and more important for Serbian economy. The reinforcement of SME sector role in the period 2001-2008 is, at the first place, the result of general business environment improvement and enhancement measures undertaken by the all administration levels. Accordingly, the development of the SME sector in Serbia has favorable trends, regarding the growing number of this enterprises, the number of employees, the overall turnover, and, finally, the profitability level.

The SME sector in Serbia is participating with 99.8% in the total number of enterprises, 65% in employment, over 2/3 of total turnover, over 36% in GDP creation, about 60% of BDV, and over 50% of export, while the small and medium enterprises are the most profitable segment of Serbian economy in the recent years. The importance of this sector in moderating the unemployment rate (the result of great industrial systems' restructuring and privatization process), as well as the implementation of structural reforms through increase of private sector contribution in GDP creation, regarding the fact that practically all the Sims's are private ownership should be underlined.

The SME development in Serbia (and in the other Western Balkans countries)[7] show that there has been a significant improvement in business environment and SME development in the county since 2000. Serbia has adopted the SME development policy whichis in accordance with the EU policies and it is activly engaged on improvemnt of the macroeconomic measures in order to foster the further SME development.

Macroeconomic stability, the reforms in judical system, tax system, customs system, as well as in the procedures regarding starting a business are evaluated to have a positive impact on business environment. It is reported that the most significant changes are made in the procedures related to starting a business, getting credits (through guarantee fund establishment, sturt-up support, exports and innovations), also by organizing different agencies on national and regional level the small and midium-sized business is being facilitated. Furthermore, the improvement has been made concerning investitors' protections by adoption of new law on bankruptcy proceedings. On the other hand, there are still missing the improvements in the field of entrepreneurship education, e-business, cluster establishment, access to foreign markets, as well as in the administrative regulation and institutional infrastructure.

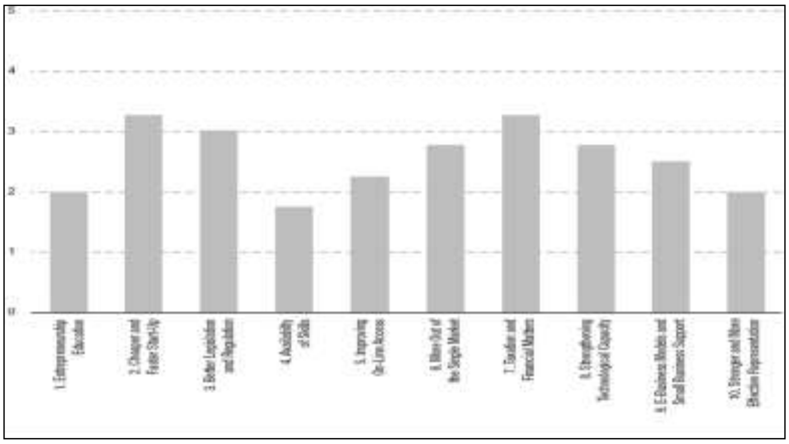
Serbian SME policy index for 10 policy dimensions has the value of 2 and 3 (according to the data for 2007), which indicates that Serbia is on the half of its way towards a well structored system of SME incentives neseccasry for EU accession in comparison to the other Western Balkans countries[8].

[6] "Strategy for development of competitive and innovative SMEs in the period 2008-2013", 2008

[7] Igor Brkanovic, Milan Lalovic, Aleksandar Lakic, Srdjan Tilger, "Study on Micro-finance Support to Start-up in Serbia", International Labour Organization, Belgrade, 2007

[8] "Report on the Implementation of the European Charter for Small Enterprises in the Western Balkans" – OECD, EU, 2007

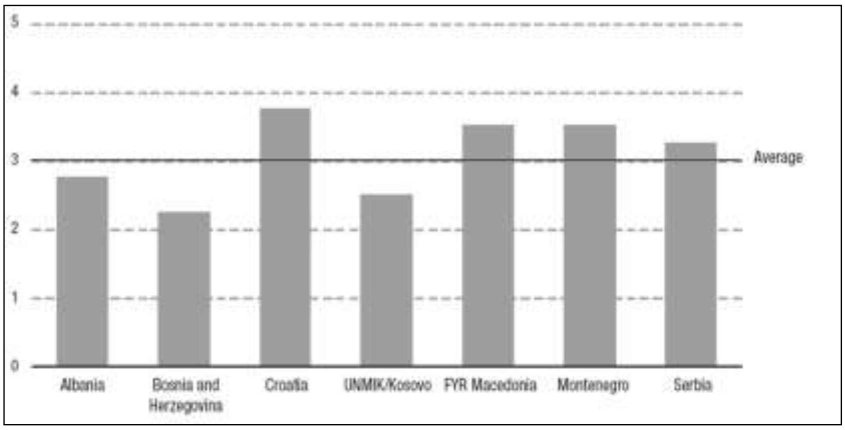
Graph.1. SME policy index for Serbia based on EU and OECD data



Source*: "Report on the Implementation of the European Charter for Small Enterprises in the □estern Balkans" – OECD, EU, 200□*

Serbia is evaluated favourable concerning faster and not so expensive business estblishment, legislative improvements, SME taxation and financing and also technological capacity building. However, Serbia is lacking behind the other Western Balkans countries concerning entrepreneurship education and training, e-business, skills and knowledge necessary for SME development, SMEsupport within the public sector.

Graph 2. SME policy index for □estern Balkan for taxation and provision of finance based on EU and OECD data



SOURCE: *"REPORT O□ THE IMPLEME□TATIO□ OF THE EUROPEA□ CHARTER FOR SMALL E□□TERPRISES I□ THE □ESTER□ BALKA□S" – OECD, EU, 200□*

In spite that Serbia is well ranked in comparison with other Western Balkans countries in the pillar of taxation and provision of finance, the numerous changes in relation between banking sector and SMEs should be made.

2. Basic indicators of the banking sector development in Serbia

Financial sector of the Republic of Serbia comprises of a number of different financial institutions, dominant are, understandably, banks (with 90% of the total balance amount of the financial sector in 2008.), while non-banking institutions, like insurance, leasing companies, and voluntary pension and investment funds take significantly lower share.

The size and structure of Serbian financial sector since the beginning of intensive transitional changes (generally spoken, since the beginning of 2001.) has been constantly changing, in a first place by influence of restructuring and privatisation process in banking and insurance sector, together with institutional infrastructure reshaping which allowed the business activities not presented in the former Serbian financial system (including investment funds, voluntary pension funds and leasing companies) [7]. The changes in the number of business entities comprising Serbian financial sector is presented in the following table 1.

Table 1. Structure of the financial sector in Serbia in 2000-2008 period (number of business entities)

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Banks	86	49	50	47	43	40	37	35	34
Insurance companies	35	n/a	n/a	40	40	19	17	20	22
Leasing companies	-	-	-	10	12	13	15	17	17
Voluntary pension funds	-	-	-	-	-	-	1	7	9
Investment funds	-	-	-	-	-	-	-	10	12

The biggest, and for SME's activities the most important, part of Serbian financial sector in general, is banking sector. The massive restructuring were successfully implemented within this sector during the passed period. Changes in the number of banks, their ownership structure and the participation of determined categories in total balance sum of Serbian banking sector could be represented by the following table[9].

a . an s o n rs s r r and an n s or n r a a an s s ar n e-riod 2002-30.09.2008.

End of period	No. of banks	State owned banks		Privately owned banks			
				Private dom. banks		Foreign banks	
		No.	Share ( )	No.	Share ( )	No.	Share ( )
2002	50	23	49.4	15	23.6	12	27.0
2003	47	17	46.7	19	30.4	11	22.9
2004	43	14	36.1	18	26.2	11	37.7
2005	41	11	26.1	12	10.6	18	63.3
2006	37	8	14.9	7	6.5	22	78.6
2007	35	8	15.7	6	8.8	21	75.5
2008	34	8	15.5	6	9.4	21	75.5

EBRD has declared that Serbia made the obvious progress in banks' reforming (Table), creating the prerequisites for establishment of stable and efficient financial system. However, although it has made a significant improvement since 2001, and also has the key performances on the region average, Serbian banking sector is still in delay in comparison to the Croatian, which is the region leader.

Table 3. Transitional indicators of banking sector restructuring and interest rate liberalization

	2001	2002	2003	2004	2005	2006	2007	2008
Albania	2.33	2.33	2.33	2.33	2.67	2.67	2.67	2.67
Bosnia and Herzegovina	2.33	2.33	2.33	2.33	2.67	2.67	2.67	2.67
Croatia	3.33	3.33	3.67	3.67	4.00	4.00	4.00	4.00
Montenegro	1.67	1.67	2.00	2.00	2.33	2.33	2.67	2.67
Serbia	1.00	2.33	2.33	2.33	2.67	2.67	2.67	3.00

[9] "Doing business 2009", World Bank

3. System of financial support to SME sector in Serbia

The finance resources' provision under favorable conditions is of a key importance for SMEs. Due to that fact, the relations between SMEs and financial sector improvement is crucial for current business operations and SME further development. Thus, it requires special attention.

A relatively wide system for financial support to SMEs has been formed in Serbia, which, first of all, entails commercial banks services (from their own sources or through credit lines from abroad) and support provided by public (state) sector, as well as leasing companies. Besides, there is a considerable number of organizations doing business in Serbia (from international organizations, non-profit and humanitarian organizations of the civil sector to private entities) which are a part of the support to SMEs offering various forms of assistance in financing or providing direct access to particular sources of financing. At the same time, unlike other countries in transition, offer by micro credit organizations as well as the role of private investment funds in SMEs funding is limited.

In the banking sector of Serbia, during the last few years, there has been an increase in loans granted to SME sector. Majority of banks formed divisions for small and micro enterprises and created bank products to suit the needs of these economic entities. Some banks offer technical support to SMEs in the process of filling in loan applications and bank risk assessment. Apart from that, good territorial coverage has been provided by the banks which provide easier access to loans by SMEs from almost all parts of the country.

Unfortunately, regardless of the increase in the offer of banking sector, the conditions for loan making are still not favorable, especially from the point of view of the capital price, collaterals (which amount up to 200% from the loan requirement) and complicated and expensive procedures (whose realization is difficult due to the lack of a unique system of cadastre in the whole country) and different methodologies in submitting loan applications.

Possibilities of SMEs to access bank sources have still been unfavorable if compared to big enterprises. That, however, refers to effective interest rates as well as loan approving procedures. Access to sources of financing is still limited to this sector.

Table 4. Weighted average 12 months interest rates and interest rate spread 2000-2008, (as)

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Active interest rate	77.90	32.52	19.16	14.81	14.59	14.41	15.88	11.13	18.11
Passive interest rate	6.31	4.08	2.62	2.74	3.60	3.71	5.06	4.08	7.32
Interest rate spread	71.59	28.44	16.54	12.07	10.99	10.70	10.82	7.05	10.79

The biggest problem lies in high interest rates on loans granted by commercial banks, which are relatively high in Serbia. High interest rates on loans granted by commercial banks are caused by the Central bank's policy, level of credit risk of the country (BB-), but also by overall situation on bank's products market in Serbia.

These circumstances have led to the strengthening of the financial leasing. During the last few years Serbia has made a big step forward in the field of financial leasing, and became the leader in the West Balkans region. According to the research made by OECD and EU on SMEs development in Serbia and other countries of the Western Balkans region [8], the sector of leasing operations got the best score in Serbia. Financing through leasing brings about several advantages to SMEs, starting from a simpler procedure, possibility of financing up to 100% of the value of the object of leasing, tax treatment of the leasing (which are considered to be operational costs) as well as payments made according to the inflow of finances and servicing of the equipment.

Understanding, on the one hand, the importance and the role of SMEs in economic development and the need for more favorable conditions in financing on the other, the state support to SMEs sector becomes more versatile. The Republic of Serbia has developed an ever increasing system of financial support to this sector under much favorable conditions in relation to market conditions provided by the banks.

The Fund for development of the Republic of Serbia, National service for employment and the Guarantee Fund have a special role in facilitating the access of SMEs to the sources of financing. These institutions enable SMEs to get subsidies. Such loans are often below the level of inflation, which makes them extremely favorable (e.g. Fund for development of the Republic of Serbia provides long-term loans (5 years) with one year grace period and interest rate of 3% per annum). During the last few years special attention has been paid to «start-up» loans (through the National service for employment) which commercial banks are not interested in because of borrowing power and collateral.

Moreover, the government of the Republic of Serbia tries to provide access to international credit lines through mediation or initiation of direct contracts between domestic banks and foreign financial institutions (European Agency for Reconstruction, European Investment Bank, German development bank KfW, Italian Mondimpresa, etc) in order to enable SMEs to take more favorable loans, as well as get incentives by foreign governments.

Apart from that, through the network of regional agencies for development of SMEs, the state assists in providing information to entrepreneurs on credit conditions and helps in evaluating entrepreneurs' ideas. It also provides training for business plan development (financial management) and offers assistance in filling in loan applications.

However, there are numerous problems in offering help to the SMEs financing by the public sector. Survey showed[10] that loans which are offered by the public institutions are not available through the whole year, but temporarily in accordance to annual plans of these institutions. Administrative procedures in terms of applying for a loan are complicated for SMEs and greatly centralized (with low or no influence of local institutions in decision making process). Apart from the National service for employment which has a wide network of branches and affiliations all over the country, other institutions are mainly located in the borrower's place of residence. Consultancy services are not of a high quality, and they often refer to application procedure only. Due to centralized procedure, costs are disproportion ally high.

Funds available to SMEs through non-profit organizations are fairly limited and far below demanded. What makes loans granted by such organizations attractive is the habit of these organizations to visit clients in the place of their residence and create loans which directly suit the client's needs. Also, consultancy services are of a better quality. Although the prices of the loans are relatively high, they are much lower than those provided by commercial banks.

Concluding remarks

For further SMEs sector improvement, it is necessary to create more favorable business environment in which the improvement of relations between banking and SMEs sector would be of a key importance. Still, finances have been one of the main issues and needs regarding the SMEs sector. In order to solve financial problems of the SMEs, it is necessary to strengthen and improve partnership between SMEs and financial institutions including financial institutions through which the state stimulates development of this sector.

Establishing partnership between SMEs and banking sector entails improvement of business and investment climate, development of appropriate financial products (especially increasing offer of banking products in terms of providing access to mid-term and long-term sources of financing) as well as introduction of new mechanisms of financial support to SMEs by the state (particularly in access to "start-up" loans, female entrepreneurship funding, etc), incentives to the system of micro financing and improvement of tax incentives and simplification of tax policy. This entails implementation of

[10] Igor Brkanovic, Milan Lalovic, Aleksandar Lakic, Srdjan Tilger, "Study on Micro-finance Support to Start-up in Serbia", International Labour Organization, Belgrade, 2007

legal and other normative activities in order to create appropriate institutional environment harmonized with the EU, as well as to strengthen institutional capacities for support to SMEs.

At the same time, it is necessary to strengthen internal capacities of SMEs through knowledge improvement on finances and financial management. It is necessary to raise awareness on the importance of financing from the equity capital, as well as development of business incubators and clusters.

During the last few years Serbia has made a significant step forward in developing functional frameworks for support to SMEs. Despite the existence of such framework, support has not been coherent and integrated and it is not adequately financed. Significant efforts should be made towards improvement of partnership between SMEs and financial sector. Along with that, it is necessary to develop better coordination between financial and non-financial support to SMEs, especially for the newly established enterprises.

Limited financial potentials of the public sector and unfavorable loan conditions remain key problems of SME financing in Serbia. Due to that, many SMEs are directed to internal (often very limited) sources of financing, and many entrepreneur ideas remain undeveloped. Strengthening of competition on the financial market should enable development of credit activities towards SMEs sector, both from the banking sector and other financial institutions, with reduction of prices and improvement of capital maturity. Unfortunately, negative effects of the world economic crisis do not contribute to resolution of these issues, because state funds intended for financing of SMEs (due to reductions in budget) are becoming scarce, and banks are becoming more cautious in terms of SMEs financing, which creates unfavorable conditions for creation of new SMEs and their existence on the market.

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INSURANCE MARKET VOLATILITY: CASE OF SEBIA[*]

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Abstract

This paper presents empirical analysis of volatility for insurance sector in Serbia. Generally speaking, the Serbian insurance sector is very small, undeveloped and also in the state of transition, regarding period observed in analysis (from 200□to 2009). In this analysis we applied univariate GARCH models on daily data for two stocks listed at the Belgrade Stock Exchange (www.belex.rs), Dunav Insurance Company (D□OS), and Globos Insurance Company (GLOS). □e examine volatilities of these insurance companies stocks over time. However, we found that volatility of insurance companies stocks in Serbia is infinite. In general, results of our analysis confirm that Serbia is a country with relatively low per capita income and very high volatility (risk), especially in insurance sector.

Key words: *insurance, volatility, conditional standard deviation, GARCH model.*

1. Introduction

The Serbian insurance sector is small, a fact evident from regional as well as a global comparison, and highlighted by the movement of larger firms from neighbouring countries (Croatia, Slovenia) in the Serbian market. The Serbian insurance sector is likely to remain small for the short to medium term. While many insurance companies are highlighting their ventures into emerging markets such as those in Central and Eastern Europe, these ventures are generally on a small scale, and it is the view of some that Eastern European insurance markets are not likely to experience substantial growth in the short to medium term [14].

Given the underdevelopment of insurance in Serbia, a country with relatively low per capita incomes, it is unsurprising to find the dominance of non-life segment lines, and in particular motor insurance, and compulsory insurances, such as general and Compulsory Third Party Motor Liability (CTPML) business in particular [14]. The National Bank of Serbia (NBS) is concerned at recent global financial events, and noted recently that: “Insurance companies in Serbia must be prepared to respond to the arising challenges, given the cohesive nature of the world economy and possibility of the spillover of effects in terms of rise in the price of capital, fluctuations in exchange rates of major currencies and poor performance in the securities market”. In early 2007 the life segment and the new Voluntary Pension Funds in particular, was the focus of a lot of media comment and excitement. Unlike the non-life segment, and the insurance sector as a whole, the life segment is dominated by foreign owned insurers. DDOR Novi Sad and Dunav Insurance Company, the state owned group that is the largest insurer overall, account for less than 20% of life premiums. The life segment remains tiny. The net asset value of the Voluntary Pension Funds is still less than US $20 mn. Seven companies have been granted licences to manage the new Voluntary Pension Funds [14]. Over the long term, the insurance sector should be a significant beneficiary of Serbia’s ultimate membership of the World Trade Organization (WTO) and the EU [14].

The development of insurance market itself enables us to conclude that this fact is becoming progressively important, because in today’s high-risk market circumstances, the insurer needs to determine the adequate price to its product, in order to secure financial stability, and at the same time, keep its

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clients' trust. Therefore, it would be impossible talking about contemporary insurance without its established technical organization. This is, at the same time, the premise of modern insurance, and is based on existing and applying statistic and econometrics methods [9].

Statistics is one of the main elements of insurance. It represents the core means which help the insurance organization determine the amount of its obligation towards the client. The level of accuracy of determined obligations depends on the scope and reliability of statistic data, as well as applied methods for their processing. When the risk statistics are created, it is required to observe homogeneity risks (according to their size and nature). The goal of each statistic research is analyzing the possibilities of risk occurrence, its frequency and scope, all in order to maintain the necessary insurance fond [5].

The aim of this paper was to perform volatility modeling of Serbian insurance sector. Again, statistics and econometrics are halpfull for our analysis. For our empirical analysis we used univariate Generalized Autoregressive Conditional Heteroscedastic (GARCH) models, with EViews program. We estimated univariate GARCH models using daily data from the Belgrade stock exchange (www.belex.rs) of daily log returns for two stocks (Dunav Insurance Company, DNOS and Globos Insurance Company, GLOS). The data set covers the period from January 8, 2007. to May 4, 2009. Before we could proceed with volatility modeling, we performed an Autoregressive Moving Average (ARMA) analysis for the log returns of stocks. After testing of residuals for ARCH effects, we specified a volatility model if ARCH effects were statistically significant. When performed a joint estimation of the volatility equations, we gave discussion of results.

The rest of the paper is organized as follows. Section 2 presents stochastic nature of insurance sector. At the beginning of the second section we present data of Dunav and Globos Insurance Companies. The rest of Section 2 presents ARMA analysis of these stocks. Section 3 presents volatility of these insurance stocks. The Section 4 concludes.

2. Stochastic nature in insurance sector

Every insurer, or insurance company, while dealing with everyday business, is faced with a fact that its future financial results will mostly be a consequence of current premium calculation. Business success or its dependence on the scope of determined premium is especially frequent in property insurance, considering rather limited possibilities of return of investment. Due to this fact, it would be needless to emphasize that every insurer who thinks appropriately of its financial stability, needs to pay great attention to both, methods of determining the premium, and creating adequate risk statistic – a ground on which the premium is built. Insurance portfolio stability is expressed in statistic values, probability that insurer's accumulated incomes will be sufficient to cover arranged payments, as well as possible deviations from expected payments. Without direct implementation of these theories, insurance business would be equal to accidental activities, with no real possibility of determining required scope of premium, as well as scope of possible risks [9], [5].

However, we can say that insurance process has stochastic nature. We proceed with empirical analysis of data from insurance sector, in order to demonstrate its stochastic aspects.

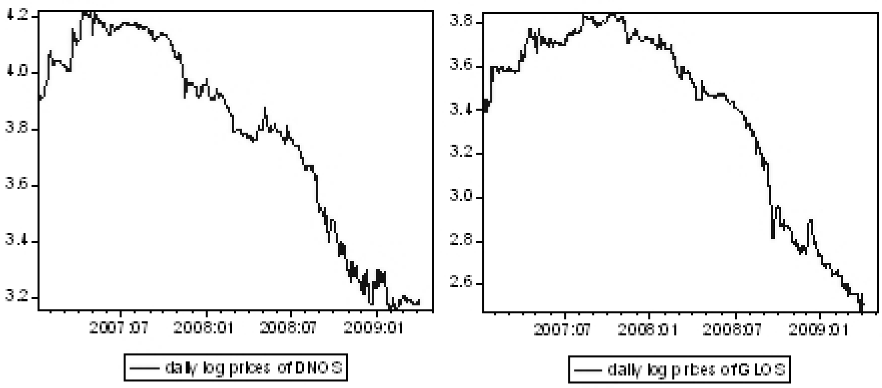
2.1. Data

Although all insurance companies in Serbia are corporations, the most of them is in the dominant ownership of one or two institutional investors (i.e. institutional investors owned more than 90% of equity in 19 from 24 active companies), and their stocks are not in the free float at the Belgrade Stock Exchange. So, we chose the insurance companies in Serbia which stocks are most frequently traded, Dunav and Globos. Our main goal is to analyze volatilities of these stocks. The data set covers the period from January 8, 2007. to May 4, 2009.

Dunav Insurance Company is the biggest and oldest insurance company in our country. It relies upon the 150-year long tradition of Serbian insurance. In spite of all the changes our society has been though during the period of one and a half century, Dunav Insurance Company has managed to remain a secure and strong support to citizens, companies and institutions. Today, this company couples its vast experience with the most up-to-date world trends in the insurance business. Its knowledge and good insight into local market conditions give to Dunav Company the crucial advantage. Its lives and business activities are entirely committed to others. Today, it is a modern company, the leader on the home insurance market and one of few insurance companies registered for all insurance classes. This company possesses a strong business network which, through continual business and information system development, reaches the top standards of the major European insurance companies. The name Dunav, as the symbol of the link between Europe and our country, was established in 1974 [16].

Globos Insurance Company is a Serbia-based company principally engaged in the insurance sector. The company's offer includes property insurance, life insurance, vehicle insurance, health insurance, transport insurance, agricultural products insurance and financial assets insurance, among others. The company has one branch office in Novi Sad and six representative offices in Backa Topola, Sombor, Sremska Mitrovica, Zrenjanin, Kragujevac and Nis. The majority stakeholder of the company is Vojvodjanska banka ad Novi Sad that owns a 83.7% stake in its capital [17].

Figure 2.1 The graphs of daily log prices of Dunav Insurance Company (DNOS) and Globos Insurance Company (GLOS) stocks.



Numerous empirical evidences suggested that the price series (log values) of both stocks of insurance companies are not stationary and are stationary when they are first differenced. Augmented Dickey Fuller Tests reveal that price series of DNOS and GLOS stocks contain a unit root [8]. Therefore, the first difference of the logarithm of DNOS and GLOS prices, the continuously compounded rate of return as calculated below, had applied in the estimation process.

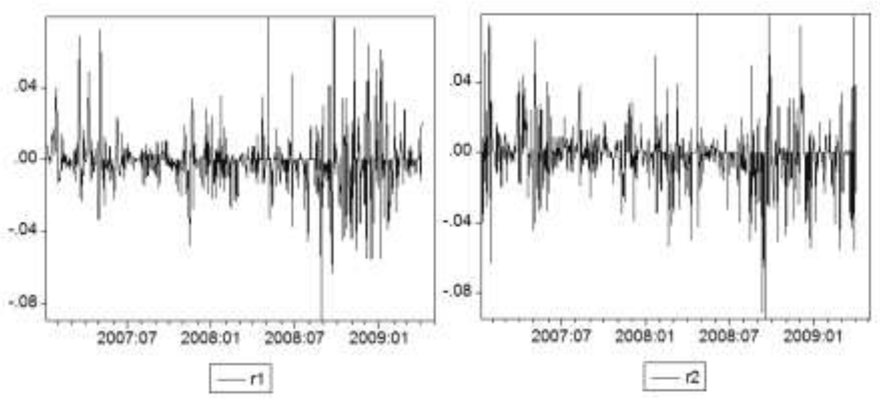
$$\textit{DNOS daily continuous return} \quad r_{1,t} \quad \log P_{1,t} / P_{1,t-1}$$

$$\textit{GLOS daily continuous return} \quad r_{2,t} \quad \log P_{2,t} / P_{2,t-1}$$

where $r_{1,t}$ and $P_{1,t}$ represent the daily continuous return and daily closing price of DNOS at time t respectively, and $P_{1,t-1}$ is the daily closing price of DNOS at time t - 1. Similarly, $r_{2,t}$ and $P_{2,t}$ represent the daily continuous return and daily closing price of GLOS at time t, and $P_{2,t-1}$ is the daily closing price of GLOS at one period prior [8]. Figure 2.2 presents log returns of these stocks.

We observe from Figure 2.2 that the log returns of DNOS and GLOS stocks evidence the well known the volatility clustering effect. It is tendency for volatility in financial markets to appear in bunches. Thus large returns (of either sign) are expected to follow large returns, and small returns (of either sign) to follow small returns [2].

Figure 2.2.The graphs of daily log returns of Dunav Insurance Company (D□OS, r_1) and Globos Insurance Company (GLOS, r_2) stocks



Our analysis contains specification of a mean equation by testing for serial dependence in the data and building an ARMA model for the log return series to remove any linear dependence. Then, it contains testing for ARCH effects in residuals (Subsection 2.2). The analysis contains specification of a volatility model if ARCH effects are statistically significant and joint estimation of the mean and volatility (GARCH) equations. Finally, it contains diagnostic checking of the fitted models (Section 3) [10].

2.2. ARMA modeling

We perform an Autoregressive Moving Average (ARMA) analysis for the log returns in order to obtain a residual series which is free of serial correlation. We have tested several combination ARMA(p,q). We specify and estimate ARMA models which minimize the information criteria (Akaike, AIC and Schwarz, SIC). Akaike's criterion suggests ARMA(2,2) model, and Schwarz's criterion suggest ARMA(1,1) model for log return of DNOS stock. We know that SIC correctly identifies an ARMA model, whereas AIC tends to overfit the model [1]. Then, according SIC criterion we choose ARMA(1,1) process for log return of DNOS stock. So, we infer that right model for log price of DNOS stock is ARIMA(, ,). Akaike's criterion suggest ARMA(,) model, and Schwarz's criterion suggest ARMA(2,2) model for log return of GLOS stock. Similar as previous, according SIC criterion we choose ARMA(2,2) process for log return of GLOS stock. It can conclude that right model for log price of GLOS stock is ARIMA(2,1,2).

The residuals obtained from ARMA models for both series are not normally distributed according to coefficients of skewness, kurtosis and Jarque-Bera (JB) normality tests. However, even if the distribution of the residuals is not normal, the estimates are still consistent under quasi-maximum likelihood (QML) assumptions [15]. Obviously, the residuals have to be tested for the absence of autocorrelation. With the Ljung-Box (Q) test, we test whether the residuals behave like a white noise process [11]. There are the significant Q-statistics for squared residuals across many lag lengths for DNOS and GLOS stocks and we infer the presence of ARCH effects. On the other hand, the Lagrange multiplier (LM) test shows strong ARCH effects for these stocks with test statistic $F = 4.881$, $p = 0.0002$ for DNOS and $F = 9.292$ with the p-value of which is zero for GLOS.

3. Volatility of Serbian insurance market

Volatility plays an important role in controlling and forecasting risks in various financial operations. For a univariate return series, volatility is often represented in terms of conditional standard deviations. The autoregressive conditional heteroscedasticity (ARCH) model and the generalized ARCH (GARCH) model are useful and important in describing the time-varying variances of economic data in the univariate case [12], [6]. For detail about theoretical and empirical modeling univariate GARCH processes you can see references [6] and [7].

We consider univariate time series models in order to examine volatility of Serbian insurance companies. We estimate the univariate GARCH models with EViews program, Version 4.1 using daily data from Belgrade stock exchange for two daily log returns of stocks (Dunav Insurance Company, DNOS and Globos Insurance Company, GLOS). The data set covers the period from January 8, 2007. to May 4, 2009.

We find that coefficients for ARMA processes for DNOS and GLOS are significant at the 5% level. Then, coefficients for GARCH process for DNOS are highly significant at the 1% level and for GLOS are significant, too at the 5% level. From Equation (3.2) we observe that sum of the ARCH and GARCH parameters close to unity, for example $a_{ii} \quad b_{ii} \quad 1$. This suggests the persistence of ARCH effects in the DNOS datasets and, hence, implies that current information remains important for forecasts of conditional variances at all horizons [13]. This special type of GARCH model is termed as Integrated GARCH (IGARCH). In order to examine IGARCH process, we apply Wald test. The first, we formulate the null hypothesis: the sum of the ARCH and GARCH coefficients is very close to one. According to results of Wald test (F = 1.009, p = 0.316; p > 5%) the null hypothesis is not rejected. Hence, we can conclude that log returns of DNOS follows IGARCH process.

A joint estimation of the ARMA(1,1)-IGARCH(1,1) model for DNOS gives

$$r_t \quad \underset{0.0007}{-0.0027} \quad \underset{0.0028}{0.9842}\, r_{t-1} \underset{0.0099}{-1.0103} \quad {}_{t-1} \quad {}_{t}\,, \tag{3.1}$$

$$ {}^{2}_{t} \quad \underset{2.29\,10^{-6}}{6.17\ \ 10^{-6}} \quad \underset{0.0657}{0.2334} \ {}^{2}_{t-1} \quad \underset{0.0444}{0.8032} \ {}^{2}_{t-1}. \tag{3.2}$$

A joint estimation of the ARMA(2,2)-IGARCH(1,1) model for GLOS gives

$$r_t \quad \underset{0.0006}{-0.0010} \underset{0.1184}{-1.2301} r_{t-1} \underset{0.1254}{-0.3350} r_{t-2} \quad \underset{0.1143}{1.1632} \ {}_{t-1} \quad \underset{0.1292}{0.2972} \ {}_{t-2} \quad {}_{t}\,, \tag{3.3}$$

$$ {}^{2}_{t} \quad \underset{8.73\,10^{-6}}{1.78\ \ 10^{-5}} \quad \underset{0.0402}{0.1260} \ {}^{2}_{t-1} \quad \underset{0.0558}{0.8307} \ {}^{2}_{t-1}. \tag{3.4}$$

It is interesting to note empirical regularity in Equations (3.2) and (3.4) that the estimates of ARCH terms are small and positive, with the estimates of GARCH terms much larger. Again, in equation (3.4) we see that the sum of the ARCH and GARCH coefficients is between 0.9 and 1, for GLOS stock. These parameter values imply that the time-varying volatility is highly persistent [3]. According to results of Wald test (F = 1.872, p = 0.172; p > 5%) the null hypothesis about the sum of the ARCH and GARCH coefficients close to unity is not rejected. Hence, we can conclude that log returns of GLOS follows IGARCH process. We know that if residuals follows an IGARCH process, then the its unconditional variance is infinite, so neither residuals nor squared of residuals satisfies the definition of a covariance-stationary process [4].

Thus, DNOS stock follows ARMA(1,1)-IGARCH(1,1) model, and GLOS stock follow ARMA(2,2)-IGARCH(1,1) model. The fitted models can be checked by using the standardized residual and its squared process. The Ljung-Box statistics (Table 3.4) of standardized residuals and those of its squared show that models are adequate for describing the heteroscedasticity of the data.

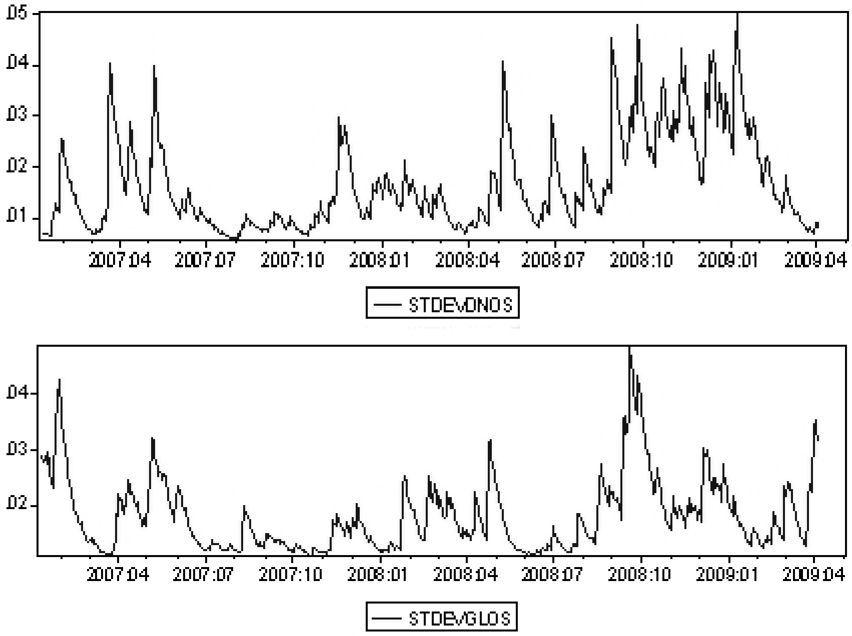
We apply the ARCH test on the standardized residuals to see if there are any ARCH effects left. Both the F-statistic and the LM-statistic are very insignificant, suggesting no ARCH effect up to order 5 or 10 for both series DNOS and GLOS stocks (see Table 3.4).

Table 3.4. The Ljung-Box statistics and ARCH-LM test of order 5 and 10.

	The Ljung-Box Statistics		**ARCH-LM(5) test**		**ARCH-LM(10) test**	
series	**Q(36)**	**Q^2(36)**	**F-stat**	**Obs*R^2**	**F-stat**	**Obs*R^2**
DNOS	37.648 (0.306)	33.990 (0.468)	0.3278 (0.8963)	1.6513 (0.8950)	0.4831 (0.9013)	4.8838 (0.8988)
GLOS	27.111 (0.713)	21.971 (0.908)	0.1880 (0.9671)	0.9482 (0.9666)	0.599198 (0.8150)	6.044808 (0.8115)

On Figure 3.1 we plot the conditional standard deviations for DNOS and GLOS stocks.

Figure □1. The conditional standard deviations for D□OS (termed as STDEVD□OS) and GLOS (termed as STDEVGLOS) stocks, respectively



In addition to visual inspection Figure 3.1 tell us conditional standard deviations series exhibit significant changes over time for both stocks. Therefore, these volatilities are very unstable over time.

Conclusion

This paper presents empirical analysis of volatility in Serbian insurance market. For empirical analysis we had to perform univariate GARCH analysis using daily data listed at the Belgrade stock exchange of daily log returns for (Dunav Insurance Company, DNOS), and (Globos Insurance Company, GLOS) stocks. It has been observed that conditional standard deviations exhibit significant changes over time for both stocks. Especially, volatilities of Dunav and Globos insurance companies stocks satisfy Integrated GARCH process. This suggests that the time-varying volatilities are highly persistent. In another words, we infer that unconditional volatility of insurance companies stocks in Serbia is infinite. As we said before, the Serbian insurance sector is very small, and undeveloped. Main finding of this paper is that volatility of insurance sector is unstable and persistent - which means that Serbia is a country with relatively low per capita income and very high risk in insurance sector. In this observed period from 2007 to 2009 we can say that Serbian insurance market is in transition, with property of high volatility (risk). We hope that Serbia will become member of the World Trade Organization (WTO) and the EU, as soon as possible. In that case, we expect that the Serbian insurance market could get a significant benefit.

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BANKING SECTOR IN SERBIA: ITALIAN BANKS - CASE OF POSITIONING BANCA INTESA AS THE LEADING LOCAL BANK

Jelena Tošić[1]

Abstract

Banking sector was of the outmost interest for foreign investors locally once the Serbia entered the process of privatization and, before break of crisis, the most growing one. Given that the Italy is one of the single biggest investors as a country in Serbia, it was more than expected that the Italian banks will enter in the local banking game. Banca Intesa was the first in 200[illegible], penetrating market through purchase of majority package of former Delta Banka, followed by privatization of Panonska banka by Banca San Paolo in 2006 and change in ownership of HVB Bank that was acquired on global level by Unicredit bank, one of, not only Italian, but European biggest financial group[2].

The following article will refer mostly to the Banca Intesa (now present after merger with San Paolo as Intesa Sanpaolo) as a case of how successful acquisition of a local bank, further investment and the strengthening of the gained benefits positioned it as the leading local bank. Success of the Bank in reaching the highest goals, e.g. in retail and card business is setting and excellent example and highest standards for other banks, contributing overall quality of banking business in Serbia.

Key words: *banking sector, Italian banks, Banca Intesa, leading local bank*

Introduction

Banking sector in Serbia have driven over the years development of the overall economy and, although highly regulated, is the most dynamic and liquid one with still very high rates of growth.

Banking market has not contracted in the number of Banks largely over the period given that the foreign banks are highly monitored and directed by their mother companies, with no signs of future possible mergers.

Regardless the financial crisis, with its outburst in the last quarter of 2008, most of the local banks have recorded large profits in 2008 of about RSD 33.5 billion dinars or 44.5% more than in 2007. It seems that 2008 was very fruitful year for many banks, especially for the two Italian banks that generated 21.41% of the overall profit of banking sector, being amongst the first 5 banks by profits in 2008 (see table below).

Table 1. Profits of the biggest five banks in 2008.

2008		**000 EUR**
1.	Raiffeisen bank	78,585.44
2.	**Banca Intesa**	**72,332.11**
3.	AIK Banka	68,149.31
4.	EFG Eurobank	47,337.73
5.	**Unicredit bank**	**35,347.54**

Source: *Udruzenje banaka Srbije*

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[2] Findomestic is the third currently present Italian bank locally but given lack of comparable data published and rather smaller size than the other two banks made it difficult for comparison. Some of the most important data are presented in Appendix to this text.

Presented banks have realized 60% of the overall profits of the banking sector in 2008 or almost EUR 302 million.[3] 2 banks were "winners" in 200 while have realized losses amongst which there are broadly seen "new-comers" like Marphin bank and Meridian (Credit Agricole) bank accompanied with Metals' bank huge loss. These three banks took 0% of the losses in 200 .[4]

Huge profits were partly contributed to considerable increase of the market share, primarily by Banca Intesa, followed by two Greek banks, Vojvodjanska banka and Eurobank EFG, and aggressive Belgium KBC and OTP bank.

In spite crisis, taken as a whole, financial situation of the banks is not remotely warring as expected and it seems that strict regulation of the National Bank of Serbia has contributed to sustain sound banking sector that is surpassing crisis with no greater difficulties. The level of placements in the banking sector has increased by 13.8% in 2008 in comparison to 2007 but still half less than the growth that has been recorded in the past given high level of loans already granted to corporate clients and privates.

According to the Q1 2009 financials most of the banks are realizing profits and expected to continue in the same manner given the recent slight loosening up of the restrains and revival of the business activity. The real peril, though, still lies in the fact that real business activity is jeopardized with fluctuations of FX rate, decreased level of activity and turnovers that are strongly related to considerable non-liquidity of companies, which pace of downturn will finally influence the activity and profits banks are realizing. The situation is slightly worsening given that the percentage of corporate clients delaying in repayment of the loans at end of April 2009 is 9.2% against 6.3% end of December 2008.[5] It is noticeable as well that the clients are repaying loans to banks but this market is contracted for the time being with no large new disbursements. It seems that banks are opening again to attracting new customers, at least according to the recent aggressive commercials that can obviously be seen as a good sign of possible recovery in the market.

Banca Intesa seems not to be stopping its activity, supported by its mother company that appears according to its financial record, hasn't been heavily influenced by crisis.

1. Banca Intesa International

Given that the major topic of the work is how Italian banks are present locally, i.e. how and with what numbers they are contributing local economy with, special emphasis will be placed to Banca Intesa as the local banking leader, together with the size of the Banca Intesa globally, being aware that good business policy "spill over" to other markets where the Bank is present.

After numerous regrouping of small Italian banks, Banca Intesa was formed in 2002, the same year where, on the other side was formed Grupo Sanpaolo IMI, where later on (2007), by the merger of these two, was formed Intesa Sanpaolo bank, an international banking conglomerate with:

- **19.7** million customers (app. 11,2 million Italy and 8,5 million abroad)
- **8.318** branches (6,354 in Italy and 1,964 abroad)
- Total assets of **639 billion** euros
- Direct customer deposits **436 billion** euros
- Net income of over **1 billion** euros in 1Q 2009.[6]
- Rated: AA- by Fitch, Aa2 by Moody's and AA- by S&P
- **Number 1** in Italy in by: placements (17.4%), deposit (18%), factoring (24,3%) , asset management (27.4%) and as a pension fund (28.1%).
- Present in **13** countries: Albania, Bosnia and Herzegovina, Croatia, Czech Republic, Egypt, Greece, Hungary, Romania, Russia, Slovakia, Slovakia, Ukraine and Serbia.

Roughly, Banca Intesa realizes 18% of its operating income in Italy and 82% in other countries.

[3] Profits before income taxes - Exchange rate 31st December 2008, RSD 88.6010 for 1 EUR.
[4] Source: Banker www.kliping.rs
[5] Data published by Udruzenje banaka Srbije internet site www.ubs-asb.com
[6] Internet site of Intesa Sanpaolo

According to the Eurozone ratings Intesa Sanpaolo is rated 5th by banks' market capitalization, followed immediately with UniCredit, confirming that between Intesa Sanpaolo and UniCredit there is a tight struggle on the global level, much more than in the local market given that Banca Intesa takes 1st place where, on the other side, UniCredit being 6th or 8th bank by most of the crucial parameters.

Unicredit Group operates in **22 countries** with **10.200 branches** having quite larger network than Banca Intesa, but always being one step behind Banca Intesa making their rivalry driver of the better quality service in Italy. Although having five century long history in banking, Unicredit as it is today was created through merger of nine of some of the biggest Italian banks with Capitalia Group and German HypoVereinsbank Group in 2005.

2. Purchase of Delta banka by Banca Intesa

Banca Intesa has entered the local banking market though single largest transaction of bank purchase in Serbia via acquiring the largest local bank, Delta Banka in June 2005. At the time, Banca Intesa acquired 75% majority stake for the price of EUR **277,5 million.** Italian Banca Intesa or its related parties now own 100% of Banca Intesa Beograd.

Banca Intesa started with spreading its network through Eastern and Southeastern Europe by founding Central International Bank (CIB) in 1979, the fourth largest bank in Hungary. Later on, two other leading financial institutions were purchased–Croatian Privredna Banka Zagreb (PBZ) in 2000 and the Slovak Vseobecna Uverova Banka (VUB) in 2001, the second largest banks in the relevant countries. Banca Intesa also functions in the Czech Republic, in Slovenia through its Italian branch Banca Popolare FriulAdria and in Russia with ZAO Banca Intesa.

Through acquiring Delta Banka, Banca Intesa overtook the leading position in the Serbian banking market with **144** organizational units in more than 100 towns in Serbia, **30%** of the FX transactions and **20%** of the RSD transaction done through Delta Banka. 14-year long experience of Delta Banka, modern system of operations and large accounts of the Government as well as private institutions strongly attracted Banca Intesa to pay fair share in order to enter into local market with guaranteed market share, both in corporate and retail banking.

Benefits Banca Intesa realized is very high market share in performing both, FX and dinar transactions, contributed to strict dedication of the Bank to operate with companies for almost 11 years and trying to be on top of offering up-to-date services to its clients (e.g. electronic FX transactions that were not that common service at the time, etc.). One of the biggest fortes of the Bank is that the Delta Banka at the time started as provider of Master Card for the local market and gained large market share (90%) that was kept then on. Banks has, as well, the most developed network of POS terminals that together with the market share in Mastercard, help the Bank to increase the market share even making as clients even companies bank is not having credit lending activity with. Practice showed that all companies engaging in retail business are always going to engage in cooperation with Intesa banca given that their POS terminals are the only ones that can be used for the all credit cards and, to the common knowledge, are offering lowest commission for this kind of transaction due to wide-spread network.

Banca Intesa actually acquired bank that already was a market leader with immense know-how particularly in offering electronic services and card business. Nonetheless, although bank head strong developed wholesale, presence of Banca Intesa helped to develop retail network, introducing first all new products, that now differentiates Banca Intesa as leader in retail, as well. Merger via absorption with Panonska banka in 2007 certainly contributed to increase of already huge market share of Intesa.

2.1. Privatizing of Panonska banka by SanPaolo Bank

In July 2006 Serbian Government has reached the agreement on sales of 87,39 % of the, at the time, socially owned capital of Panonska banka for the price of approximately 122 million euros, paid by Italian bank "San Paolo INI" from Torino, third in Italian banking market at the time, whereby government announced that the funds obtained from the proceeds from the sale was 4,7 times higher than

the book value of the bank.The whole transaction amounted 140 euros million with payoff of small shareholders.[7]
Until the end of 2007 the merger by absorption was carried out whereby the Bank acquirer was Banca Intesa and the acquired bank Panonska banka. Upon this merger Panonska banka ceesed to exist and its shares were withdrawn and annulled.[8]

3. Banca Intesa as a local leader

According to 2008 financials Banca Intesa has managed to sustain or become:

- Number 1 by revenues
- Number 1 by Total Assets with 14.3% market share
- Number 1 by total placements to customers with 15.3% market share
- Number 1 by total customer deposits with 13.9%
- Number 2 by total capital

Table 2. Ten biggest banks by assets in 2008

ASSETS (RSD million)	Dec-08	Dec-07	change in assets
Banca Intesa	***250,201***	***193,938***	***29.01%***
Komercijalna banka	*1□0,861*	*1□□,20□*	*16.10□*
Raiffeisen bank	*160,896*	*1□□,1□0*	*2.□0□*
Eurobank EFG	*12□,029*	*8□,110*	*□□.□0□*
HypoGroup Alpe Adria	*11□,□99*	*1□□,□9*	*□1□.□0□*
Unicredit Banka	***89,514***	***73,070***	***22.50%***
Vojvodjanska banka	*86,□12*	*8□,9□2*	*□1.□0□*
AIK Banka	*8□,□28*	*□8,289*	*6.60□*
Societe Generale	*□1,89□*	*6□,□0□*	*9.90□*
ProCredit Banka	*6□,808*	*61,6□□*	*□10□*

Source: *□ational Bank of Serbia website*

For many years in the row, Banca Intesa is the biggest by the assets in the local market. Although its assets, according to the presented figures, have been in this period above other local banks, still, after Eurobank EFG, they are having the biggest rate of growth. Unicredit, another Italian bank, is not going back far in the line, being 6th by the value of its assets, recording high rate of growth as well.

Table 3. Ten biggest banks by market share in 2008

Amount of placements to clients (million RSD)	Market share December 08
Banca Intesa	***15.3%***
Komercijalna banka	*9.8□*
Eurobank EFG	*8.□□*
Raiffeisen bank	*□9□*
HypoGroup Alpe Adria	*6.6□*
AIK Banka	*□□□*
Vojvodjanska banka	*□□□*
Unicredit Banka	***4.4%***
Societe Generale	*□0□*
ProCredit Banka	*□□□*

Source: *□ational Bank of Serbia website*

[7] **Source:** *www.blic.rs*
[8] **Source:** *Audited financial report Banca Intesa for 2008*

Value of the assets and the capital are showing strong dedication of the bank to maintain in the local market as one of the leading banks, at the same time benefiting from the high potentials of the local market, both in wholesale and retail banking.

Banca Intesa has a considerable market share by the number of placements to the customer and growing, on year to year basis (11,7% in comparison to 2007).

Overall Placements in 2008 were RSD 60 billion higher than with the second rated bank, Komercijalna banka (11.1% growth 2008/07 basis), while in absolute amount, have risen by RSD 74.3 billion in comparison to 2007.

Placements have risen contributed both, to aggressive marketing campaign, as well as quality service accompanied by reasonably acceptable interest rates. It seems that the increased competition produced by aggressive strategies of most of the major banks have proven that the quality of service and widespread presence of Banca Intesa (through 230 branches throughout Serbia) made it bank of a choice for wide majority of clients. Above said are also the major reasons why Banca Intesa is the leading bank by the level of deposits made by customers.

Table 4. Ten biggest banks b of s o r d os s n

Amount of customer deposits	**Market share December 08**
Komercijalna banka	***13.9%***
Raiffeisen bank	*1□0□*
Eurobank EFG	*9.2□*
Unicredit banka	*8.□□*
Vojvodjanska banka	***5.5%***
HypoGroup Alpe	*□.□□*
AIK Banka	*□.1□*
Societe Generale	***4.4%***
Alpha Banka	*□.6□*
	□.□□

Source: *Banca Intesa official website*

Unlike growth experienced in placements toward customers, the share of deposits has decreased from 14.3% in 2007 to 13.9% in 2008 (5 of the listed banks have experienced decrease in the volume of deposits in 2008 as well). The reasons for this decrease could be looked up in the aggressive marketing promotion of other banks offering high deposit interest rates, but most of all, in the panic of the possible non-liquidity of the banking sector with the outbreak of financial crisis. It seems that the privates, as well as companies, took a word of advice from major country's economic figures and split deposits over several banks (absolute winners after these divisions were, most certainly, Komercijalna banka and Eurobank EFG being the only ones with substantial increase in deposits as of 2008 end). Given the sustained withdrawal of cash and its moving to other assets, Banca Intesa can be more than satisfied with the level of deposits of approximately RSD 142 billion.

Table 5. Major Banca Intesa financials in 2008

RSD million	**2008**	**2007**	**change 2008/07**	**% delta**
Net operating Margin	21,584	13,834	7,750	56.02%
Total Operating costs	8,348	5,273	3,075	58.32%
Net operating pf	**13,236**	**8,561**	4,675	54.61%
Net profit before income tax	**6,409**	**3,327**	**3,082**	**92.64%**
Income tax	517	170	-	-
Net profit after income tax	**5,892**	**3,157**	**2,735**	**86.63%**

Source: *Banca Intesa official website*

With no attempt to go into deep analysis of the Income statement the above table is only mere overview of the financials of the bank presented in a way to grasp the pace of growth of revenues and, not falling behind, profits of the Bank.[9]

Banca Intesa seems to be so successful applying up-to-date technology and offering to its clients top service in this respect. Even from the period of Delta Bank it has been general provider for Mastercard in Serbia having the far ahead the largest number of users. It was the first bank that revived the business with American Express cards. The bank has widespread network of POS terminals and every good retailer that wants its business to be done in fast and efficient way has a POS terminal of Intesa bank (being the only one in the local market that is able to pass any of the major credit and debit cards). The reason why this is pointed out two times in the work is the fact that this particular service offered generates large turnover for the Bank followed up with the high revenues generated on this kind of transactions. Up until recently (prior to financial crisis) in the situation of high based interest rates and tight margins conducted with high competition in the local market, auxiliary business and achieving high level of turnover on the clients' accounts were the major points of generating extra revenues. Banca Intesa gain its more than fair share of the market by offering the excellent electronic services to its customers, through card business and e-banking.

Conclusion

The case of Banca Intesa shows how smart acquisition of the local bank and constant investment in the prestigious quality of work can make certain bank a leader in a banking sector and, more over, sustain this position period throughout the period.

According to the official data by Banca Intesa, there is about 1.350.000 customers in the local market, both private and corporate[10]. As already explained, customers are attracted with high level of service and vicinity of 230 branches of Banca Intesa. When privatized in 2005, bank was a leader in the wholesale in local market while the know-how and investment made by Mother Company made it leader in retail banking.

According to the Q1 2009 results Banca Intesa is still operating very well recording income (before taxes) of about RSD 1.5 billion while maintaining current branch network and number of employees (Banca Intesa hired 88 new people in Q4 2008 unlike other banks that were decreasing number of employees[11]). Nonetheless, it is not expected that number of branches and employees will grow in the forthcoming period given the overall negative growth trend in economy. In order to collaborate that banks, in spite crisis are still doing well, are the excellent results of Unicredit bank for Q1 2009 that recorded profit of about RSD 664 million or 13% more than in the same period last year. Officials of the bank are saying that the number of employees has increased by 100 and number of branches by 20 in comparison to same period last year.[12]

Striving for excellence and firm commitment to its presence in the local market are once again reasons why Banca Intesa is the leading bank by its assets, volume of placements to customers and deposits made by customers, leader in retail banking with over 1 million issued cards, largest POS and ATM network and leader in domestic and foreign currency payment.

Customers of bank are benefiting from excellent service of the Bank while state is benefiting from the taxes on income made by the Bank. Banca Intesa has generated 14.38% of the overhaul profits (21.41% together with UniCredit as the other Italian bank).

Nonetheless, it is obvious that the banks, and therefore Banca Intesa , will have to slightly change the way of doing business in the situation of highly contracted market. One of the way-outs is participating in the various Government programs organized to stimulate activity of the economy, like Govern-

[9] **Source:** *Audit financial report of Banca Intesa Beograd 2008*
[10] **Source:** internet site *www.bancaintesabeograd.com*
[11] **Source:** *□BS report on banking business – last quarter 2008*
[12] **Source:** *Bankar June 2009 – □umber □0 issue*

ment subsidized loans and moreover, loans for agriculture where Intesa joined from the very beginning in the approval process. Intesa has granted around 108 million euros of Government subsidized loans since the beginning of campaign and participated amongst 8 banks that have granted 470 loans in overhaul amount of 135 million euros to agriculture.

It is expected that the banks will have to offer in the future more sophisticated service and tailor-made products in order to attract and maintain clients. The escalation of the financial crisis have proven, if anything, that the over production of the banking loans with very shallow insight in the client's business and its needs, with nothing but the will to sell, by all means, cannot sustain as banking business policy in the long-run. Therefore, the know-how combined with deep understanding of clients' needs will have to provide future guideline for all the banks on how to do business. Banca Intesa obviously realized this timely so we are yet to see how, even in the turbulent times, it will act as a driver of changes, conducting business where both, clients and the bank, will benefit.

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APPENDIX

Findomestic banka basic information

Findomestic bank has entered Serbian market through purchase of local bank Nova banka in 2006 and has acquired a certain part of market share since than. Findomestic was present mostly in retail banking through points of sale direct to customers in 1.980 places.

Owners of the Findomestic bank S.p.A., founder of Findomestic banka, are is BNP Paribas 50%, Banca CR Firenze 47.17% (member of Intesa SanPaolo Group) and Casa di Risparmio di Pistoia e Peschia with 2.83%.

Loans granted in 2008 with regard to the consumer credit sector totalled EUR 27.1 million, up 11.7%. As at 31 December 2008, gross loans totaled EUR 84.3 million, up 62.9% compared to 31 December 2007.

Approximately 32% is represented by consumer credit activities and 68% by traditional banking services. The company suffered a loss of EUR 2,017 thousand, a decrease (-24.6%) compared to the loss recorded in 2007 (equal to EUR 2,674 thousand).

Profit of the Findomestic Group amounted some EUR 62 million with small decrease of 9.8% in comparison to 2007.

The aim of the Group is not to position its self as a leader in market, like Intesa SanPaolo and UcuCredit but more to search for the niche in the retail sector, to small outlets and points of sale.

FOREIGN DIRECT INVESTMENTS IN SERBIA – WHAT HAS BEEN DONE SO FAR AND WHAT CAN WE EXPECT*

Jovan Zubović[1], *Ivana Domazet*[2], *Milena Kovačević*[3]

Abstract

Strategic approach to foreign investments in Serbia has changed significantly at the beginning of XXI century. Before 2000 Serbia was a country that used high level of custom and non-custom barriers to protect its economy. During the period of nine transitional years Serbia shifted to completely liberal approach of an open market economy.

A starting impulse to foreign investments in Serbia was given by the new approach to privatization process of state companies, which attracted over [illegible] billion euros of investments. Stable and transparent political model that was created made significant impact to an increase of foreign investments into the country and growth of foreign capital share in the market as a whole, with over € 1[illegible] billion of inflow.

Since transition in Serbia in its full scale begun with ten years delay compared to other eastern and southeastern European countries, so was the first stage of the transition process completed with significant delay. For that reason it is important to understand in which way Serbia will approach second stage of transition, which is critical for sustainable development in the next period. Past experience of other countries should be used to understand what should and what should not be done in order to achieve so called "Virtual Circle of Foreign Investments". Clear strategy and vision of Serbia in the future is required in order to attract not only those FDI which are seeking for fast turnover and use of natural resources, but rather those which are able to provide high level of added value and able to transfer technology and skills to economy as a whole

Key words: *Foreign investments, transition, privatization, virtual circle of FDI*

1. Strategic approach to FDI in Serbia

Transition from centrally planned economy to market oriented economy is a long and difficult process for most countries. Limitation to foreign ownership and introduction of strict rules protecting certain sectors of the economy by allowing only domestic investments may be devastating for national policy of foreign direct investments. These types of economies are characterized by barriers to imports, which as a rule, are represented by high custom taxes. Generally those countries are not opposed to foreign investments, but their introduction of specific economic measures and strict rules diminishes value of foreign ownership. In such a way, the benefits of export oriented economy and economy with high foreign competition are minimized.

Dual effects of strategy based on barriers to import are protection of national interests on the one side and low level of FDI on the other side. High custom and non-custom barriers have in many cases forced foreign investors to reduce scale of production, which results in non-profitable operations and low level of turnover. Such strategy does not reduce dependency on foreign capital and it reduces national income, income from trade and benefits from increased employment.

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According to Zatezalo (2009) it is recommended that governments, before attracting foreign capital, create viable and sustainable strategy which will define what sectors are priority for attracting FDI. Despite ten years delay in creation of national policy for attraction of FDI compared to other countries in the region, Serbia can use their experiences and chose the best possible direction. After nine years of different methods in attracting FDIs there is a consensus among politicians which strategies have shown to be most effective. Core of the strategy should be open and transparent economy based on knowledge.

Stable and transparent political system supports growth of FDI. Knowing that the path which transitional countries have to go through to become open and transparent market economies is very long, it is certain that export oriented strategies guarantee success in attracting FDIs. Governments are applying this strategy when there is high level of unemployment, because the highest growth in export oriented countries is generated by attracting foreign investments in production sectors like clothing or electronics.

At the beginning of transition Serbia opened its market. Since then Serbia is getting closer to EU market and regional markets like CEFTA. Becoming a member of WTO and acceptance of sectoral initiatives for reduction of custom rates is a process that significantly facilitated inflow of foreign capital. A study made by several authors was a basis for acceptance of 4 sectoral initiatives by Serbia (ubovi et al, 2007, 2008).

2. Foreign investments in the first stage of transition

Privatization process is most common model to support FDI inflow to transitional economies. There is a high correlation between inflow of FDI and privatization, where one process supports the other and vice versa. Countries which have gone furthest in privatization are known to be attractive locations for investment of capital. On the other hand inflow of capital supports and gives pace to privatization (Hunya, 2003, pp 54).

Serbia is moving through transition with growing levels of foreign investments as a result of its method of privatization through tenders and auctions. Inflow of capital is growing after year 2005 with entrance of Telenor, Mobilkom, Phillip Morris Ball Packaging and other multinational companies. During last seven years the initial strategic approach for attracting foreign capital in Serbia was through privatization. Table 1 shows the results of privatization during the period of 8 years. Total level of income from privatization was not very high, but it triggered other investments. Most positive effect of privatization was transfer of employees from state owned to privately owned companies which dramatically changed their work behavior.

Table 1. Privatization of the real sector in Serbia 2002-2009

Type	Total sold/canceled	Selling price	Investments	Social Pro-ra
Tenders	107	1.173.920	1.127.086	276.689
Tenders – canceled	*16*	*[illegible]8[illegible].220*	*1[illegible][illegible].928*	*2.0[illegible]2*
Auctions	1.693	1.113.447	222.385	
Auctions – canceled	*[illegible]69*	*228.960*	*[illegible][illegible].[illegible]09*	
Capital markets	535	518.083	5.902	
Capital markets – previously canceled	114	58.907		
Capital markets – previously privatized	778	3.289		
Total	**2.449**	**2.867.646**	**1.355.373**	**276.689**

Source: *Serbian privatization agency and chamber of commerce*

From table 1 we can see that the number of privatized companies was 2.449, and according to ministry of finance they employed over 330.000 employees (Ministry of finance, 2008). The selling price for those companies was nearly 2.9 billion euros, with additional 1.4 billion reserved for investments and 280 million euros for social program. Unfortunately there is no statistical data about how this capital was used. According to available sources, we might conclude that funds were mostly spent in consumption.

Despite unfavorable status that Serbia enjoys as a investments location, there are many other factors that triggered initial investments. Among them was the privatization process, which in the year 2002 brought 300 million euros of foreign capital. As the process of privatization of so called "social companies" was getting close to the end, so the level of investments grew. Except for the year 2007, there was a constant growth of FDI in Serbia. Table 2 shows the figures about FDI by countris in the period of 7 years.

Table 2. Net FDI in Serbia by country of capital origin in the period 2002-06.2008. (000 US$)

Country	2002	2003	2004	2005	2006	2007	I-VI 2008	Total
Austria	33,876	93,747	146,104	201,189	520,356	1,161,096	355,039	2,511,407
Greece	12,496	62,268	52,968	249,536	923,698	336,401	46,091	1,683,458
Norway	74	280	0	29	1,546,993	3,187	5,608	1,556,171
Germany	82,801	75,708	51,985	187,320	905,824	69,530	68,923	1,442,091
Netherlands	2,248	598,963	102,008	92,113	-214,119	-27,958	555,200	1,108,455
Italy	7,553	21,325	10,149	18,316	52,752	155,363	385,470	650,928
Slovenia	9,561	29,036	15,706	183,563	201,241	92,856	95,324	627,287
France	87,489	7,858	24,022	62,347	159,085	84,391	69,301	494,493
Luxemburg	3,619	4,108	2,387	108,885	8,843	241,537	67,593	436,972
Hungary	1,167	4,224	16,567	24,677	244,045	31,494	15,806	337,980
UK	6,618	20,631	79,620	63,330	135,915	-26,584	9,163	288,693
Switzerland	2,913	12,559	29,401	56,990	-15,421	96,157	41,359	223,958
Croatia	5,243	34,446	10,806	40,484	25,240	35,944	44,047	196,210
Bulgaria	133	129	9,910	655	54,270	46,916	15,878	127,891
USA	18,099	15,068	18,187	22,257	-29,612	31,825	42,510	118,334
Slovakia	10	18,342	0	25,447	19,325	3,084	333	66,541
Russia	2,556	3,359	538	14,324	15,992	488	27,159	64,416
Latvia	5	15,330	17,082	6,441	10,527	3,535	234	53,154
Israel	260	207	3,052	14,294	4,544	26,510	1,233	50,100
Belgium	344	1,925	2,523	12,407	6,464	24,038	-15,108	32,593
Lichtenstein	57	2,162	2,974	-41,316	-17,538	-2,937	2,593	-54,005
Cyprus	41,717	31,581	16,310	71,551	-387,154	137,427	8,947	-79,621
Bosnia	2,951	5,056	2,104	4,692	-16,750	-838,608	-5,212	-845,767
Others	4,664	13,098	182,000	21,175	131,859	318,605	100,468	771,869
TOTAL	326,454	1,071,410	796,403	1,440,706	4,286,379	2,004,297	1,937,959	11,863,608

Source: *Siepa*

Table 3. Largest foreign investments in Serbia in the period 2002-06.2008.

Company	**Country of origin**	**Sector**	**Type of investment**	**Amount .**
Telenor	Norway	Telecommunications	Privatization	1,602
Fiat	Italy	Car industry	Joint venture	700
Philip Morris - DIN	USA	Tobacco	Privatization	611
Mobilkom	Austria	Telecommunications	Greenfield	570
Banca Intesa	Italy	Banking	Capital market	508
Plaza Centres	Israel	Real Estate	Greenfield	500
Stada	Germany	Pharmaceuticals	Capital market	475
Embassy group	India	Real Estate	Greenfield	428
Interbrew - Apatinska	Belgium	Food and Beverage	Capital market	427
NBG	Greece	Banking	Privatization	425
Biotech Energy	USA/Hungary	Oil industry	Greenfield	380
U. S. Steel - Sartid	USA	Steel and plates	Brownfield	250
Mercator	Slovenia	Retail	Greenfield	240
Fondiaria SAI	Italy	Insurance	Privatization	220
Lukoil - Beopetrol	Russia	Oil industry	Privatization	210
Airport City	Israel	Real estate	Greenfield	200
Blok 67 Associates	Austria/Serbia	Real estate	Greenfield	180
Holcim - Novi Popovac	Switzerland	Cement	Privatization	170
OTP Bank	Hungary	Banking	Privatization	166
Engel group	Israel	Real estate	Greenfield	160
Alpha Bank - Jubanka	Greece	Banking	Privatization	152
Metro Cash & Carry	Germany	Wholesale	Greenfield	150
OMV	Austria	Petrol stations	Greenfield	150
Coca Cola	USA	Beverages	Capital market	142
Lafarge	France	Cement	Privatization	126
San Paolo IMI	Italy	Banking	Capital market	122
CIMOS	Slovenia	Car industry	Privatization	100
JTI	Japan	Tobacco	Privatization	100
Droga Kolinska-Grand	Slovenia	Food and beverage	Greenfield	100
Carlsberg	Danemark	Food and beverage	Greenfield	100

Source: *Siepa*

Table 3 shows the list of top 30 foreign investments in Serbia during transition. Majority of those companies are multinational companies. Since most of them are operating in the economic sectors which bring a high level of additional value, it is to confirm that prerequisites for transfer of technology and knowledge spillover have been fulfilled. Despite the fact that there are no empirical studies to confirm existence of technology transfer, many economic sectors in which there was a high level of investments, like financial sector, retail, tobacco industries and sector of telecommunications show positive results. In our previous paper we presented the exact statistical evidence proving that growth of those sectors is much higher than the others, with financial sector leading in the group (Zubovic, Domazet 2009).

In financial sector, Deposit insurance agency had since 2004 conducted restructuring and privatization of seven banks and one insurance company. The following banks were sold for total of 814 million euros: Jubanka, Novosadska banka, Continental banka, Ni ka banka, Panonska banka, Vojvo anska banka and Nacionalna tedionica. Italian Fondiaria SAI in 200 acquired % of the insurance company DDOR Novi Sad for 220 million euros. After these successful transactions, state remained major owner of four banks (Banka Po tanska tedionica, Credy banka, Privredna banka Pan evo and Srpska banka), co-owner of Komercijalna banka and a anska banka and minority owner in few other banks. Dunav insurance is still in state ownership. Government has recently decided to sell its ownership in another six banks: Credy banka, Privredna banka Pan evo, Srpska banka, Privredna banka Beograd, JUBMES banka and Agrobanka. If we add sale of private banks owned by Serbian entities to foreign partners we get in total 1.3 billion euros of foreign capital inflow, which equals to 11% of total FDI in Serbia.

As said above, the process of privatization of socially owned companies in Serbia is nearly over. Around 1,000 companies that have not been or are not in the process of privatization will go bankrupt or will be liquidated. Other companies that have not been successfully privatized in prior tender or auction models, might be reorganized and sold by model applied in Zastava Kragujevac, the car manufacturer which signed joint venture agreement with Fiat. This method tends to attract new investments which would enable modernization, growth of employment and exports.

State owned (public) companies are not in the same position. For them does not apply Law of Privatization regarding terms of completion. Government believes that these companies are good potential to attract large scale foreign income, either by sale of majority or minority of ownership. In the period of economic crisis it is not possible to evaluate the amounts of capital that can be raised for such transfers. Privatization of public sector companies is at the very beginning and there are still legislations to be clarified. The first attempts of privatization of state companies were JAT Airways and mining complex RTB Bor, for which foreign investors did not show satisfactory interest. It was followed by sale of NIS for 400 million euros to Russian counterparts. Such small amount does not give incentive to expect overwhelming amounts for sale of state companies unless structural changes are made prior to transfer of ownership. Privatization of RTB Bor which was expected to be of high interest for foreign capital in three attempts was not completed successfully. This is to support our thesis that for privatization of public sector there must be a topic of a public debate where several different methods of privatization or restructuring should be analyzed in order to enable maximum gain for the economy. Serbian Government plans until the end of 2009 to offer Galenika, and Telekom, Airport and EPS in 2010. The expected income for those sale is over 2 billion euros. We believe that the approach which has been used in privatization of public sector does not allow us to be so optimistic.

According to Serbian Government in next few years, 3 billion euros yearly are required to support sustainable development. Since the privatization of public sector does not seam to being these amounts, more attention has to be given to attracting Greenfield and Brownfield investments and other non-privatization methods. Key factor is to have strategic approach to foreign investors, especially those which are ready to intensively participate in transfer of technology and knowledge spillover. For such a strategy to be successful it is required to create competitive advantage for Serbia compared to other transitional countries.

3. The role, opportunities and threats of FDI in the second stage of transition

As in the case of other transition countries, especially those in central and southeastern Europe, Serbia has attracted significant amount of foreign capital in the first stage of transition. According to IMF (2008) liberalization of banking sector has brought large scale capital inflow. Economy development based on high inflow of foreign capital is today more exposed to economic crisis, because high amounts of budget deficit in previous years were cover by foreign capital inflow. In the case of FDI fallout, which is happening this year, macroeconomic problems are to be expected.

Several countries in transition have meanwhile joined EU, and in such a way gained advantage in attracting FDI. Their level of risk is much lower compared to countries which are still in line for EU membership. If we compare the level of FDI in different transition countries we can conclude that there were significant differences among them. Table 4 shows data for period 2000-2007. Unlike several analyses which only cover total FDI per year, in this we show aggregate level of FDI per capita.

Countries which are already members of EU have attracted significantly higher amounts of FDI per capita. It is important to note that Serbia begun with attracting FDI only in year 2000. That was a delay of 0 years compared to other transition countries. It is also interesting to compare country's FDI inflow before and after joining EU. After joining EU all of the countries FDI inflow has risen by at least two times. That is to say that Serbia needs to speed up its efforts of joining EU in order to at least keep present level of FDI.

Depending on the way country manages their increased capital inflows, especially when analyzing inflows raised by privatization of social or state sectors, there are different results in other aspects of the economy like in foreign exchange rates, inflation, GDP growth rate and others. If the inflows were directed to investments oriented to exports, then all negative effects followed by increased foreign capital inflow will be minimized in a long-term. If the funds were used for consumption, then will country face problems because it will not be possible to enter so called “virtual circle” of foreign investments.

Table 4. Inf o of DI n rans on o n r s ar and r a a

									per capita inflow	stock per capita
	2000	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**		
Czech Republic	5404	6296	9012	1863	4007	9374	4752	5000	509	6679
Hungary	2998	4391	3185	1888	3633	6099	4874	4000	239	2600
Poland	10334	6372	4371	4067	10292	7703	11093	12000	667	4005
Slovakia	2089	1768	4397	1914	2441	1694	3324	3000	136	3269
Slovenia	149	412	1722	271	665	445	303	400	488	4059
Estonia	425	603	307	822	776	2349	1282	1300	967	10199
Latonia	447	147	269	270	513	582	1303	1300	568	3083
Latvia	412	499	772	160	623	826	1426	1300	383	2845
Bulgaria	1103	903	980	1851	2736	3103	4104	4000	519	2566
Romania	1147	1294	1212	1946	5183	5213	9082	7000	324	1756
Albania	155	232	143	158	278	224	259	300	95	698
Bosnia	159	133	282	338	534	421	338	400	104	780
Croatia	1138	1502	1197	1785	990	1425	2638	2500	606	5183
Macedonia	189	493	83	84	126	80	279	200	98	1126
Serbia	55	184	504	1204	777	1265	3504	3500	470	1589
Montenegro		5	76	44	53	393	644	600	961	2904
Byelorussia	129	107	262	152	132	245	262	300	33	247
Moldavia	138	115	89	65	120	160	177	200	51	301
Russia	2933	3069	3660	7041	12422	10258	23047	25000	176	1336
Ukraine	644	884	734	1260	1380	6263	4148	5000	107	477

Source: *U□CTAD web page*

As a result of financial crisis, since autumn 2008 world market is experiencing a dramatic shift and decrease of capital inflows in transition countries. In Serbia, except for transfer made for petroleum company NIS, there were no other significant FDIs. According to Petrovi and Vasiljevi (200 , p. 2) the peek in FDI level was at the beginning of 2008. At the same time there was significant increase in budget deficit and increased economic activity. Decrease of foreign investments has shown its first results in loss of value of Dinar compared to all major currencies, increase of inflatory pressures and large decrease in foreign trade. To avoid further cumulative effects, it is necessary to find alternative sources of foreign investments. Government of Serbia has made some positive interventions by signing an agreement with IMF. Depending on use of credit line with IMF, whether it will be used for investments of just for consumption, macroeconomic results will vary.

The role of FDI in sustainable development is not only to increase income. It is necessary to define the political framework and protection of social and natural requirements through investment process. General growth of FDI also brings higher influence of MNC on sustainable development. Multinational companies are strong and effective in spreading new and innovative technologies which support sustainable development (Vuksan, Deli 200). For that reason it is very important to develop a strategy, which will not only attract foreign investments, but which will target MNC that are willing to participate in technology transfer.

The first phase of research of the effects of Greenfield investments in Serbia has shown that despite very dynamic trends and high expectations about future growth of FDI in Eastern and Southeastern Europe, every country has to make attractive investment climate. There is a large competition for attracting FDI among countries because host country, after FDI has arrived, has much more benefits than losses, while the alternative methods of development like savings or crediting from international financial institutions are very risky because of lack of funds fur domestic savings and high debts which arise with credit arrangement for financial institutions, which are very difficult to pay back. On the other hand the state has proved to be very poor investor with misallocation of funds, so that alternative methods of development would most probably have catastrophic economic results, like it was in the era of socialism. For that reason the contract signed with IMF has to be used just for short time crisis overcoming, and not in any case for long term development strategy.

Country with high level of debt is becoming a risky country. Unlike that, foreign investors bring capital, know-how, export channels and new organization culture which applies even in the case local laws do not enforce such practices. For example, no one had doubt that foreign investors will pay their severance pay to employees, which would most probably not be the case with local investors.

As a consequence of the world crisis, withdrawal of foreign institutional investors from the market also happened in Serbia. The first results are visible on Belgrade stock market, most liquid capital market, where Belex index fell by 60%. Followed by that there came the fall of economic activity and increase of unemployment. As recovery period in employment only started after 6 years of transitional unemployment increase, it would bring catastrophic results if the unemployment does not stop to grow. For that reason all institutional measures have to be made, so that after the crisis is over, for the economy to get back to rapid recovery pace.

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RECRUITMENT PRACTICE IN SERBIAN FINANCIAL SECTOR EMPLOYEE REFERRALS AND COOPERATION WITH EDUCATIONAL INSTITUTIONS[*]

Jovan Zubović[1], Azra Hanić[2]

Abstract

In this paper we analyzed the employee recruitment process in Serbian financial sector, with special attention on two frequently utilized methods: the employee referrals and close relationship with educational institutions. At the beginning of the paper the theoretical aspects of the recruitment process itself will be observed by referring to other authors' findings, with an emphasis on two above named methods. In the second part of the paper we will present the results of the research conducted within Serbian financial institutions which will give more insight to recruitment practice in this sector. Special contribution of this paper to the conference is the attempt to prove the existence of established links between educational institutions and the industry through the process of dissemination, which in return guarantees that student after completing undergraduate studies, are equipped with skills needed by employers.

Key words*: recruitment, employee referrals, educational institutions, dissemination*

1. Recruiting process

Recruitment is a process of generating a pool of qualified candidates for a particular job. It begins with identification and attraction of candidates whose abilities, skills and personal attributes meet the requirements for currently unoccupied positions or future jobs (Przulj, 2007, pp.130). The firm announces jobs availability either inside or outside of the organization and attracts qualified candidates to apply.

Recruiting has important social and legal elements and it is one of the most important functions of human resource management departments. Recruitment system is more than a mechanic process of finding candidates and creating database from which the selection should be done. Candidates can negotiate according to their capabilities, education and work experience. Recruiting has its price and requires time. It represents a difficult process, especially if it must be repeated several times in order to attract and find suitable candidates. This process is especially expensive when the supply of work force is small and when there are no sufficient qualified candidates for the job (Torrington, Hall and Taylor, 2004, str.170). Organizations are making decision to search for workers when certain position should be filled due to employee moving to another job within the company, increased amount of work tasks, employee leaving to another company, retirement etc.

Two basic types of recruiting are internal and external recruiting. An organization can fill a position without recruiting new workers through internal sources of recruitment by:

- Work reorganization
- use of overtime work
- work mechanization
- change of working hours
- introduction part-time jobs
- new job design
- internal ads.

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Recruiting from outside the company has a number of advantages, including bringing people with new ideas. Major advantage of external recruitment is that there is a wider pool from which new talents can be chosen. It is often cheaper and easier to hire an already trained professional or skilled employee. External sources can also supply temporary employees who provide the organization with flexibility in expanding and contracting. Hiring externally gives company the advantage of potential fresh perspectives, aspects of problem solving and different approaches. New employees enable exchange of information and transfer of experience from competitors. Sometimes it also makes economic sense to search external specialists rather than to bear the expense of training current workers in a new process of technology.

Disadvantages of external recruiting arise because assess to work of new employees is more difficult and time for adapting and reorientation is much longer. Ethical problems may also arise between new and old employees in organization who believe to be qualified for the position new peers have been employed (Dessler, 2007, str. 76)

External recruitment methods are:

1. employee referrals
2. cooperation with faculties and schools: many organizations cooperate with schools and faculties, giving the scholarships for the best students, giving the chance for the practical job in their companies in order to hire them later
3. hiring agencies: ensures candidates and services of mediation which are usually free of charge
4. private agencies: register unemployed candidates and people who want to change their jobs
5. juvenile societies which can be used for fast stuffing of temporary jobs
6. open applicants data base used for recruits to be called when necessary
7. e-recruitments: due to the fast technology development it is more and more popular to recruit new candidates through internet
8. advertisement **-** which is the fastest and the cheapest way of recruiting.

2. Employee referrals

Very common recruitment methodology is the employee referrals. Studies have shown that employees who were hired trough referrals from current employees tended to stay with organization longer and displayed greater loyalty and job satisfaction than employee who were recruited in other ways. Referrals can be an effective recruitment tool, because employees have a good sense of what it takes to be a successful worker and member of the organization (Ratzburg, 2008)**.** There are some clear advantages to using employee referrals. At first, there is a good chance that company’s current employees know other people in the same line of work. There is also a good chance that the recruit already knows something about firm. In many cases, the present employee becomes successful. This method of recruitment is quick and inexpensive. Companies believe that their employees are more aware of what skills are required for a particular profile. Recruiting candidates trough referrals system results in huge savings as large amounts on advertisements and placement agencies costs are saved. Most referred candidates prefer to work in an organization where they known someone, and have a buddy by their side to help out or guide them trough. Companies reveal that the cost of hiring a referral candidate works out to be 60-70% cheaper than that of going through an external agency and recruitment advertisements (Naukrihub 2008).

In the research Fernandez and Weinberg (1997) compared referred applicants to others, and found that referred had advantages in interviews, better computer and language skills. Fernandez, Castilla and Moore (2000) found that employee referrals had better work histories than non-refferals. Castila (2005) found that referrals were more likely to complete a two-mount training program, and that their performance is much higher. They also received more training due to knowing other people in the company who provided them with knowledge.

The referral programs are made tempting by the employers so that employees are motivated enough to refer people they know to organization. The companies are giving up huge rewards to the employees who bring in candidates, especially for hard-to-fill positions, and award them mostly when the candidate is inducted. The rewards range from cash bonuses to gift coupons and even luxury items. Companies are encouraging their employees to refer candidates whom they know. It also helps in team-building, as it gives employee a reason to feel that they are contributing to the growth of the company. For example Saint Francis launched new employee referral program by which employees may earn up to $2000 by referring a quality external applicant (SFMC).

3. Cooperation with educational institutions

Faculty recruiting is an important source of trainees and potential employees (Fisher et al 1993). To get the best out of this hiring strategy, the organization and its career opportunities must be made straightforward (Richardson). Human resource administrators regard college students and potential graduates as potential employees who know where their careers will take them in the future. The organization that will succeed, then, is the one that can show how the work it offers meets students' needs for skill enhancement, rewarding, opportunities, personal satisfaction, flexibility and compensation

According to Richardson two major advantages of this strategy are the cost and the convenience, since many candidates can be interviewed in shot time in the same location with space and administrative support provided by the college itself. For the organization to gain maximum out of this strategy, it must be first identified what educational institution should be targeted. Selecting a small number of educational institutions which have proven to create satisfactory graduates may be cost-effective. In such a way organization may build its reputation within the educational organization, so that the students are aware of it from the very beginning of their studies. Dissemination process plays a critical role when applying this strategy, and ii brings benefits to both sides, the organization and the educational institution.

This is an important source of recruitment, especially when it is a specific and scarce profession and when previous working experience is not required. Faculties often present different brochures and videos to their students which companies distribute in order to present their way of work. Although the main goal of the company is to find and select good candidates, they are available from this kind of source only once per year. This problem may be solved through pre-contracts or through acceptance of candidates to practical work prior to graduation. There are two main problems related to candidate recruitment from faculties. At first this process is expensive and it takes a lot of effective work time of recruiters. Work plan must be done in advance; evidence of data has to be done by interviews with candidates, and lot of time has to be spent in educational institution. Secondly, recruiters sometimes do not have success due to the bad organization, weak interest of candidates and utilization of inadequate criteria when extricating potential candidates. Students often stay in companies where they have had practical work, if their skills, attributes and abilities meet needs of the job (Analoui, 2007, pp. 144).

4. Role of dissemination

According to Heller (2008) higher educational institutions created adder value by upgrading of knowledge, and for it to bring maximum to society it is necessary to develop strategic customer relationship management (CRM). In that way they would intensify their relationship with industry in order to shift from traditional role of educational institutions which is distribution of human talents to being a partner in deploying those talents. Educational institutions should enter more intense relationship with their environment. They need to identify what are their targets with whom they need to develop new and productive relationships. Among other goals of European programs like Tempus is intensification of dissemination processes. For that reason in this paper we have made an empirical research in Serbian financial industry. We have interviewed 15 out of 71 financial institutions which operate in Banking, Insurance and Leasing activities. These three sector represent 99,8% of total capital of all financial institutions in Serbia, and 15 interviewed organization represent 33% of capital and employ 35% of all employees in these three sectors. Questionnaire covered among others the question of recruitment methods. Table 1 shows the results of the research.

From the research we can see that most commonly used method of recruitment is by one of internal methods. If we look at external methods we need to look separately on different positions in organization. For management positions most commonly used method is employee referrals. For professionals and technicians most commonly used are employee referrals and postings on its web site. For administrative jobs organizations preferably use contacts with educational institutions and for manual labor most frequently employees are engaged by advertisements in newspapers. These results confirm that employee referrals and cooperation with educational institutions are most frequently used recruitment methods. It is interesting to compare these results with the results from the research made in USA which are shown in the table 2.

Table 1. Recruitment sources and methods used by organizations in Serbian financial sector

	Management /Supervisors	Professional /Technical	Administration	Manual labor
Internally	53%	80%	40%	33%
Private employment agencies	40%	27%	0%	0%
Advertisements	13%	53%	40%	53%
Employee referrals	**53%**	**60%**	**47%**	**27%**
Postings on its Web site	27%	60%	40%	47%
Postings on commercial Web sites	20%	27%	20%	20%
From educational institutions	**7%**	**40%**	**60%**	**7%**
Permanent open postings	7%	20%	27%	27%
National employment agency	0%	7%	7%	0%

Table 2. Recruitment sources and methods used by organizations in USA

	Management /Supervisors	Professional /Technical	Administration	Manual labor
Internally	95%	89%	94%	86%
Private employment agencies	60%	58%	28%	11%
Advertisements	50%	54%	6%	7%
Employee referrals	**64%**	**78%**	**87%**	**83%**
Postings on its Web site*	-	-	-	-
Postings on commercial Web sites*	-	-	-	-
From educational institutions	**45%**	**81%**	**24%**	**15%**
Permanent open postings	7%	17%	10%	8%
National employment agency	23%	38%	66%	68%
* No data				

Source: (Schuler et al 2009, pp. 225)

Compared to research made in Serbian financial sector in 245 companies from USA on which the research was conducted, there is significantly higher percentage of internally employed persons. This is due to a fact that analyzed companies are operating for much longer period in a stable organizational culture, unlike organizations in Serbian financial institutions which are in the period of last 9 years operating in rapidly changing environment. Looking at data about employee referrals and links with educational institutions, companies in USA also prefer those methods of external recruitment.

We must note that our empirical research covered only financial sector and in no case we should conclude that these findings apply to all industries. Financial sector has proven to be fastest developing sector in Serbian economy (ubovi , Domazet 200).

As mentioned previously EU programs like Tempus look forward to enhance dissemination between educational institutions and industry. Educational institutions need to define targets for their relationships. Like other organizations, educational institutions tend to depend on timely information. Information is typically communicated poorly between educational institutions and industry. Focus of their activities is insufficiently adding value to the institution's partners. Effective internal communication between departments of the organization is essential to be able to give shape to an external focus on relationships. The educational institution will then be able to switch from being a distributor', mainly focusing on bringing its own product supply to the attention of its target groups, into an institution that takes on the role of partner' in its relationships. In practice in Serbia the program named "Buona" delivered in the period 2007-2009 has proven to establish close relationship between Belgrade Banking Academy on the one side and their target industry, being Serbian financial sector. Curriculum offered is created in cooperation with financial institutions, and the result from this cooperation may be viewed in the results of the empirical research we conducted. Word of mouth is becoming most important source for BBA in enrolling students, and on the other hand, graduated students employed mostly in financial institutions give the best references to their former colleagues during studies. In that way dissemination process became a virtual circle of information which is essential for development of both interested parties.

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IN N I NM N M D PM N IN SERBIA[*]

Marija Lazarević[1], Isidora Beraha[2], Slavica Stevanović[3]

Abstract

Small and medium enterprises (SME) are the leading power of economic development in market economies. The role of development generator is acknowledged by their signifacant participation in employment, export and trade, as well as in creating competitive advantage in global economy .Owning to the absence of appropriate institutional structure and business culture in Serbia, the potentials of SME sector are not fully used. Small and medium enterprises are still facing numerous difficulties in their functioning. Although SME sector currently make up for the largest part of total active companies in Serbia, their contribution to the total national economic development is by far smaller than the one the same sector achieves in the EU states. Therefore, following the examples of other EU market economies, the Serbian government has been implementing significant legislative and normative activities thus enabling further functioning and development of market economy and small and medium businesses. Assuming that necessary measures aimed at creating environment stimulative enough for development of SME sector and entrepreneurship initiative will be undertaken by the government, it is to be expected that SME sector will function more efficiently.

Key words: *business environment, small and medium enterprises, competitiveness, economic policy*

1. Evaluation of SME sector in Serbia

Small and medium enterprises (SME) are becoming the essential part of economic reforms and the crucial factor of industrial restructuring and moving towards market economy. Comprising the importance and the role that SMEs play in overall economy development, our country, by following the model of EU countries' economies, has taken intensive support measurements in order to create environment suitable for development and more efficient functioning of SMEs.

The unique definition of SME still does not exist. The criteria for enterprise classification according to its size are different from country to country, which makes the SME sector's comparative analysis among various economies very difficult, even impossible. The enterprise's classification in Serbia is realized based on three criteria (number of employees, overall annual income and assets value), while at least two of them define the certain category, e.g. the type of enterprise. Concerning the mentioned criteria, the medium enterprise is the entity comprising 50-250 employees, with the total annual income of EUR 2.5-10 millions in RSD (Serbian dinar) and average assets value of EUR 1-5 millions in RSD. Economic entities holding lower values than mentioned are considered as small firms. Besides the above mentioned differences in classification, these firms, no matter where they are or how they function, share similar characteristics, especially high flexibility and inclination to innovative projects. Additionally, all SMEs are facing almost the same challenges: limited access to financial resources, low productivity and specialization, lack of strategic orientation, etc.

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Table 1. Number of enterprises in Serbia (2000-2008)

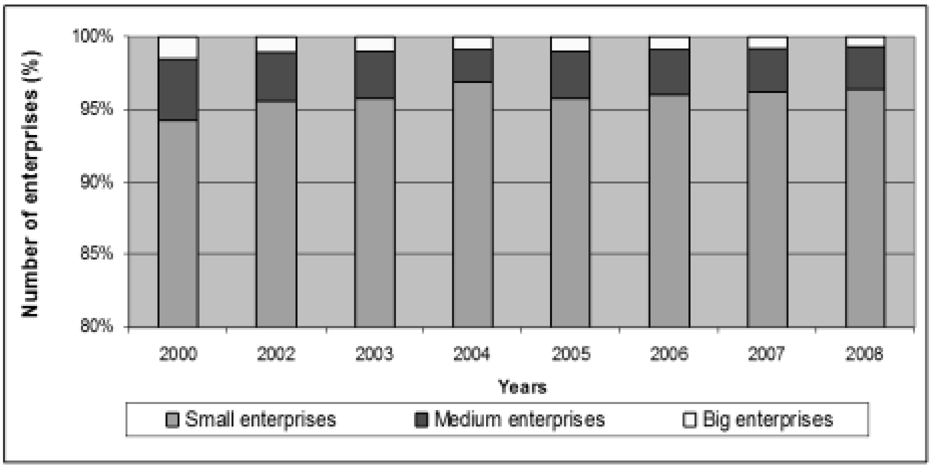
Number of Enterprises	2000	2002	2003	2004	2005	2006	2007	2008
Small	59106	63995	65547	66989	68309	73382	80939	83939
Medium	2616	2223	2181	1515	2292	2347	2572	2572
Big	937	742	663	605	702	665	598	598
Total	62659	66960	68391	69109	71303	76394	84109	87109

Source:*Serbian Chamber of Commerce*

SMEs' share in total number of enterprises in Serbia, as well as their role in economy development, is growing year after year. According to the Serbian Chamber of Commerce, the total number of companies in Serbia in 2008 was 87,109. The SMEs account for 99% of all active enterprises. An increase in the number of small enterprises was the fastest one in the observed period of time. The number of small firms increased by 25, 277 in 2008, comparing to their number in 1999.The average annual small enterprises growth rate was 4.58%. On the other hand, the growth of medium enterprises in overall structure was less intensive and with certain oscillations. The SMEs dominate in almost every sector of the economy. According to the ownership structure, the greatest number of these companies pertains to private sector.

The number of SMEs is growing as a result of government policy aimed at creating business environment which is more adequate and more stimulating for development of small and medium businesses in Serbia. Moreover, a set of new legislation and regulations referring to enterprise's establishment and performing procedures, contributed greatly to the dynamics achieved in the number of new companies.

Figure 1. SME's share in total number of enterprises



The growth of SMEs' share is noticed in almost all activities and aspects of doing business in Serbia. It is estimated that the SME sector currently accounts for 99.7% of total number of companies, participates in 2/3 of total turnover, about 60% in GDP, and 40% in export. According to the results the SMEs have achieved, it can be stated that they are the most profitable part of Serbian economy. The SMEs' participation in overall employment should not be neglected, either. According to the Serbian Chamber of Commerce, the SMEs' share in total number of employees (, 7, 2) was about 54.7 % in 2006. In the same year the majority of employees worked in private sector. The number of employees in SMEs has been growing permanently, and it is estimated that it accounts for 60% of total number of employees in Serbia. The present trend in employment is expected to continue in the following period of time.

The SMEs' activities and obtained results had influenced to a great extent the efficiency improvement of the Serbian economy. In spite of the fact that certain progress has been made, the disposing potentials of SME sector are still not fully used. It is still believed that efficiency of SME sector is primarily conditioned by external factors, particularly by state implemented policies. It is the lack of entrepreneurship initiative and awareness of innovativeness and knowledge importance that makes the contribution of SMEs in Serbia by far smaller than the one the same sector achieves in the EU states. At the other side, economies which based its development on knowledge and entrepreneurship achieved to be on the top of world competitiveness.

Assuming that business environment stimulating enough for SMEs' development will be created in the future, as well as that entrepreneurs' awareness of the importance of strategic thinking and acting will be awaken, it can be expected that SMEs will function more efficiently, achieve better results and contribute greatly to the overall economic development of our country.

2. Business environment analysis in Serbia

Although the initial phase of Serbian economy's transition was very prosperous and the results were certainly noteworthy, especially in the field of macroeconomic stability, there still is a number of obstacles and serious barriers in creation of healthy market economy. The important improvements are necessary in segments which define the quality of business environment in Serbia, and thanks to which Serbia is classified into the group of countries with inconvenient business environment.

The quality of business environment is primarily determinate by factors such as regional environment, employment, fiscal system, institutions (official and unofficial), infrastructure, access to financial resources, macroeconomic environment. After the changes in October 2000, and particularly in the period from 2001 to 2006, the great steps have been made in tracing the way of flexible, liberal and effective business environment in Serbia. The Serbian government realized considering steps forward in transforming business environment by price and foreign trade liberalization, initiating the privatization process, reforms in fiscal policy, banking and financial sector, and implementing tight monetary policy.

Despite certain steps, business environment in Serbia can still be described as inconvenient. In fact, the World Bank's experts in their report Doing Business 200 , comparing the business environment and facilities in 181 country, ranged Serbia at 94 place which is considered as rather disadvantageous position, particularly concerning the ranking of neighboring countries (Romania 47, Slovenia 54, Bulgaria 45, Hungary 41, Macedonia 71), and the fact that in the same report for 2006. Serbia was pronounced the world leader in implementing pro-business reforms.

The European Bank for Reconstruction and Development outlined in its report (Transition Report 2005: Business in Transition) the following obstacles as essential ones in Serbian business: business regulations high cost, low level of institution quality, weak property rights and unstable macroeconomic environment.

The institutional framework of business surrounding in Serbia is characterized by explicit lack of confidence in system of justice and its organs, which are attributed as inefficient and often subject to corruption, and by high cost of legal proceedings. Concerning the criteria of perception of juridical independence and subjection to politician, citizens and firm's influences, Serbia is ranked 0 out of 4 countries (World Economic Forum, Executive Survey, 2007, 2008). The SME is particularly sensitive to justice system efficiency, for they are often subjected to liabilities collection, when the payments depend on juridical assistance. Besides the juridical organs, organized criminal and corruption are important institutional obstacles for doing business in Serbia; nevertheless the certain progress has been made in their restraining.

Economic growth, attraction of foreign direct investments and developed SME sector cannot be achieved without serious institutional reforms. There is a strong and unbreakable connection between legislation reforms and economic development. The SME's development requires simplification and applicable regulations, protection from state and public administration and big business systems, as well as creation of financial institutions' network available for SME's necessities.

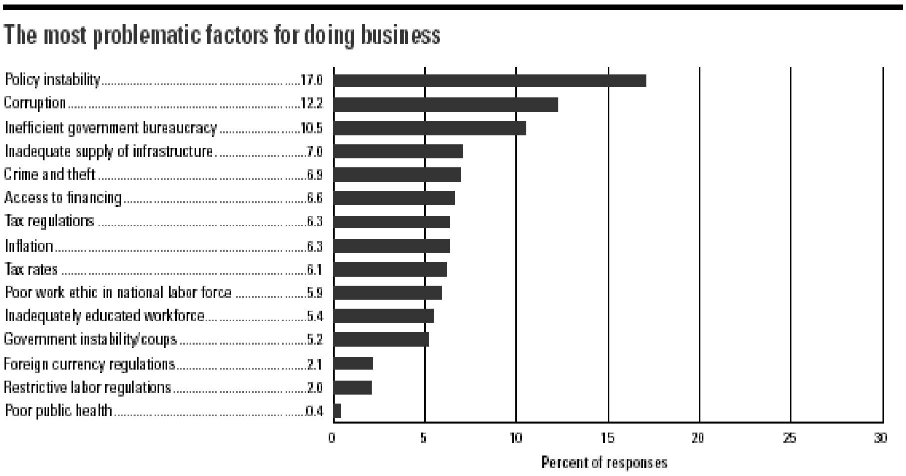
Following the examples of other EU market economies, the Serbian government has taken the initiative and made efforts to create institutional framework for enabling development of SME sector. Concerning the importance of small and medium business for the overall development of Serbian economy, and the fact that SME sector has the greatest contribution to production growth, new jobs opportunities and export expanding, the government adopted the SME's Competitiveness and Innovativeness Development, Business Incubators and Clusters Program for 2009. The government is giving support in education and training, as well, through a number of seminars directed to all target groups, from business secretaries to top management.

Business environment in Serbia is characterized by expressed presence of infrastructural obstacles, primarily in terms of telecommunication services, land access, electric power industry and transport. In a wide analysis of infrastructure quality, presented in the World Economic Forum Report (The Global Competitiveness Report 2008-2009), Serbia was ranked on 119 position, out of 134 countries.

The absence of regulations in property and legal relations has negative impact on business climate in Serbia, and especially on attracting direct foreign investments. The land is state-owned, the property of the Republic of Serbia. As being such, cannot be alienated (excluding the case mentioned in article 84, Law on Building and Planning), but only given for use. The roots of these relations rise from the period after the World War II when property was nationalized, and nowadays are one of key barriers for foreign investors in Serbia. The problems are expected to be solved by new legal regulations and completion of the process of privatization and denationalization, which are contemporary prerequisites for Serbia's accession to the European Union.

The World Economic Forum in its Global Competitiveness Report 2008-2009, as the most inconvenient factors for doing business in Serbia stated fifteen (according to their ranking), as follows:

Figure 2. The most problematic factors for doing business in Serbia



Source: *□orld Economic Forum, The Global Competitiveness Report 2008□2009*

Owning to the fact that problems of SME sector in Serbia are mostly referred to difficulties in providing necessary financial funds for starting up production, buying fixed assets and row material, the government has organized the financial resources' network available to small and medium enterprises. Besides the domestic institutions (Developing Fund of the Republic of Serbia, Developing Fund of Autonomous Province of Vojvodina, a number of commercial banks), SMEs have access to international financial institutions through credit lines (credit lines of the European Agency for Reconstruction, micro credit lines realized through certain banks). The Developing Fund of the Republic of Serbia adopted the Program of Credit Support for Beginners e.g. "Start-up" Credits in 2007, and Micro Credit Program for Employment in 2007, in cooperation with the National Employment Agency.

Although reforms directed to massive and exhausting bureaucracy are developing slower in relation to the ones directed to legal framework, the lack of adequate infrastructure for efficient implementation of new laws is still present. According to the World Economic Forum, Serbia is ranked 102 out of 134 countries, in relation to legal framework efficiency (Global Competitiveness Report 2008/2009). The majority of laws referring to business activities were adopted after changes in the year 2000. The important progress has been made in the following segments: starting up business, bankruptcy regulation reforms, labor force market flexibility and fixed property evidence through cadastre offices.

The Network for business environment improvement has been established in order to enhance business climate in Serbia. The Network activities are focused on business relieving, strengthening the business sector, particularly SME sector, and simultaneously unemployment decrease and living standard growth. The finalization of restructuring and privatization process of social and public companies, together with implementation of current business, management and organization methods will undoubtedly cause the growth of unemployment rate (this rate was 13.5% in 2008). In order to avoid this negative implication, it is necessary to assure faster development and strengthening of the SME sector, as well as opening new jobs.

In years to come the government should systematically, seriously and decidedly engage to improve determinative factors that create business surrounding in Serbia. Only such an atmosphere will facilitate development of the SME sector, as a leading factor of economic development, employment growth, social stability and country welfare.

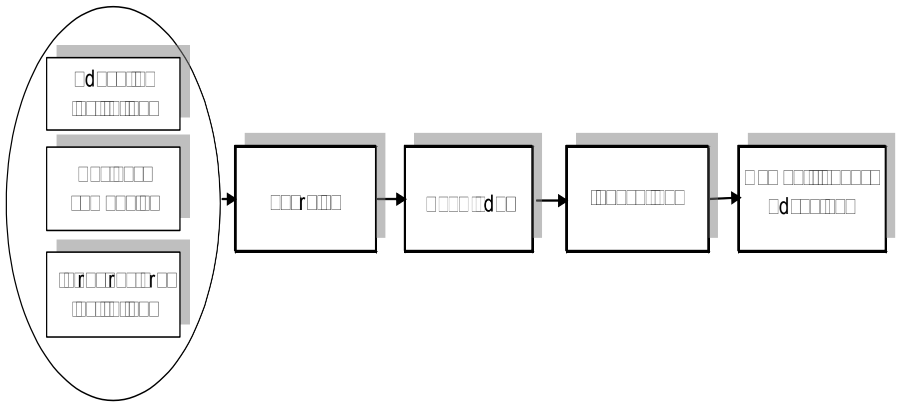
3. The role of clusters in SME's development in Serbia

In spite of the considerable investment support provided by the state during the last years, the small and medium business is still facing great challenges which are limiting their development and competitive advantages improvement. The barriers, such as difficult access to necessary resources (financial, technological, professional staff, information, etc.), the low efficiency in using disposed means, and particularly the lack of strategic orientation, put the topic of defining future development of SME sector in focus again.

Numerous institutional, financial and market barriers in Serbia restrain the SME’s development and functioning. For that reason, the permanent searching for new forms of doing business and management is necessary in order to eliminate or partially levitate the above mentioned restrictions. Clusters, as approved in practice of many developed economies, are effective instrument for SME’s efficiency improvement, and at the same time, they are the way of overcoming certain barriers these systems are facing daily.

As a model of firms’ networking, clusters are becoming the particularly important issue in modern times. Clusters represent the geographical concentration of interconnected companies, of similar or different business. Nowadays there are many examples of successfully organized and efficient clusters. Following Scotland, the pioneer in cluster forming, many other economies, likewise Spain, Italy, Germany, Switzerland, etc. are implementing beneficial cluster policies.

Figure □ Cluster



Cluster's geographic scope can cover either an area of a town, a region, or a number of countries. As a result of that, various approaches can be used when creating and organizing such form of cooperation. Regional cluster, described by M. Porter, is classical, and perhaps the most common type of cluster. Commercial clusters are the second type. They usually gather big companies and represent a form of cooperation based on membership, precisely defined tasks and jointly carried out projects. The third type is called national cluster and it is a cluster of national importance formed by a group of companies and organizations together with government. National clusters are particularly common in undeveloped and developing economies.

Regardless of the type, defining and developing clusters is always very complicated. Forming a cluster requires high – grade cooperation among a number of actors: government representatives, firms (cluster's candidates), financial, educational, and other institutions. Additionally, local governments, regional development agencies and other economic institutions play an important role in cluster's improvement, creation and functioning. Their influence is noticeable in terms of strategic directing, donations, organization of trainee seminars and other services aimed at creating business culture favorable for clusterization.
A cluster's success depends on a number of factors, especially on a level of environment development, characteristics of its members, and presence of entrepreneurship spirit. Knowing how efficient clusters are in strengthening SME competitiveness, it is necessary to enhance and intensify their forming in Serbia.

Understanding the importance of such form of business cooperation *The Ministry of Economy and Regional Development* has defined the long-term "Cluster Development Support Program". The realization of the Program has already started and will be completed by the end of 2011. The Program is being carried out trough the following stages:

- First stage: Preparation and cluster establishment (2005-2006.)
- Second stage: Cluster stabilization and growth (2007)
- Third stage: Strengthening operational capacities and current clusters commercialization (2008)
- Fourth stage: Strengthening links with international business network, common innovative projects, etc (as of 2009).

The Program is expected to gather SME, scientific and research institutions and business associations in order to enhance economic growth, increase employment and export promotion. Twenty clusters have been formed so far, out of which four are in the third stage of development: Automotive cluster of Serbia – AC Serbia (cooperation between 22 firms, 5 scientific institutions, 8100 employees), Serbian software cluster (including 11 firms, 4 scientific institutions and 1200 employees), BIPOM cluster - Balkan and Black Sea industry of agricultural machinery (joining 15 companies, 5 scientific institutions, 701 employees) and Flower producers cluster (including 68 firms, 3 scientific institutions and 350 employees). The other ones are in various industries: tourism, food - processing industry, engineering, shoemakers, etc.

Successful cooperation within a cluster form will benefit mutually to SME sector in Serbia. United with other institutions, SMEs have better access to new knowledge, financial resources and information exchange. Belonging to a cluster eliminates SME's most common problems, creates potentials for gross production (gross economy), and strengthens its negotiation power and competitiveness.

Conclusion

Contributing significantly to employment, export and competitiveness, SMEs have confirmed its role of basic turning point in development of EU market economies. Owing to its flexibility, inclination to innovative undertaking and risk, these companies are faster and more efficient in adjusting to market and in fulfilling consumers' necessities than the large ones.

The role of SME in overall development of Serbian economy had been underestimated for a long period of time. As a result of that, appropriate development policy was never adopted. In the year 2001 great social and economic reforms were undertaken, which significantly improved the situation. Despite the fact that certain improvements have been made, the potentials of SME sector are still not fully exhausted.

It is clear that the creation of competitive economy, based on knowledge, innovativeness and quality, e.g. elements and advantages possessed by SME, requires certain changes in factors by which business environment is determinate.

Only by assuming that the government will manage to create business environment convenient and stimulating enough for development of entrepreneurship initiative, it can be expected that SME sector will function more efficiently and will have greater contribution to the overall development of Serbian economy.

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THE ROLE OF OFFICIALLY SUPPORTED EXPORT CREDIT INSURANCE IN ITALY AND SERBIA RECENT DEVELOPMENT AND FUTURE PROSPECTIVE

Periša Ivanović[1]*, Jelena Vapa-Tankosić*[2]

Abstract

This paper presents a conceptual framework for the strategic management of government export credit agencies in developed and developing economies. The framework, which analyzes the traditional role of Export Credit Agencies (ECAs), integrates the new models („quasi–market player-QMP“) and strategies targeted at a better export performance and assistance. This article describes the existing ECA model in Italy (SACE Spa) as one of the potential guidelines for the development of Serbian ECA (AOFI a.d.). It further analyses the relevant Italian practice and emphasizes the need for providing support to export companies by programs of export insurance and financing. It gives recommendations for the future development of Serbian export trade programs supported by the State through export credit agencies.

Key words*: government export credit agencies, SACE Spa, quasi–market player, export credit insurance, political and commercial risks, AOFI a.d.*

1. Export credit agencies as a state strategic tool

An export credit is a form of trade finance, a loan issued by a Government Export Credit Agency to finance exports. An export credit may be extended to a domestic exporter or foreign importer: in either case it allows the final purchaser to defer payment. Moravcsik[3] outlines that export credits are the "financial lubricant" of international trade. On the other hand, export credit insurance can cover the commercial risk, which is provided and priced on a commercial basis, and political risk, which can include currency non convertibility and transfer restrictions, confiscation or expropriation, import license cancellation, breach of contract by a government buyer, and political violence which cause the non-payment by an importer. Deutsche Bundesbank[4] research proves that high correlations of risks in an export credit portfolio and strong time-varying risk exposures constitute characteristics of export credit risks that make them different from other (industrial) risks and challenge the insurability of export credit risk.

According to the special study of the World Trade Organization[5] the aggravated asymmetric information problem in international trade (especially in countries with less developed financial systems), and the inability/unwillingness of commercial banks to take on certain economic and political risks (especially for large, long term trade contracts) is often seen as an economic justification for government involvement in trade financing. Government support for trade finance relies on export credit agencies (ECAs). ECAs can generally provide various forms of trade financing, generate and provide information, serve as a forum for government and industry lobbying towards contract fulfillment by foreign governments and traders, and protect against risks.

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Export credit agencies function as a strategic tool in the hands of the state to promote trade borrowing from the State treasury or public capital markets and using the funds to finance exports. The basic role of an ECA is to support and encourage exports and outward investment by providing financial support, through insuring or guaranteeing international trade and investment transactions and, in some cases, providing loans or finance directly. Their traditional role was of the insurers of last resort against political risks and commercial risks that were not deemed insurable by private markets. Today, in the light of increased pressure on the ECA in regard to the fulfilling the aim of the long term profitability and covering operational risk (losses) ECA operations must be cost-covering (including losses under normal economic condition), and governments must provide a guarantee for operations on the government's account.

ECAs support the expansion of trade thorough reliable, adequate, and cost-effective sources of financing, both long-term and short-term. They deal with the market of several segments according to maturity, from short-term (usually 0 to 180 days, but possibly to 360 days) to medium and long-term. The medium to long-term end is generally considered to be over two years, and is subject to the OECD Arrangement on Guidelines for Officially Supported Exported Credits (the Arrangement)[6] when insured or guaranteed by a Participant to the Arrangement.

Export credit insurance has been initiated as a government program. Subsidized export crediting and state insurance provided for export credits were first introduced in the beginning of the 20th century as a tool to promote the recovery of world trade after wars. Gianturco[7] points out that the first agency was the United Kingdom's Export Credits Guarantee Department (ECGD) established in 1919. Other developed countries followed in the 1920s and 1930s. In 1933 the US Eximbank was created and in the period following World War II most countries created their own export credit guarantee instruments. In 1961 the Foreign Credit Insurance Association was formed to insure U.S. exporting companies against defaults by foreign buyers and political risks. The FCIA was originally an association of private insurers operated in cooperation with the Export/Import Bank of the United States, an independent government. The private insurers underwrote the commercial risks while the Eximbank covered the political risks, until the private sector withdrawal from operations left Eximbank to cover both risks.

The Berne Union[8], a unique organization of export credit agencies that promotes best practices and information exchange, was established in 1934. Today 51 organizations from 42 countries participate in the Berne Union and they cover 10% of global trade which amounted to 1.4 trillion dollars up in the year 2007.The aims of the Union that their members accept "sound principles" in the export credit sector and practice and respect the Union's regulations and to cooperate in creating a favorable climate for the growth of export credit and foreign investments.

To this end the members of the Union are committed to:

- exchange information with each other and with the Union so that it can accomplish its tasks consult each other regularly on an ongoing basis for the purposes of research, enterprise, and participate in projects;
- cooperate closely and where appropriate take coordinated action;
- -work with other international organizations, particularly with so-called IFIs (FMI, World Bank, Regional Development Banks).

After the Second World War, other developing countries set up their own agencies, and many transition economies did so as well in the 1990s (Table 1). The growth of international trade since World War II was much faster than the expansion of world output while trade in goods has grown by an average 6 per cent a year in real terms, whereas world merchandise output has increased by 3.9 per cent a year. Today the major ECAs include Export Credits Guarantee Department (ECGD) of the United Kingdom, Export-Import Bank of the United States, Euler Hermes of Germany, Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE) of France, Sezione Speciale per l'Assicurazione

[6] Arrangement on Officially Supported Export Credits, www.oecd.org
[7] Gianturco D. (2001), p. 41.
[8] www.berneunion.org.uk

del Credito all'Esportazione (SACE) of Italy and International Trade Policy Bureau, Nippon Export and Investment Insurance (NEXI) of Japan.

Table 1. Timeline of ECA Development

1910s	1920s	1930s	1940s	1950s
UK Germany	Netherlands Norway	US Mexico Switzerland Sweden	Canada Austria France Italy	Japan Finland Belgium India Israel South Africa
1960s	**1970s**	**1980s**	**1990s**	**2000s**
Hong Kong	Australia Denmark Korea Taiwan Portugal Spain Sri Lanka	Egypt Jamaica Turkey China Indonesia	Nigeria Colombia Romania Thailand Philippines Malaysia Hungary Bosnia Slovenia Slovakia Bulgaria Czech Repub- lic Poland Singapore Brazil	New Zealand Pakistan Africa Yugoslavia Macedonia Vietnam Bangladesh

2. SACE - From traditional insurer to innovative market player

Servizi Assicurativi del Commercio Estero or SACE was founded in 1977. as the commercial and industry policy instrument with the aim of providing support for the exporters who were dealing with less developed markets with information asymmetry and significant failures. The main business of SACE, as of most export credit agencies, is insurance of finance provided by exporters or banks. Insurance policies provide for SACE to reimburse the lender for losses up to a certain percentage of the credit covered and under certain conditions. Lenders or exporters pay a premium to SACE. Insurance policies protect the lender against political or transfer risks in the borrowing country that prevent the remittance of debt-service payments.

Today SACE is a leading Italian insurance and credit management company. The company offers insurance cover in more than 150 countries and at present insures commercial transactions worldwide for an overall outstanding value of approximately 7 billion. In addition to traditional credit insurance, SACE provides integrated credit management solutions such as political risk insurance, sureties, financial guarantees for commercial and financial transactions and cover for project & structured finance. The holding company SACE S.p.A. is rated by Moody's with Aa2 and stable outlook.

Table 2. SACE Group Key Figures[9]

n	At 31/12/2007	At 31/12/2006	At 31/12/2005
New guarantees	23.614	17.364	12.993
Gross written premium	312	241	198
Claims paid	50	44	74
Net Profit	377	510	757
Shareholders' funds	5.572	8.724	8.591
Outstanding guarantees	37.055	31.980	24.352
Employees	511	463	445

SACE achieved a significant improvement of all main economic-financial indicators in the last four years. It is important to stress out is that SACE guaranteed assets are zero weighted under Basel I and under Basel II. SACE's support is fully backed by the Italian Government and provides longer tenors and all-in cost of funding. It provides transfer of risk and improves company's balance sheet composition.

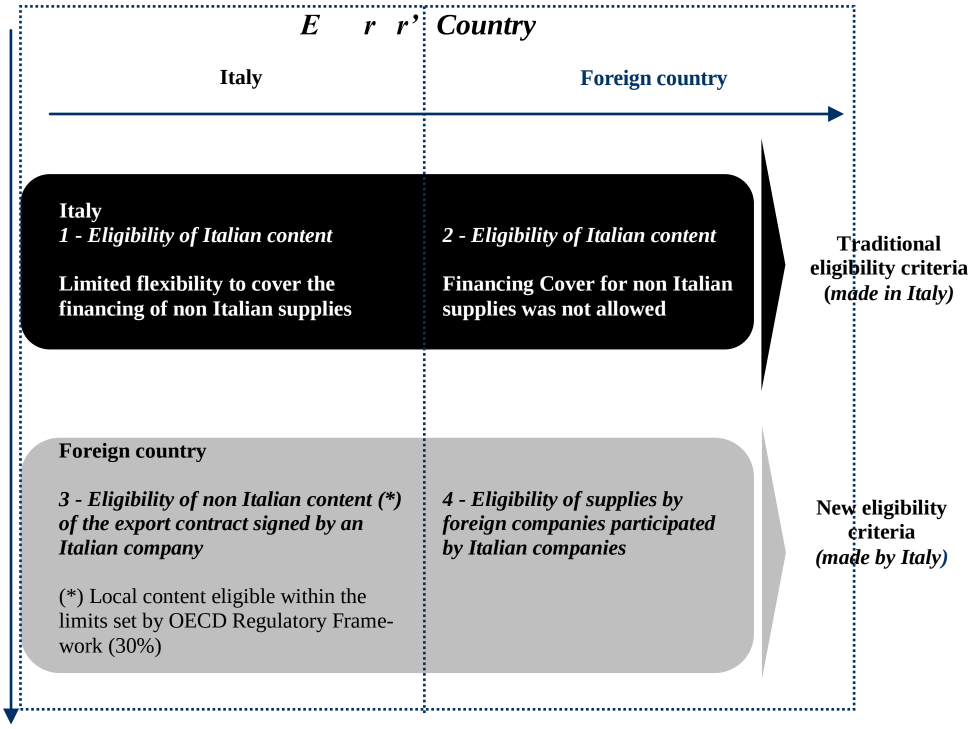
From its' beginning SACE has traditionally acted as "an insurer of last resort". Ascari[10] points out in the mid-nineties SACE resulted burdened with claims, with a bad reputation, staff lacking skills and motivation, and not so good control on future risks. SACE, like other ECAs, has been insurer of the last resort of the monopoly regime without a direct quest for profit. Its' business model was purely connected to the national product and national exporter. The government at that time even raised the issue of SACE closure.

In the second part of the nineties the Italian State took the strategic decision to hire new management with the task of stabilizing the situation by limiting new commitments, introducing better evaluation processes and reforming the governance. These measures proved themselves extremely fruitful and as a result this created a framework for revived growth. A long term development business plan had to be based on a solid institutional foundation and a new business model was introduced in the year 2000. This model had brought the following strategic and management changes:

- new recruitment effort & training & remuneration package (MBO system);
- customer satisfaction comes first & improved quality of the services;
- new set of products & diversified product range;
- new modern risk techniques & better pricing policies (price-to-risk);
- new corporate governance & policies in line with best market practices.

[9] www.sace.it
[10] Ascari R. (2007) Is Export Credit Agency a Misnomer, The ECA Response to a Changing World, SACE Working Paper No. 02.

Picture 1. Traditional eligibility criteria (made in Italy) vs. new eligibility criteria (made by Italy)



Pursuant to the Law enacted in 2003 and effective January 1, 2004, SACE became a limited liability joint stock company whose shares are wholly owned by the Ministry of Economy and Finance. Under this new structure, SACE continues providing medium- and long-term official export credit insurance and began to provide short-term insurance on its own account through the subsidiary company SACE BT in accordance with the new EU regulation on State aid.

2007 Budget Law further enlarges SACE’s operational scope and range of insurable parties in order to further strengthen Italian economy and interest:

- loans granted **to import raw materials or semi manufactured good** used to export goods/services or to improve production processes of Italian firms benefiting Italian economy;
- loans granted **to build infrastructure (also domestic)** to support Italian economy internationalization such as transportation (highways, railways, ports etc..) or utility facilities (oil & gas pipeline etc..);
- loans aimed at **supporting Italian bank system abroad** in order to increase its competitiveness in international markets;
- loans granted for **Italian interest transactions** such as environment, tourism, logistics etc.

As shown in the Picture 2 the historical business of sovereign risk insurance has almost disappeared, and it has been able to enter into entirely new transactions such as large structured and project finance deals.

Picture 2. SACE portfolio structure[11]

The greatest change was that now SACE transformed its market approach turning it into a proactive approach both in seeking new opportunities in the traditional segments but also in penetrating new markets. This commercial attitude had nothing in common with the traditional old monopolistic public Agency. Yet, the transformation would not be possible without an institutional mandate that allowed the flexibility needed to follow the market and the skills of the SACE staff to implement it.

3. Export credit insurance policy in Serbia

Since the year 2000 and the breakup of the Socialist Federal Republic of Yugoslavia, exports from the FRY accounted only for US$1.7 billion compared to US$5.8 billion in 1990. Foreign trade volumes as a percentage of GDP had declined significantly, and trade deficit was widening. The whole economic situation was in chaos having in mind the limited access to finance, poorly managed banks, high perception of political risk, poor public infrastructure. All this issues have increased the difficulties for exporters to compete in foreign markets, regain lost markets, and/or identify new buyers. Exporters did not have any kind of support for their activities since the domestic banks did not have the financial status and the credibility necessary to support exporters in international markets. Foreign companies or banks would not accept to take a risk of non-payment by a domestic enterprise or bank, thereby preventing exporting enterprises from importing materials essential to performing export contracts. In particular, guarantees issued by Serbian and Montenegrin banks were not deemed acceptable by overseas buyers or bond-giving banks.

The export credit agency (ECA) of the FRY did not survive the structure of the former regime system since JUBMES has been converted into a commercial bank (JUBMES a.d.). Exporters and banks have been deprived of the highly specialized financial products (such as credit insurance) that are available to all developed and most developing countries in the world.

The first step was taken by establishing SMECA (Serbia and Montenegro Export Credit Agency) by the Law on Export Insurance and Financing Agency passed on 18th January 2002 by the Parliament of the Federal Republic of Yugoslavia (Official Gazette of FRY No. 3 dated 18th January 2002). Funding for SMECA operations as an export-credit agency was provided from the World Bank loan and the donation from the Italian Government. The Development Credit Agreement was signed between the World Bank and the Government of the Federal Republic of Yugoslavia on 31st October 2002 and became effective as of 28th August 2003, after all the requirements from the Agreement had been met. The amount of the loan was SDR 9.100,000 under IDA conditions. The Italian Grant Agreement for the donation given by the Italian Government in the amount of USD 8.920.714 was signed at the same time as the Development Credit Agreement. Based on these two Agreements, the World Bank and SMECA signed the Project Agreement, which defined the responsibilities of SMECA as the implementing agency.

[11] Baldacci (2007) Mercati globali, "unbundling" della produzione e supporto all'internazionalizzazione, Convegno "Le Banche di Credito Cooperativo nel processo di internazionalizzazione delle PMI italiane. Ruoli e prospettive", Roma.

According to the report of the World Bank[12] the project was designed in order to support exports through the following facilities:

- Export credit insurance, to cover a seller against the loss arising from the failure of a buyer to pay for goods sold and delivered (or services rendered) to that buyer whenever the insured seller is not in default under the terms of its contract to supply the goods (or render the services);
- Working capital loans and guarantees, to provide working capital to domestic exporting enterprises;
- Exporter performance insurance, to support all the types of contracts where the buyer requires some kind of a guarantee, covering the exporter's performance, such as guarantees covering tenders, advance payments, and performance obligations by exporters; and
- Medium term import insurance/guarantees, supporting the import of machinery to be associated with export activity.

Imports were to be facilitated through the following facilities:

- Political risk insurance, to attract foreign entities making investment or extending credit to domestic entities, by mitigating their perceived country risk; and
- Limited comprehensive import credit insurance, to support a domestic enterprise to acquire machinery - on medium payment term - predominantly used to produce goods for exports, thus facilitating the supply of essential inputs to the Yugoslav industry.

SMECA also provided credit information on domestic and foreign exporting enterprises and financial institutions that facilitated economically viable transactions, both import and export activities.

The second step was taken by establishing AOFI[13] for the "promotion of national exports" by a Law approved in July 2005 with an initial capital of 25 million. AOFI received for the growth, in the year 2006. and 2007, of its activities funds out of the state budget. The total amount of funds the State determined for exports is currently EUR 40 mil. AOFI has supported 13.3% of total Serbian exports in 2007 and 10.8% in 2008. being concentrated on financing export transactions, while SMECA focused on short term commercial risks insurance and factoring.

As per the comparison of their strategic orientation, AOFI is authorized to provide a similar range of activities to SMECA. AOFI, as a young institution, focuses on short-term lending, factoring, short term commercial and non commercial export insurance with a perspective to become an export credit agency that offers further export-tailored products. AOFI currently provides export insurance against commercial risks and short-term loans either directly to the exporter or through a bank. In addition, AOFI charges interest rates on terms that are more favorable than those charged by commercial banks (mainly because AOFI is not subject to the mandatory 45% reserve requirements for commercial banks).

Both of them are involved in all exports branches from food-processing, processing and metal industry. AOFI and SMECA support private and public companies. They service the main exporters in Serbia as US Steel Serbia, Tigar, MSK, HIP Petrohemija Pancevo, Impol Seval from Sevojno, Tarkett Sintelon, Dijamant, Hemofarm Concern, Trayal Korporacija, Alfa Plam, Valjaonica Bakra Sevojno, Sojaprotein, Livnica Kikinda Cimos, Kuzman, Apatinska Pivara, Concern Swisslion Takovo, Delta M, Metalac and Tetrapak Production.

It is important to stress out that the Serbian Government in the year 2008 has adopted national Export Promotion Strategy[14] for the period from 2008 up to 2011**.** This involves defining and prioritizing the most significant economic branches as well as setting the export target markets. For the Serbian exporters it is imperative that the Government has the foresight and expertise to implement their strategy.

It is a fact that both institutions have been based on different business models. SMECA has been working on market principles, not using government funds and not issuing guarantees against political risks. This is a restrictive condition for the SMECA and one of the reasons why SMECA will be

[12] World Bank (2008), p.5.
[13] www.aofi.rs
[14] http://pks.komora.net/Portals/0/Inoaktivnosti/08042008StrategijaPovecanjaIzvoza.pdf

merged into AOFI. The main characteristics of the Export Credit Agency in the industrious and developing economies that they have their the government support and act in the name and on behalf of the Government for the insurance of export non- commercial risks. During the year 2009 SMECA will be merged into AOFI but the specifics of the merging process have not yet been revealed. The State through a new merged institution should provide the exporters highly specialized financial products (such as credit insurance) and easier access to export loans with similar conditions as in other countries. As for the future merger, it is expected that this move will constitute a stronger and more efficient approach for the State support of the Serbian exporters.

4. Recent development and future perspectives

The changes in the global economic and financial environment and the increasing role of the private sector in the economy are among the factors calling for a change in the export credit insurance business model. It is important to stress that the European Union has taken a regulatory action by restricting ECA activities to non-marketable risks (in contrast to marketable risks). According to the European Union Commission Communications marketable risks comprise[15]:

- Normal commercial risks of private debtors;
- Political risks on public and non-public debtors in the EU and in certain OECD countries (Australia, Canada, Iceland, Japan, New Zealand, Norway, Switzerland, USA).

At the same time non-marketable risks comprise:

- Catastrophe risks (war, revolution, natural disasters, nuclear accidents and the like);
- Commercial risks on non-OECD countries;
- Political risks on non-OECD countries.

The rationale behind this decision is to eliminate distortions of competition in the export risk insurance market, where private insurance companies are expected to cover (for example short-term business to OECD core members) the demand at reasonable risk premium. In this way, ECAs are restricted from short-term public export guarantees that aim at covering export risks to OECD core members with a maturity of less than two years since 1998. Export business with duration of over two years can still be insured by ECAs. Increasingly, ECA operations must be cost-covering (including normal losses), but governments provide a guarantee for operations on the government's account.

Following this framework many ECAs from developed countries have recently been forced to strategically rethink their business models due to several factors**,** such as[16]:

- Financial subsidies have been eliminated from OECD ECA medium- and long-term systems as a result of official export credit disciplines put in place over the last 20 years at the OECD;
- Private insurance companies have become main competitors that now dominate in the insurance of short term risks and increasingly operate also in the medium-long term segment;
- International capital markets have become more sophisticated, interrelated, structured and converge towards banking industry;
- Globalization has resulted in complex supply chains, with virtually all capital equipment having some significant amount of foreign content;
- In the last years, non-OECD ECAs, such as those in China and Brazil, have emerged as major players in medium- and long-term business while operating without the constraints of the OECD Arrangement.

All these factors has led to new business models and to ECAs' new governance and ownership structures. As shown in the Table 3 there is no single business model. Countries have adopted various approaches to support exporting firms. The traditional model prevails in the US (Exim), in Japan (NEXI), and UK (ECGD). The models of private companies operating also as state agents are profit-seeking private insurance providers. They also operate as government agents with state guarantee (or re-insurance) in markets where the private sector cannot or is not willing to operate (e.g., MLT risks in

[15] www.europa.eu.int
[16] US Export-Import Bank (2007) Report to the U.S. Congress on Export Credit Competition, Export-Import Bank of the United States, Washington.

EMs). The main examples are Euler Hermes, COFACE, and Atradius. At the same time third differentiated model is the intermediate model. This model implies export credit companies with a private-sector business model. The state is the major or only shareholder. The company supports domestic firms' internationalization while ensuring adequate returns to the public capital (e.g. SACE, CESCE, ONDD and GIEK).

Table 3. ECA traditional and new models[17]

Models	**Government agencies with mandate to support national interest**	**Private companies na ona ad rs operating also as state agents**	**Intermediate model**
Strategy	Support national interest	Market oriented export credit insurance	National interest program and traditional business
Ownership structure	The state is a major shareholder	Private shareholders	The state is the main shareholder with minor private shareholders
Risks	„non-marketable" risks	Split of activities: -national account „non-marketable" risks -commercial account "marketable risks"	-National interest program "marketable risks" -traditional business „non-marketable" risks
Examples	**US EX-IM (SAD) ECGD (GB) NEXI (Japan) EFIC (Australia)**	**Euler-Hermes (Germany) Coface (France) Atradius(Netherlands)**	**SACE (Italy) OND (Belgium) GIEK(Norway) CESCE (Spain)**

Conclusion

The field of traditional export credit support has significantly altered in the last years due to global trade and financial integration, structural transformation in real sector, current shortage of liquidity and confidence on financial market and enhanced regulatory framework. The globalization and the financial crisis have radically increased the interdependence of countries leading the developed and developing countries to review their trade policy and implement state backed trade policy measures which rely on promoting export through export finance. New financing instruments have been developed, international risk assessment has improved, and cooperation on co-financing especially large projects has developed. Trade finance instruments help reduce trade costs thereby generating additional export and FDI and allow firms to focus on core activities (including by freeing resources for R&D and product quality upgrade). ECA traditional products support trade in long-term operations and new products introduce "made by" concept and call for better risk management.

The active inclusion of export credits within the rules of the WTO has pushed ECAs to consider that, unless they can demonstrate that they intend to manage and operate on a long-term breakeven trajectory with market-based pricing, they may be subject to litigation. Globalization of sourcing options has translated into companies becoming multinational in form and creating more competitive supply chains, irrespective of their primary domicile. Further, as buyer countries become more developed, there are other alternatives to export credit and there is an increase in competition between some ECAs and the private sector in search of attractive returns to meet their profit objectives. In response to these new challenges, several ECAs have been operating more like the private sector in terms of how and where they do business (e.g., higher income markets) and redefining the equation for determining "national benefit" by extending support to goods produced by a national company in another country.

[17] Vapa-Tankosi J. (200) Savremena tr i na strategija agencija za osiguranje i finansiranje izvoza, Fakultet za ekonomiju i in enjerski menad ment, Novi Sad.

This article has shown that the role of ECAs has changed over time from the basic "insurer of the last resort" to global market player. Still, a key premise behind government-sponsored export credit insurance schemes is that they will serve to boost exports. While the structure of ECAs varies from country to country, virtually all operate in close cooperation with their national government, and most operate with government financial support of some type. Serbia has opened, step by step, its market to international trade since 1990, after a long period of import constraint. Serbia is involved in a continuing process of reform, adapting its policy instruments and institutions to achieve the objectives of continued growth in conformity with the adopted national Export Promotion Strategy. Serbia's agency is still relatively young and it can profit from experiences of Italian agency which, as shown in this article, has been able to gradually move from an old traditional model to a quasi market player. On the basis of the above mentioned, every individual state as well as Serbia, having in mind the existing ECAs models on the market, should constantly review their existing model and optimize their function for the best support of Serbian exporters and for promotion of nation exports.

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FOREIGN DIRECT INVESTMENT AS A FACTOR OF ECONOMIC GROWTH AND DEVELOPMENT OF THE SERBIA*

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Abstract

In the globalized economy, foreign direct investment (FDI) represent one of the key factors of the country development. For an invest destination, FDI means new job creation, export stimulation and in general, that presents the generator of economic growth and development. Until 2000, Serbia was not an attractive destination for foreign investors, but after the democratic changes, the country became one of the most atractivness European destinations where the volume of FDI have noted a large expansion. The global economic crisis, that reduced the volume of FDI inflows, also affected their inflows in Serbia and the other countries of the same region which among the other factors, led to a significant slowing down of the economic growth, and other adverse macroeconomic consequences. The paper describes the analysis performed and the scope and structure of FDI in Serbia in the period after the democratic changes of 2000. It determined a positive relationship between the volume and structure of FDI and economic growth and development of Serbian economy. Inflow of FDI is the factor that had a large impact on the rapid economic growth, as well as the establishment of macroeconomic stability. Notwithstanding the positive impact on employment and the growth of budget revenues as well as the significant acceleration in the growth and development of a number of branches, such as the banking system, telecommunications, and other activities. Also, we have found factors that will in future have a key influence on the scope and structure of FDI in Serbia.

Key words*: foreign direct investment (FDI), Serbia, economic growth and development, the world financial crisis.*

Introduction

The foreign direct investments (FDI) involves a capital investment by company or individual to carry out profitable activities in the territory of one country. In today's world economy, foreign direct investments are the fastest way of the development of a country and region and, as such, are welcome in the most developed countries of the world as well. Foreign investors may be a company whose seat is abroad, a foreign natural person and citizen of Serbia residing abroad more than a year, and the highest number of foreign investors in Serbia comes from the European Union and the United States.

The division of foreign direct investment can be made according to several criteria. One of them can be division on the primary and special shapes. According to this criteria, the basic forms of foreign direct investment includes: the establishment of companies (Greenfield investment) and the acquisition of majority shares owned by the existing companies (the purchase through the privatization, share purchase or direct purchase of property shares - acquisition). As special forms of foreign direct investment are considered: concessions, B.O.T. (Build-operate-transfer), business (approval of foreign investors to build and use the facility or plant, as well as infrastructure and communication facilities,

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with the obligation to transfer ownership to the state by the end of the contract). One of the classification of foreign direct investment, which comes from the World Bank, is the division according to the motives for investment. This division can be very useful, because in this way the target group of investors can easily be determined. According to this division, there are: investments that require resources, investments that require market, investments looking for existing capacities in order to maintain and promote long-term goals of own company (they are facing, first of all, privatization, and acquisition, because by purchasing one of existing companies they keep production program and existing market).

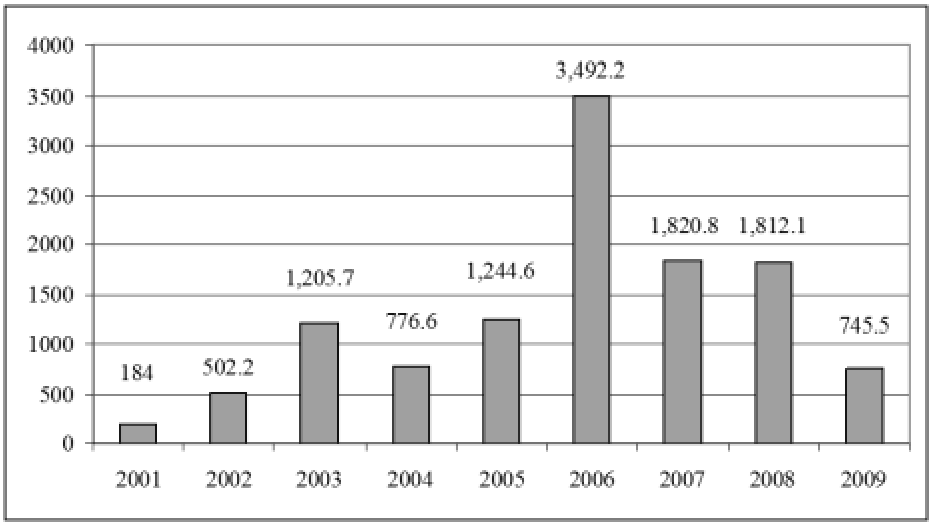
The division of foreign direct investment can be done in other ways. However, it is important to understand that each company has different reasons for making decisions about where and how to invest. Whether one foreign company decide to invest capital in one country depends on many factors, and, above all, the estimates of profit that can be made, long-term of business, and the readiness of the host country to accept, speed up and facilitate business. Thus, each state is to create a good investment climate, and clear and stable framework for business to attract the best companies.

FDI are now one of the basic mechanisms of the globalization of world economy, taking the role of the key factor of development of each state. For a country in which are invested, foreign direct investment means new jobs, increase exports and, in general, initiation of economic growth and development. On the other hand, direct investment, as a form of investment of foreign capital, enable the investor to acquire ownership, control and management on the basis of invested capital. In addition to new markets, investments in other countries can also mean faster and better supply of raw materials, electricity, easier transportation, or access to free economic zone. Because the goal of the paper is description of the FDI as the factor of economic growth and development of Serbia in the first step analysis of volume and the structure of FDI in Serbia in the period after the democratic changes of 2000. year is carried out. After that, at the positive link between FDI and economic growth and development of serbian economy is pointed out. As well as their impact on employment and the growth of budget revenues as well as the acceleration of growth and development of a number of branches. At the end, it is pointed out to some of the factors that will have a significant impact on the scope and structure of FDI in Serbia in future, and especially in the world financial crisis.

1. Foreign direct investment in Serbia volume and structure

Since the onset of economic reforms in 2001, Serbia has grown into one of the premier emerging investment locations in Central and Eastern Europe. To date, FDI inflow in the country has exceeded $17 billion. The scope of FDI in Serbia noted, until 2006, mainly significant growth rates to the year and had its peak (that year the net FDI amounted to EUR 3.49 billion), and later under the influence of political instability in the country, and after that the impact of world financial crisis that took hold of Serbia, came to the significant fall.

Figure 1. Foreign direct investments in Serbia, net, in million EUR (2001–2009)



Source: *MoF*

Serbia's strong FDI track-record is substantiated by internationally recognized awards for local Greenfield investors. Between 2004 and 2006, Greenfield projects in Serbia were awarded by OECD as the largest investments of this type in South East Europe. The first Award was presented to Ball Packaging Europe (headquartered in USA), followed by METRO Cash & Carry (Germany), and Israeli Africa-Israel Corporation/Tidhar Group for their Airport City Belgrade real estate project.

In terms of the country structure, investors from the European Union lead the way accounting for about 85% of the total FDI influx. The top spot on the country list is held by Austria, followed by Greece, Norway, Germany, and Netherlands, while significant investment also stems from the United States, Slovenia, France, Great Britain, and other world's leading economies. The actual amount of U.S. investment is significantly higher than the official figure due to their companies investing primarily through European affiliates. This also holds for Slovenia, Italy, Israel, Belgium, Russia, and a number of other countries.

Table 1. Net FDI in cash by countries (2000-2008)

Country	Investment value ($000)	Country	Investment value ($000)
Austria	2,633,585	Italy	753,942
Greece	1,687,437	Switzerland	305,283
Norway	1,556,700	Montenegro	296,134
Germany	1,477,990	Croatia	296,407
Netherlands	1,063,757	Bulgaria	133,897
Slovenia	655,439	USA	133,409
France	503,618	Slovakia	67,692
Luxembourg	445,654	Latvia	53,659
Hungary	353,479	Israel	48,155
Great Britain	295,291	Belgium	63,947

Source: *NBS and SIEPA*

According to the NBS in the period January-March 2009 net FDI in Serbia amounted more than $ 805.8 million, of which the largest part belong to Russia ($ 511 mill), and then follows Austria ($ 115 mill) and Switzerland ($ 40.9 mill).

Over the past five years, service sectors have proven to be the most attractive to international investors. The financial sector recorded the biggest FDI inflow of $ 5,2 billion, with telecommunications holding the 2nd spot with $3.1 billion, while manufacturing sectors ranking 3rd with $2.77 billion.

Table 2. Inward FDI by industries in mill USD (2004-march 2009)

Industry	Total investments
Financial intermediation	5,193.4
Transport and telecommunications	3,107.2
Manufacturing	2,773.6
Real estate, renting	1,954.5
Wholesale, retail, repairs	1,909.6
Mining and quarrying	576.1
Construction	345.4
Agriculture	119.2
Hotels and restaurants	93.2
Electricity, gas, and water	89

Source: *□BS*

Table 3. Leding foreign investors (2002-2009)

Company	Country	Industry	Investment type	Amount (EUR mill)
Telenor	Norway	Telecommunications	Privatization	1,602
Gazprom Neft	Russia	Energy	Privatization	947
Philip Morris	USA	Tobaco	Privatization	611
Mobilkom	Austria	Telecommunications	Greenfield	570
Intesa San-paolo	Italy	Banking	Acquisition	508
Stada	Germany	Pharmaceutical	Acquisition	475
AB InBev	Belgium	Food	Acquisition	427
NBG	Greece	Banking	Privatization	425
Mercator	Slovenia	Retail		240
Fondiaria SAI	Italy	Insurance	Privatization	220
Lukoil	Russia	Energy	Privatization	210
Airport City BG	Israel	Real estate	Greenfield	200
Block 67 Ass.	Austria&Serbia	Real estate	Greenfield	180
Holcim	Switzerland	Construction	Privatization	170
OTP Bank	Hungary	Banking	Privatization	166
Carlsberg	Denmark	Food	Acquisition	152
U.S. Steel	USA	Metail	Privatization	150
METRO	Germany	Wholesale	Greenfield	150
Coca-Cola	USA	Food	Acquisition	142
Lafarge	France	Construction	Privatization	141

Source: *SIEPA*

The list of leading foreign investors is topped by world-class companies and banks, such as Telenor, Gasprom Neft, Fiat, Philip Morris, Mobilkom, Banca Intesa, InBev, and many others.

2. The impact of FDI on the previous and future development of Serbian economy

The effects of current FDI inflows are proportional to their modest scale, in which Serbia share the experience of other transition countries. FDI have followed the process of privatization, and most placed in the take over of existing firms. A smaller part refered to greenfield investments, and it started to grow only in the past few years . By the end of privatization such a relationship will be detained. As is shown, most of the FDI is placed in the service sector: banking, trade, telecommunications, tourism and catering, business services, distribution of petroleum products. In the manufacturing sector, FDI is placed in the primary and secondary processing of metal and non-metals, the exploitation of mineral water, food industry, production of beer, milk and milk products. Past effects of FDI inflows to the Serbian market and the economy can be summarized in the following: buying the market before buying production capacity, market distortions (oligopoly in wholesale distribution and hypermarket chains, banking, manufacturing cigarettes, beer, coffee, milk and milk products; monopoly in the production of steel), and a growth of competition as well, increase exports, and imports (most important: U.S. Steel Serbia); begining of greenfield FDI oriented on export at foreign market, creating a modest vertical connections with domestic firms; taking over management knowledge of the local successful companies; rudiments of involvement of local ICT companies in the international production and distribution network.

Insufficient use of the potential positive effects of (modest) inflow of FDI in the Serbian economy can be explained by: taking over of companies in the privatization process, spending privatization revenues on social needs and imports, the concentration of FDI in the service sector, high technology gap betwen serbian economy and the developed world, low absorption capacity of domestic firms to assumption the new technology and knowledge; unstable political and legal system, and unfinished institutions.

The specific impact of FDI on growth and development of serbian economy can be best viewed using the movement of some macroeconomic indicators of the serbian economy in the period after the democratic changes and substantial initialization of the transition, as it is given in the table below.

Table 4. Republic of Serbia - Basic macroeconomic indicators in the period 2001 - June 2009

	2001	2002	2003	2004	2005	2006	2007	2008	2009
Gross domestic product, in millions EUR	12,820.9	16,033.7	17,416.4	19,075.0	20,358.0	23,520.6	29,542.7	34.2591	30.8631
Gross domestic product, per capita, EUR	1,708.7	2,137.8	2,328.2	2,555.9	2,736.0	3,173.5	4,002.2	4.6511	4.1901
Gross domestic product, real growth, in %	5.6	3.9	2.4	8,3	5.6	5,2	6,9	5,42	-2,01
Consumer prices, period average	93.3	16.6	9.9	11.4	16,2	11,7	7.0	13.5	9.1
Export of goods	1,922.2	2,870.4	2,441.0	2,831.6	3,608.3	5,102.5	6,432.2	7,428.3	2,254.4
Import of goods	4,759.2	5,956.6	6,585.5	8,623.3	8,439.2	10,462.6	13,506.8	15,580.5	4,495.1
Foreign trade deficit	-2,837.0	-3,754.7	-4,144.3	-5,791.7	-4,831.0	-5,360.1	-7,074.5	-8,152.1	-2,240.7
Current account deficit (excluding donations)5	977.0	-1,842.7	-1,674.8	-2,688.4	-2,050.0	-3,091.8	4780,96	-6,086.2	-990.3
Current account deficit (excl.donations), % of GDP	-7.6	-11.5	-9.6	-14.1	-10.1	-13.1	-16.2	-17.8	-
Balance of payments, total5	559.9	981.1	813.5	360.2	1,627.6	4,316.1	742.1	-1,714.6	-213.6
Foreign direct investments, net, in million EUR	184.0	502.2	1,205.7	776.6	1,244.6	3,492.2	1,820.8	1,812.1	745.5
Foreign currency reserves of NBS, in million EUR	1,325	2,186	2,84	3,117	4,935	9,025	9,641	8,16	8,914
Citizen savings, million EUR, end of period	329.8	812.9	1,099.6	1,464.6	2,274.7	3,414.1	5,028.5	4,881.0	5,02
Employment level, average (thousands)	2,102	2,067	2,04	2,051	2,069	2,026	2,002	1,999	1,977
Unemployment level, end of period (thousands)	-	-	-	-	896	916	785	728	768
Net wages - real growth rates	16.5	29.9	13.6	10.1	6.4	11.4	19.5	3.9	2.4

Source: *MoF*

You should bear in mind that between the implementation of FDI and its effect on economic growth, there is a certain time delay. It is a consequence of the fact that the period of time is needed in order to activate investment, which means that in the coming period significant effects as a result of activation of current FDI can be expected. Both variables, the net inflow of FDI and value of nominal GDP of Serbia shows a similar trend. GDP and net FDI of Serbia shows a strong, high and positive correlation that exists between these two variables, which is in line with accepted economic theory about positive effects of FDI inflows on economic growth which is the main conclusion based on the idea that the inflow of FDI provides high quality transfer of technology and know-how and, increasing productivity in the recipients of FDI inflow. High inflow of FDI had significant effects on the growth of deposits and consequently on the development of the banking system and capital markets. Effect on the growth of deposits was a two-sided. On the one hand as a result of sales of companies the part of received money is puted in the banking system in the form of deposits. On the other hand through the process of foreign investment in the Montenegrin market, credible foreign companies had come that have become a significant customer of the banking system as a depositor and as a loaner. The process of foreign investment had a significant effect on the budget. The process of foreign investment influenced on the one hand the growth of economic activity and the growth in tax revenues, and on the other hand significant number of job places is saved through the process of foreign investment. Altought, FDI had some negative effects. Thus, for example FDI directly affected the growth of deficit of current account balance of payments. On the one hand it is a consequence of accelerated development, because foreign investors made additional investments in companies that they bought, in order to increase their level of competitiveness.

After a period of time, this investment should have significant positive effects on economic growth. The second course was a consequence of the fact that a large number of individuals significantly increased their level of living standards by selling shares. In such conditions there was a significant increase in consumption of cars, household equipment and the like. They are durable consumer goods that are not produced in Serbia, so the result was the growth of import. Interrelationship between foreign direct investment and imports is not specific only for Serbia, but also for other economies in transition

Conclusion

It is undivided positive opinion about the importance of FDI for the successful transition of former socialist countries, and Serbia as well, and their growth and development. It is undoubted that they have a large positive potential. Will it be used, depends on many factors. The main conclusions about FDI and its effects can be summarized as follows: FDI have a strong development potential: first, they are an additional inflow of investment capital, particularly important for countries that have a small rate and volume of domestic savings, secondly, they start a new economic activity or increase existing in the manufacturing or service sector; third, one of the most important effects is the overflow technology, knowledge and productivity.

In general unfavorable conditions, in which Serbia already is, it is difficult to design and implement a successful development policy. One of the ways out from the difficult situation has been, for some time, is seen in the stronger attraction of FDI. It is counted on the undoubtedly potential beneficial effects of their presence. In accordance with the results of numerous empirical studies on the effects of FDI on the domestic economy and the effects of incentives policy, remains in force recommendation that the good governance in the area of FDI policy to consider the package of measures of investment incentives as part of the overall industrial policy of the country, and every incentive to make available under equal conditions to all investors, both foreign and local. Stimulus should be focused particularly on those activities that create the strongest potential for overflow, including the links between foreign and local firms, education, training, R & D.

On possible benefits and damage of the presence of FDI in the Serbian economy should be looked to objectively, consider the experience of others. There are examples of one and the second, and successful and unsuccessful. Investors are managed by their logic, and the FDI per se have a neutral sign. Where will they be able to be placed, and how, depends on the domestic legal system and business environment. They do not come with ready solutions, and potential benefits of their presence may be materialized only by domestic firms.

At the end it should be awared that the positive global conjuncture had large impact on the movement of foreign direct investment. The appearance of the global financial crisis that affects a large number of business firms, throughout out whole world, and that will lead to negative effect of welfare will inevitably have a negative effect on attracting foreign direct investment in the coming period.

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BUSINESS AMBIENT AND ENTREPRENEURSHIP IN SERBIA REALLY AND POSSIBLE[*]

Slavenko Grgurević[1]

Abstract

Democratic revolution in the year 2000, happened at the changing of the centuries and millenniums, found Serbia in the conglomerate of cacophonic ideas, interests, paradigmatic visions, that were at the same time support and restriction for the creators of the strategies and complex program of stabilization – transition of the Serbian economy. That is the reason why IMF and World Bank characterized, in their official report, progress and application of the reforms in Serbia as unequal, and atmosphere and ambient in which reforms are applied were politically unstable, also without base in values, from standpoints of civilization standards. In general, these financial institutions think that there were some important movement in the field of macro-economic situation, liberalization of prices and exchange rate, and quite partly in restructuring of state and public sector and regulatory frame that defines business ambient.

Positive macro-economic effects that are significantly important for developing business ambient: relatively stable exchange rate of dinar and inflation under control – are hardly sustainable on the long run in the circumstances of high public expenses and deficit of foreign trade balance. At the same time, industrial production stagnates with a little hope for the long-term revitalization and announced structural changes. Therefore, the real question still stays open: how long it is possible to keep stability of the rate of prices, as well as import-export balance, i.e. deficit – without new production and significant rise of the export? Development of entrepreneurship initiative is significantly restricted and it is reflection of general situation – non-stimulating business ambient. Further on, the text shall include evaluation of the situation, as well as of perspective and possibilities for creation of the stimulating business ambient in Serbia.

Key words: *stabilization, transition, IMF, World Bank, business ambient, rate of prices, deficit, entrepreneurial initiative.*

1. Economic trends in Serbia early in 2009

The negative economic developments in Serbia in the conditions of global financial crisis have not evaded similar tendencies characteristic for all transition countries. Limited supply of capital, increased prices of loans, reduced demand and insolvency crisis. Also, the inflow of foreign investments has been reduced, and the conditions for obtaining cross-border loans have been aggravated.

According to the data from polls carried out by the Union of Employers of Serbia (UPS) and the Chamber of Commerce of Serbia (PKS), the net inflow of foreign direct investments early in this year was $650 million ($509 million from the sale of the national oil company)[1]. In the following text we will point out some key moments.

1.1. Demand

Foreign demand has been decreased from the EU countries, Russia, countries in the region. Reduction in demand is variable, somewhere between 10 - 100 %, depending on the economic branch that the companies are dealing in. The companies from the area of ferrous and non-ferrous metallurgy have recorded decrease in demand from the USA, and those in metal and electric industry even from Nigeria, Morocco and Algeria, which leads to the conclusion that a decrease in demand has been recorded also in underdeveloped countries, in which the Serbian export was only symbolic.

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Certain companies have noted increased demand from the countries in which decrease in demand is otherwise characteristic: the EU countries, Russia, countries in the region. At company level, an increased demand has also been registered from Ukraine, Georgia and Slovakia (food industry), Japan and Saudi Arabia (forestry and wood and timber industry), Switzerland, Germany, Russia and Bulgaria (ferrous and non-ferrous metallurgy), and Russia, USA and Middle East (chemical, pharmaceutical and rubber industry).

1.2. Production

On the basis of data from the poll, the anticipated decrease in industry production is in the range of up to 75% (construction up to 30%; agriculture and food industry up to 25%; forestry, wood and timber industry and paper industry up to 60%; metal mines, ferrous and non-ferrous metallurgy up to 50%; metal and electric industry up to 75%). It is worth mentioning that the data from the polls by UPS and PKS are approximate to those from the National Bank of Serbia, as in the time period between January and February of 2009, the industry production has been reduced by 18.7% compared to the same time period in 2008 (and in February it was reduced by 22% in comparison with the 2008 average)[2].

1.3. Employment

A decrease in employment of up to 50% is anticipated, although the unemployment rate in Serbia is 14.8%, according to the official statistic data. Forced and unplanned vacations, as well as reduced working hours in the duration of up to one year, are all means in which the employers in Serbia see the possibility to postpone the drastic solution of firing the workers, whose number otherwise is higher than the necessary number of employees.

1.4. Solvency

The problem of insolvency is nothing new in Serbian economy, and it has been specially emphasized since the last quarter of 2008, and the great risk is specially emphasized under the conditions of extended terms for payment. According to the data from the poll, the problem of insolvency is completely visible in all companies in the fields of forestry, wood and timber industry, ferrous and non-ferrous metallurgy. In other industry branches it is somewhere up to the level of 90% (food industry – 90%; construction industry - 80%; chemical and pharmaceutical industry - 87%; metal and electric industry - 70%). According to the data from the National Bank of Serbia, the total number of the companies unable to fulfill their financial obligations has been increased by 30% in comparison with 2008.

1.5. Foreign exchange

The total Serbian foreign exchange of goods with other countries in the first quarter of 2009 has been reduced by 36% in comparison with the same time period in 2008. If we take a look at individual countries, during the first quarter of 2009, most goods were exported to Germany ($182 million), Italy ($116 million), Bosnia and Herzegovina ($117 million) and Montenegro ($100 million), and imported from Russia ($334 million), Germany ($231 million), Italy ($183 million) and China ($177 million). In the export structure, the most represented are reproduction products (60%), general consumption goods (30%), equipment (10%). In the import structure are reproduction means (60%), general consumption goods (25%) and equipment (15%). Surplus has been achieved in exchange of goods with B&H, Montenegro and Macedonia, and the greates deficit has been achieved in the exchange with Russia, due to the importation of energy substances.

1.6. Bank investments and foreign exchange schedule

The loan activity of banks in December 2008 was reduced by 1.1%. in comparison with the investments in the same year. According to the data from the National Bank of Serbia, in the first quarter of 2009 the total bank investments have been increased by 5.7% in comparison with the end of 2008. Moreover, the loans to the population have been increased by 3.8% and the loans to the companies by 6.8%. A reason to worry is that in the first quarter of 2009, an average weighed interest rate on bank loans amounted to 20.95 % at the annual level, which is by 12.6% higher than the interest rate recorded in January 2009. At the same time, a constant increase in an average weighed interest rate on the bank deposits has been recorded, from 4.33% as it amounted in January 2008, to 7.6% in January 2009. In February of the same year, this interest rate amounted to 8.39%.

The foreign currency reserves of NBS in the first quarter of 2009 amounted to 8.2 billion EUR (an increase has been achieved thanks to the inflow from the privatization of the national oil company). Still, the foreign currency reserves of the National Bank of Serbia at the end of 2008 amounted to 8.15 billion EUR, which means that they were reduced by 892 million EUR in the last month of 2008, and during the whole of 2008 the foreign currency reserves were decreased by 1.5 billion EUR. The dinar has nominally lost its value compared to the euro in the first quarter of 2009 by 5.5% during the same time period, the nominal effective exchange rate was depressed by 8.3%. The Serbian currency nominally grew weaker in comparison with the euro during 2008 by 10.6%, while the nominal effective exchange rate was depressed by 11.8%.

1.7. Economic trends - summary

On the basis of previous general data, it can be concluded that the current economic developments show decrease in import and reduction in the domestic demand, which has led to a decrease in industry production. Especially negative for the economy is the reduction in export orders to the biggest exporters, as this will be reflected in reduction of their procurements from the domestic suppliers, as well as in the decrease in demand in the services sector, especially in the cargo transportation. With purpose of reducing the costs, forced vacations have been introduced in certain companies, in order to adapt the number of workers to the reduced production capacities. As a consequence of these circumstances and uncertainty as to the scope of the crisis and its duration, purchase of permanent consumption goods has been decreased, as well as other goods with elastic demand due to the decrease in expenditure and postponement of planned purchases. This will have a negative effect on the production in the following time period.

Although, within the measures taken by the Government of the Republic of Serbia, in order to stimulate demand (through loans with subsidized interests), an increase in loan applications has been recorded – the expected effects on the economy have not occurred as yet.

According to the poll carried out by UPS and PKS, the employers point out that the crisis has only emphasized teh numerous problems and limitations for business activities which had existed before as well. Generally a limitation for employers is lack of favourable loans, and this is especially felt in the fields of construction industry, food industry, ferrous and non-ferrous metallurgy. According to the same data, the employers think that the adopted measures for the increase in economy solvency are only a partial response to the needs of the economy, and that they can have only short-term positive effects. The adoption of a comprehensive program and strategy for surmounting the crisis has not occurred. The greatest risk for the banking system is the high share of loans with foreign currency clause. Due to insufficient export and the obvious decrease in export demand, as well as the high loan risk that the citizens are exposed to – a great depreciation of dinar may lead to currency risk turning into the loan risk, i.e. lead to increase in uncollectable claims and decrease in bank assets. The currency risk also poses a substantial limitation for planning business activities within the economy, but there is no doubt that the higher macroekonomical risk is the public expenditure that is too high and not harmonized with the level of economic development in Serbia. Under these conditions, it is very complicated to lead a policy of stimulating economic development and providing macroeconomic balance. Therefore, the so far adopted measures are different, and even contrary to the measures adopted in other countries, especially in the EU.

2. Entrepreneurship in Serbia: some aspects

2.1. General

The political circumstances and business environment are not stimulating the development of MSP (small and medium companies) in Serbia. The slowness and lack of thorough reform initiatives have caused the initial transitional difficulties to last, which supplements the decades-long negative heritage, which distances Serbia from global integration currents.

The numerousness and the status of active commercial entities (300,000 small and about 15,000 larger firms with 1,200,000 employees) is followed by the almost zero economic efficiency of Serbian companies (where the expenses are larger than revenues), contrary to the conditions in developed countries, where rentability is above the level of 10%.

The problem of economic efficiency is even more complex, as the small companies account for 95% of the total number of firms and absorb 54% of the employed in Serbia. These are the main reasons which place Serbia within the small group of the least developed countries in Europe.

2.2. Limitations

The main limitation to the development of young entrepreneurship in Serbia can be explained in the following way:

1. The institutional framework is unsatisfactory (although certain developments have been made – Labour Act, Company Act, Law on bancruptcy proceedings, Law on mortgage and Law on Business Registers Agency), because the legislatory solutions in direct function of developing small entrepreneurship have not occurred (Law on handicrafts, systemic governing of free interest organization of employers, definig norms for real influence of employers over the adoption of all commercial regulations, harmonization of standards in the production and services with the EU standards).

This actually calls for a dominat influence of the employers over the economic and overall social circumstances in the country. A special problem is the real institutional suport to establishment of small firms. Namely, the existing institutional network (employment services, agencies for development of MSP, commercial associations, certain economic services etc.) - have no practical influence over the development of small entrepreneurship. In fact, their support is limited to partial provision of help to potential entrepreneurs when establishing new firms and counselling concerning the development of the existing ones (seminars and individual consultations), which sometimes lack quality.

2. The current tax policy, although modernized compared to the situation before 2000, is CLEARLY DISCOURAGING for employers. Namely, the tax plocy should be simplified and adapted to the realistic payment capabilities of commercial entities. In doing this, the relationship between the tax burdens and accumulation must be carefully balanced, so that in practice it can enable both functioning of the state and the development of commercial entities. In practice, this means that the state should URGENTLY rationalize the tax burdens for the users, and to lead the tax policy primarily for the benefit of development of commercial entities, in order to enrichen the tax base not only for the not only for the overall expenditure, but also for the common expenditure.

3. The present situation of the financial support to the foundation of entrepreneurial firms is quite unfavourable. Therefore it is worth mentioning that the National Employment Service provides certain financial support for self-employment and new employment, buti its overall scope and individual sums that are allocated on that basis are not sufficient to substantially stimulate foundation of small firms and acceptance of new workers. Certain developments in this direction, through the financial support to self-employment which started in 2005 and are exercised through the Development Fund of the Republic of Serbia, have not in their scope substantially influenced the decrease in current unemployment. The situation is similar in the financing of development of active employers. Namely, certain state funds (primarily the Development Fund of the Republic of Serbia, Development Fund of AP Vojvodina and some regional funds) attempt to seriously contribute to the development of employers by granting short-term and long-term loans at lower interest rates and longer „grace" periods, but the main problem are still the unsurmountable difficulties in obtaining bank guarantees, having in mind their strict criteria and primarily the lack of legal acts on the protection of private property, i.e. the dominant situation that the available mortgage property is not recorded in the books.

Therefore, the banking system which is nowadays dominated by foreign banks, grants loans to employers with extremely high costs (interest rates and other burdens), which are far above the level of discount rates (of about 10%) and which in practice amount to over 30% in short-term and over 15% in long-term loans. Here it should be added that, due to the internationall announced high legal insecurity and risk for doing business in Serbia, the foreign partners now very rarely decide to make direct investments, which is drastically obvious under conditions of the global financial crisis.

4. Finally, the foreign donor support to the development of private entrepreneurship after 2000 is certainly welcome, but its scope is practically negligible. It primarily includes financing the reform of secondary-school education, and foundation of entrepreneurial „incubators", as well as some programs for development of innovations and training of the unemployed by the entrepreneurs. More detailed analysis of the effects that such donations have, first of all shows the small scope of these financial assets, and uncritical incorporation of foreign experiences in those areas, not taking into account the existing transitional differences and undeveloped entrepreneurial tradition.

2.3. Analyses based on polls

All of this is showing us that the current conditions for the development of free entrepreneurship in Serbia are very difficult in comparison with the conditions of the same kind in the developed countries, and the same as in other transitional countries. This is also confirmed by the results of polls carried out by the Union of Employers of Serbia on the sample of 1,657 pollees (owners of small firms structured in two groups: a) micro firms with up to two employees; b) mini firms from 3 to 49 employees). Namely, most of them (924, or 57 %) stated economic necessity ar the reason for foundation of their own firms (Table 1). This answer actually shows us that our active employers have started their businesses not because of favourable business conditions and their entrepreneurial potential and motif, but simply because of existential necessity – which, of course, questions their real potential in relation to the requirements of doing business in the said, very difficult business conditions.

Previous statement on the employers' motives is indirectly confirmed by the further results of the poll which concern the industry structure of small entrepreneurs in Serbia. Namely, in relation to the entire population of pollees, the dominant number of them (1,121, or 69%) have chosen service business, especially trade (Table 2). The reason for that is certainly the fact that these industries do not require large starting investments.

This also confirms the previous statement, according to which the great majority of our potential employers enters the small business primarily counting on their own very modest material basis, thereby not expecting any financial support from state funds, commercial banks and other financial institutions. In a word – small entrepreneurs in Serbia decide to start their business aware of the difficulties in the overall business conditions, but primarily with an intention to secure their own family existence, thereby counting on their own unknown etrepreneurial capabilities and unsistematically acquired business knowledge - which is actually indicating the still present great limitations which the current business conditions impose in relation to the real status of the employer function in Serbia.

The polls carried out by the Union of Employers of Serbia show us the basic causes for the unfavourable results that the employers have achieved and which are above all related to the unfavourable business conditions (Table 3, i.e. large tax burdens, difficult loan-making for the development and the accompanying legal insecurity in doing business - 918 or 60%). The rest of pollees (612 or 40%), state as the reason the unfavourable material status of the employers as regards equipment and current assets, which is mostly also in relation to the impact of the difficult business conditions which still last.

For the above reasons, the pollees think that the increase of economic efficiency of employers in Serbia can be achieved first of all by improving the overall business conditions, in combination with the improvements in business competences of employers and their workers.

Conclusion

As opposed to the developed countries, and the successfull countries in transition, where the MSPs are a socially cohesive factor, the business environment in Serbia in not stimulating the development of MSPs. Their economic situation is in a permanent degression which is confirmed by long-term negative trends manifested through economic inefficiency of MSPs in Serbia: In 2005 - 2009, the loss rate is higher than the profit rate and the ratio between the loss and capital is higher than the ration between the profit and capital, and finally, loss per employee is higher than profit per employee... Is there an end to this?

The absorption power of MSPs from the point of view of employment in Serbia is estimated at 500,000 – 700,000 of new workplaces in the period of next 3 – 5 years, of course under circumstances of a stimulating environment and sustainable growth, which is so far only a vision, while we are waiting for concrete institutional solutions, elementary political stability and responsibility of the authorities in Serbia.

Tables

Table 1. Reasons for which the pollees have decided to start firms

Offered answers	Micro firms		Mini firms		Total	
	Number	%	Number	%	Number	%
a) economical necessity	549	58	375	55	924	57
b) material gain	250	27	143	21	393	24
c) social status	15	2	47	7	62	4
d) other reasons	125	13	120	18	245	15
Total	939	100	685	100	1.642	100

Source: *The poll carried out by the Union of Employers of Serbia*

Table 2. Ind s r s a o s f r s d a n

Offered answers	Micro firms		Mini firms		Total	
	Number	%	Number	%	Number	%
a) production	38	4	69	10	107	7
b) services	728	78	393	57	1121	69
c) combined industry	167	18	224	33	391	24
Total	933	100	686	100	1.619	100

Source: *The poll carried out by the Union of Employers of Serbia*

Table 3. Basic reasons for the employers' unfavourable results

Offered answers	Micro firms		Mini firms		Total	
	Number	%	Number	%	Number	%
a) unfavourable economic situation	378	43	234	36	612	40
b) large tax burden	405	45	252	39	657	43
c) difficult conditions for loan-making	54	6	92	14	146	10
d) legal insecurity	42	5	73	11	115	8
Total	879	100	651	100	1.530	100

Source: *The poll carried out by the Union of Employers of Serbia*

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ATTRACTIVITY OF THE BALKAN COUNTRIES FOR THE FOREIGN IVESTORS*

Srdjan Redžepagić[1], Gordana Vukotić-Cotič[2]

Abstract

What is already well-known in the literature of economic sciences, it's reality that the fall of the Berlin Wall, at the end of the year 1989, symbolically marked the beginning of the transition from the socialist system towards the market economy. Little after this historical event, the communist political régimes made enter the Central and East European Countries (CEEC), the Baltic States and the Commonwealth of Independent States (CIS) in a new – well-known era according to the expression "the era of post-socialism". The governments of these systems urged the reforms necessary to make "pass" these socialist economies towards savings in capitalist type and as soon as possible pass to a new political and economic system founded on the democracy and the free market. The transition in some Balkans countries was late. The conditionality, the strategy, sequentially, the preliminary prospects and results form the profile of transition in the majority from the Balkans countries. Principal factors of the (late) transition are grouped in a complex of the political, social and economic factors, which they ambivalent are – their external and internal effects are obvious. An institutional vacuum limits the complex particularly, with a significant influence on the political aspects and of the transition. An analysis of the two groups of interlaced factors is useful as the bases for the manufacture of a projection of the future dynamics of course and reform in Serbia. The various scenarios are present in this article.

Key words: *investments, transition, Balkan countries, integrations*

Introduction

What is already well-known in the literature of economic sciences, it's reality that the fall of the Berlin Wall, at the end of the year 1989, symbolically marked the beginning of the transition from the socialist system towards the market economy. Little after this historical event, the communist political régimes made enter the Central and East European Countries (CEEC), the Baltic States and the Commonwealth of Independent States (CIS) in a new – well-known era according to the expression "the era of post-socialism". The governments of these systems urged the reforms necessary to make "pass" these socialist economies towards savings in capitalist type and as soon as possible pass to a new political and economic system founded on the democracy and the free market.

The transition in some Balkans countries was late. The conditionality, the strategy, sequentially, the preliminary prospects and results form the profile of transition in the majority from the Balkans countries. Principal factors of the (late) transition are grouped in a complex of the political, social and economic factors, which they ambivalent are – their external and internal effects are obvious. An institutional vacuum limits the complex particularly, with a significant influence on the political aspects and of the transition. An analysis of the two groups of interlaced factors is useful as the bases for the manufacture of a projection of the future dynamics of course and reform in Serbia. The various scenarios are present.

An increase or a reduction in the dynamics of transition is conditioned by the elimination of the negative impacts of the political and economic factors, i.e. by the promotion of the positive aspects of the solutions. In Serbia, for example, the growth is strong, inflation made a point (highest), and political uncertainties weakened. But the total economic developments suggest that the remainders of the economy of Serbia incompetents to provide the growth robust with inflation and, at the same time, to keep

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the external balance of payments overdrawn at the bearable levels. One waits until the gross domestic product (GDP) continues to increase with 6-7 percent during years 2008-2009. However, the growth remains too dependent on the activities "non-tradable" (banking operations, purchases, communication…), whereas exports do not follow the imports of increase. The prospects for growth are prone also at the risks of fall of the external courses, because the overflows of total financial agitation could increase the costs of foreign placement and lower an external request. Two factors which were absent in Western Balkans turbulent, stability and regional co-operation, are now recognized like line of rescue to prosperity and seem to be truly realizable.

If the countries of this area (in particular Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Montenegro, Romania and Serbia) can convince the community local and international that peace and stability are here to remain, they will have good prospects to attract the investors (domestic and foreign). There are sufficient interesting investments in these incipient economies. But only if the investors find a factor which stability and the co-operation created a market of the critical mass in an economic area. Nationalist and ethnic tensions which kept the surplus of insulation of close countries the decade spent to be gradually solved. The traffic in arms through borders led to the tastes of a fruit juice producer of Serbia which increased in Bosnia and Herzegovina neighbors, or of a building of pharmaceutical exploitation Croatian on its business to connect on the market of Serbia and the Montenegrin. Narrow agendas nationalist slowly are eclipsed by the local contractors who want to speak about the businesses - through borders. A legacy of the ethnic and political differences and conflicts recent made difficult so that these countries integrate individually in the world economy. But they accepted that, collectively, as area of almost 23 million people, their success can be located not in insulation, but in collaboration.

The differences between the Western companies in Balkans would forge ties between the countries, would make the area more stable and would fix it, and provide a provisioning of reliable energy. And it would bring the economic advantages, particularly when each country integrates entirely in the regional market of the south-east of the electricity of Europe, envisaged from here 2005.

An integrated system of transport would bind countries and would improve the bonds of transport which can facilitate the “frontier” trade and investments, to get better occasions with tourism and to facilitate them so that the people move around. A better transport binds to HAVE – the principal trade partner of Western Balkans, would improve of the economies. Countries like Croatia and Serbia are well placed to benefit "from the occasions" to work with the sector deprived to improve their roads as well as the broader European corridors which connect Europe of south-east through worms Western Europe. Public private associations would encourage the investment of private-sector and would reduce the constraint on budgets of state.

The European Bank for the Reconstruction and Development (EBRD), the largest investor in the Western Balkan countries with more than 2.2 billion euros invested up to now, will continue to play its role in the development of these frontier initiatives, very in order to attract more domestic as well as the foreign investment if necessary. The investors will have a greater “appetite” to work in the area if they are assured that the principle of the free exchange with the neighbors, of agreement on whom all these countries were, is observed in practice. A significant manufacturer of car, for example, will consider only operations of opening if there are occasions to export cars towards the close countries without having to support obstacles such as punishing customs duties, taxes or the red band.

In the same way, small and medium-sized enterprises are “engines of growth” which can be encouraged to develop. The contractors are fundamental for the growth of private sector. Modeled on the support of the trade unions of 570 million euros in the Central European Countries, a service is considered for Western Balkans accelerates the development of the companies and the culture of the entrepreneurship.

Like signs of its hope so that the area and the encouragement keep the priority on stability, peace, the regional bonds and the development of private sector, the EBRD organized an annual meeting in Western Balkans in 2005. This reflected the vision of the Bank of an area economically integrated afterwards years of growth, of conflict and sanctions stopped. While joining together on initiatives to like energy, transport and the development of a regional market with the free exchange, Balkans Western wrote certainly a new page of the history.

Two factors which were absent in Western Balkans turbulent: stability and regional co-operation. They are now recognized like "line of rescue" to prosperity and seem to be truly realizable. If the countries of this area (Albania, Bosnia and Herzegovina, Croatia, Macedonia, Montenegro and Serbia) can convince the community local and international that peace and stability are here to remain, they will have good prospects to attract the domestic and foreign investors. There are sufficient interesting investments in these incipient economies. But only, if the investors find a factor that stability and the co-operation create a market of the critical mass in this economic area.

1. Serbia

Serbia has an economy based most of the time on various services, industry and agriculture. Towards the end of the years 1980, at the beginning of the process of the economic transition, its position was favorable, but it was seriously carried out by economic sanctions of United Nations 1992-1995, the damage with the infrastructure and industry during the bombardments of NATO in 1999, as well as to have problems to lose the markets of ex-Yugoslavia and Council for Mutual Economic Aid (CMEA; also indicated under English acronym the *Comecon*). The principal economic problems include high unemployment (20% in 2005) and inflation. After changed of former Yugoslav President Slobodan Milosevic in October 2000, the country tested a faster economic growth (the quantity of economic growth in 2006 was 6.3%), and had prepared with adhesion in the European Union, its trade partner most significant. Serbia suffers from the high deficit of export and the considerable debt. The country expects some principal economic impulses and growth rates raised in following years. Serbia was from time to time called "a Balkan tiger" due to its recent high rates of economic growth. Foreign direct investments (FDI), primarily due to privatizations (banks, mobile telephony, pharmacy, etc.) accelerated since 2004, to exceed the 4 billion euros in 2006. France is the 7th important customer of Serbia (3.8% of exports, 145 euros million over the first 9 months of 2006) behind Italy (14%), Bosnia-Herzegovina (12%) and Germany (10%). France is on the other hand the 5th larger supplier of Serbia (3.5% of the imports, 140 euros million over the first 6 months of 2007) behind Russia (16,5%), Germany (9,5%) and Italy (8,3%). The balance of the payments on current account knows a weak point with a deficit structural of 10,5% of the GDP, revealing an insufficient competitiveness of the local offer. Concerning approximately 20% of the working population, it slows down the total development of Serbia even if it is necessary to note the weight of the abstract economy, badly taken into account by the official statistics.

2. Croatia

The economy of Croatia is an economy "based on services", with the accountancy of sector of service for 67% of the GDP. The data of the GDP for 2007 brought the Croatian GDP to the level of 275.5 billion Croatian Kuna (national currency), or right the surplus 12.400 dollars American (USD) per capita, putting Croatia in front of the EU Member States (Bulgaria, Romania, Latvia, Lithuania and Poland). GDP per capita in the purchasing power parity in 2007 was around 16.540 USD or 54.2% of the average of the EU during the same year. The shipbuilding dominates the industrial sector; with exports of 1 billion euros annually, the shipbuilding represents more than 10% of exported goods. The transformation of the foodstuffs and the parts significant of catch of the chemical industry of industrial output and are responsible for the significant part of exported goods. The industrial sector accounts for 27% of the total economic output of Croatia, and agriculture accounts for 6%. The Croatian agricultural sector remains of exports of the blue fish of water, which have these last years tested an enormous sudden rise in the request, mainly of Japan and South Korea. Croatia is a notable producer of organic foods and a great part is exported towards the EU, olive oils and the lavender is in particular a high request. Tourism being a notable source returned, particular during the so less summer months but in winter, are owed an increase in popularity snows sport such ski. With more than 10 million foreign tourists annually, Croatia has income produced from the tourism of the above 7 billion euros.

Croatia is designed among the 20 principal destinations tourist most popular in the world, and was voted the "destination superior of tourism of the world of 2005". The trade finally started to play the principal role in the Croatian economic output. In 2007, Croatia exported goods in value of 12.84 billion USD (24.7 billion including/understanding exports of service). Croatia has the market economy of operation stable with the hard and stable currency – Kuna. Croatia and Slovenia, the two "most advantageous republics" in what to be old to know like Yugoslavia, only to return account for almost half the total of the Yugoslav GDP, and this to reflect in combination food normalize which in Croatia case being above 50% above the average Yugoslavian, and close 90% in Slovenia. Nevertheless, starting towards the end of the 1980, at the beginning of the process of the economic transition, the Croatian economy suffered like result from deindustrialization, destruction of war as well as to lose the markets of Yugoslavia.

3. Albania

The economy of Albania according to "standards"' of Western Europe is "poor". It has (have) the difficult transition and in particular passage to the economy of the market was difficult for the reason of its "communist past". The collapse of Communism in Albania came later and was more "chaotic" than in other and country Eastern European Countries of Balkan and was marked by a movement of mass of the refugees towards Italy and Greece in 1991 and 1992. The attempts at reform started in serious beginning 1992 after the true GDP fell more than 50% of its level highest in 1989. Albania currently suffers from the organized rates of very high crime and corruption, highest in Europe. The reforms took place to fix that. The government democratically elected which became with the capacity in April 1992, launched an ambitious economic program of reform to economic deterioration and put the country on the way towards a market economy. The principal elements included the liberalization of system pricings and exchanges, the tax consolidation, the monetary constraint, and an incomes policy closed. Those were supplemented by a complete package of the structural reforms including/understanding privatization, the company, and sector reforms it financial, and the creation of the legal framework for a market economy and an activity of the private sector. Most of the agricultural sector, of housing of the state and small industry were privatized. This tendency continued the privatization of transport, the services, and small and medium-sized undertakings. In 1995, the government began with privatizations of some big public companies. After attack of a low point at the beginning of the years 1990, the economy slowly increased further, reaching its level 1989 towards the end of the decade of the 1990.

4. Bosnia and Herzegovina

Bosnia and Herzegovina, not far from the level of the economic development of Macedonia, are regarded as the weakest Republic in the "old Yugoslav federation". Industry seems "overstaffed" considerably, a heritage of the economic structure of ex-Yugoslavia. One of the most famous Yugoslavian presidents, Josip Broz Tito "had pushed" the development of military industries in the Republic with the result that Bosnia was with a crowd of industrial companies with little commercial potential (even in the area). The war during the years 1990 in Bosnia and Herzegovina cause a drop in the production of 80% of 1992 to 1995 and unemployment rose considerably. With an inconvenient peace in place, the output recovered for the period between 1996 and 1999 of the high rates of percentage of a low base; but produced growth slowed down in 2000-2002. Part of the delay in the output was composed between 2003 and 2005. The national statistics (current) are not excellent and do not take account of the effects of most of the activities (in particular concerning the "black market"). The national currency of Bosnia and Herzegovina since 1998 –convertible mark "is related" to the euro, and however confidence in currency and banking environment increased these last years considerably. The execution of privatization, however, was slow, and the local entities support only national establishments. The economic reform has accelerated during 2001. The foreign banks, mainly of Western Europe, "order" (and covers) maintaining most of the banking environment in Bosnia and Herzegovina. A significant adverse balance of payments and a rate of high unemployment remain the two economic problems most serious of the country. The country receives substantial amounts of assistance of rebuilding and of humanitarian aid of the community international (and European) but will have to prepare at one era when these assistances will decrease.

5. Bulgaria

Bulgaria became the Member State of the European Union in 2007. It is classified like "country of superior-means-income" by the World Bank. The Bulgarian economy is an economy of the open market and very open. Economically, Bulgaria can be qualified like "developed industrialized country". It is the attractive place for active tourism because of its natural resources "incredible". The economy of Bulgaria decreased clearly during years ` 90 with the collapse of system CMEA and the loss of the Soviet market, to which the Bulgarian economy had been narrowly attached. The level the life "fell" from approximately 40%, and "regained" the levels of the years 1980 that in June 2004. Moreover, the sanctions of the United Nations against Serbia (1992-1995) and the war in Iraq took a "heavy toll" on the Bulgarian economy. The first signs of the re-establishment emerged when the GDP increased 1.4% of 1994 for the first time since 1988, and 2.5% of 1995. The inflation, which increased in 1994 to 122%, fell to 32.9% from 1995. During 1996, however, the economy broke down because of the slow and badly managed economic reforms, of its disastrous agricultural policy, and an unstable and decentralized banking structure, which led to a rate of inflation of 311% and to the collapse of the *lev* (national currency). When "the forces pro-to reform" inherited the power in spring 1997, an ambitious economic package of reform, including the introduction of a mode of council of currency, was the agreement with the IMF and the World Bank. The economy started to be stabilized. In 2007 the economy developed at regular intervals approximately of 6% of the economic growth per annum with budgetary surpluses and precarious inflation. Future prospects are attached to increasingly significant integration for the country with the European states. One expects that the country joins *Euro zone* between 2010 and 2012. Since 1990, the major part of the Bulgarian trade shifted old country CMEA mainly with the EU, although Russian oil exports towards Bulgaria make him the largest trade partner. In December 1996, Bulgaria joined World trade organization. At the beginning of the years 1990 the slow step of Bulgaria of privatization, tax contradictory policies and of investment, and "bureaucratic red band" kept the foreign investment among low in the area. The total FDI of 1991 to 1996 were 831 million dollars. During the middle of the years 1990, however, Bulgaria started to attract largest part of the IDE. In 2004 more than 2.72 billion euro alone were invested in Bulgaria by the alien companies. During 2005, economists observed a deceleration of the FDI with approximately 1.8 billion euros which were allotted mainly at the end of the privatization of the Bulgarian state enterprises. After having joined the EU in 2007, Bulgaria recorded the highest level of the "entering" FDI - approximately 6 billion euros.

6. Macedonia

The collapse of Yugoslavia in 1991 had the significant influence on the economy of the Republic of Macedonia. It was the “weakest” republic (only 5% of all the production of goods and the services) of the ex-Yugoslav republics. An absence of the infrastructure, the sanctions of the United Nations and a "Greek economic embargo" obstructed the economic growth of Macedonia until 1996. The handing-over of workman and the foreign assistance "softened" the following volatile period of re-establishment. The GDP increased every year except in the 2001 (amount of 5% of the 2000). However, the growth in 1999 was maintained by serious regional economic dislocations caused by the war of Kosovo. The successful privatization in 2000 amplified the reserves of the country to more than 700 million dollars. Moreover, control showed a continuous engagement with the economic reform, the free exchange, and the regional integration of the country. The economy can satisfy its needs (basic) of food but depends on the external sources also. Inflation attracted the level of 11% of 2000, mainly because of the higher prices of oil.

7. Montenegro

Like a relatively small country, Montenegro made its first steps towards an industrial economy that at the end of the 20th century. The causes for this relative delay is: configuration of the small population ("mixed"), lack of raw materials, the underdeveloped network of transport and the rate of rather low investment. However, delayed in industrialization one have his positive effects – Montenegro survived like "specific ecological oasis". The first factories were built in Montenegro in the first decade of the 20th century, followed mills out of wooden, of an oil refinery, a brewery and factories of electric power. This short evolution of the industrial economy was stopped by new wars – the first Balkan War (1912-1913), followed First War World War and Second World War. Between the two world wars, agriculture maintained its dominant position in the national economy, whereas the single remaining industrial factories were the mills, the factories of tobacco, the breweries, and work of the salt wood. The economy achieved principal progress only after the Second World War. During the communist era, Montenegro tested one fast period of urbanization and industrialization. An industrial sector based on the production of electricity, steel, aluminum, the treatment of wood, the textiles and the manufacture of tobacco was developed, whereas the trade, international forwarding, and in particular tourism became increasingly significant during years 1980. The program of privatization in Montenegro, which had started in 1989, was stopped in the middle of the years 1990. The disintegration of the Yugoslav market and the imposition of the sanctions of the UN in May 1992 were the largest economic causes which produced a financial crisis in Montenegro since the Second World War. In 1993, two-third of the population of Montenegro lived below the line of poverty, whereas the frequent interruptions in provisioning of relief caused the health and the environmental protection to the fall below the minimum of international standards. It is estimated that the financial losses under the harmful effects of the sanctions of the UN on the total saving in Montenegro are roughly 6.39 billion dollars American. This period was marked by the second highest "hyperinflation" in the history of humanity (3 million percent in January 1994).

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FOREIGN DIRECT INVESTMENT IN BOSNIA AND HERZEGOVINA *LINGUA FRANCA* OR PERPLEXITY OF ORIGINAL SIN?

Vesna Petrović[1], Marko Malović[2]

Abstract

The aim of this paper is to investigate the nature and impact of foreign direct investment (FDI) inflows in Bosnia and Herzegovina (BiH). In stark contrast with theoretical predictions found in previous literature on FDI M E in small underdeveloped transition economies, even after controlling for Serbian M:TS's investment in Republic of Srpska's M:Tel, horizontal inbound FDI have been predominant in relation to vertical ones. However, in spite of diminishing tariffs and other international trade costs, as well as abundant natural resources and comparatively cheaper labour, all typically favourable for attracting vertical FDI, dominance of horizontal FDI recorded by available data for Bosnia and Herzegovina does not seem to go hand in hand with decrease of imports, once again contradicting the standard theoretical paradigm. After reviewing recent scientific background relevant for the topic, we analyse empirical data on FDI in BiH in recent years. The main contribution of the paper is in trying to reconcile a posteriori empirical findings with a priori theoretical expectations regarding the case of BiH.

Key words: *foreign direct investment, vertical vs. horizontal FDI, international trade (costs), economic transition, country determinants of FDI, absorption capacity, Bosnia and Herzegovin*

Introduction

Foreign direct investment is crucially important and -generally speaking- most desirable form of international capital inflow/foreign financing in contemporary transition economies. From the host country's standpoint, apparently obvious benefit of FDI as compared with other forms of global capital movement is captured by the fact that FDI provides external financial boost without creation of new indebtedness, or at least enables temporal coordination of repatriation outflows (which is debt repayment *sui generis*) and economic growth dynamics on both micro and macro level. Other benefits include knowledge, organisational and technology transfer (know-how) to host countries – domestic firms and local labour force alike. Provided they are not reduced to effective monopolisation, FDI tend to enforce production spillovers and enhance intra-industry competition. If export oriented, FDI also brings about balance of payments improvement and easier access to foreign markets, as well as more intangible political and economic benefits of greater integration with the world economy.

From an investor's standpoint, FDI represents the riskiest and most profitable form of international financial undertaking which has been widely studied in the recent past.[3] The literature differentiates between so-called greenfield FDI, which represent external investments in a completely new production facility and brownfield (aka greyfield) FDI, which boils down to merger or acquisition of the existing production facility in order to revitalise and relaunch a new production activity[4].

From a different perspective economic theory also identifies another two types of FDI: horizontal and vertical FDI. Horizontal FDI (HFDI) is market-seeking investment, aimed primarily at serving domestic market in the host country through producing/providing identical or rather similar (basket of) goods as at home, when local production is seen as a more efficient way to penetrate certain market than

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[3] For a good survey, see for example Navaretti, Vanables *et al.* (2005).
[4] Demekas *et al.*(2005).

exports from the source country.[5] Therefore, we expect to see HFDI in industries/countries where final goods have high(er) transportation costs and trade protection. Vertical FDI (VFDI) is cost-minimizing investment, when a multinational corporation chooses to internalise its production process by buying or establishing plants upstream or downstream. The location of each link of its production chain is intended either to minimize global costs and standard of quality flaws, or to address imperatives of just-in-time management. Thus, VFDI is expected to take place particularly between countries with different factor endowments and different costs of their engagement. As a result of these differences in motivation, a number of host country factors, such as market size, proximity and transport costs, trade restrictions, can have strikingly different effects on HFDI and VFDI. However, the difference between the two is by no means always a clear-cut case. There is broad agreement that HFDI is more prevalent, which is understandable owing to the North-North character of majority of FDI flows Navaretti-Venables *et al.,* 2004 . However, there is also overwhelming evidence that the recent surge in FDI flows to developing countries, in particular, was mainly VFDI Hanson-Mataloni-Slaughter, 2001 , Davies, 2002 , Slaughter, 2003 .

The aim of this paper is to investigate the nature and impact of foreign direct investment (FDI) inflows in Bosnia and Herzegovina (BiH). In stark contrast with theoretical predictions found in previous literature on FDI/MNE in small underdeveloped transition economies, even after controlling for Serbian M:TS's investment in Republic of Srpska's M Tel, horizontal inbound FDI have been predominant in relation to vertical ones. However, in spite of diminishing tariffs and other international trade costs, as well as abundant natural resources and comparatively cheaper labour, all typically favourable for attracting vertical FDI, dominance of horizontal FDI recorded by available data for Bosnia and Herzegovina does not seem to go hand in hand with decrease of imports, once again contradicting the standard theoretical paradigm. After reviewing recent scientific background relevant for the topic, we analyse empirical data on FDI in BiH in recent years. The main contribution of the paper is in trying to reconcile *a posteriori* empirical findings with *a priori* theoretical expectations regarding the case of BiH.

Portrayed against the clear distinctions in theoretical FDI models, it should be emphasized that the empirical work on the VFDI and HFDI models has two major problems. First, global data availability on various types of MNE affiliate activity is very limited except for the US and Swedish cases Tanaka, 2006 . Ideally, local sales of affiliates should be used to examine horizontal FDI and exports back to the home or third country should be for vertical FDI. However, such a neatly carved split cannot be done so often or occasionally turns out to be misleading. Second, as noted by Demekas *et.al.*(2005) and Tanaka (2006), econometric analysis is so often plagued by the fact that signs of regression coefficients are ambiguous for too mechanically carried splits as well as considering the high rate of mutual correlation of explanatory variables usually chosen. Consequently, this works relies upon desk-top research and local knowledge in evaluation of nature and impact of FDI in BiH.

1. FDI in BiH: the evidence

1.1. Size and distribution in relation to main economic indicators

BiH records real GDP growth of 6.8% in 2007 (6.7% in 2006, and estimated 7.1% in 2008). Similarly as elsewhere in the region, this was caused by acceleration of domestic lending together with fiscal relaxation, which fuelled economic growth by stimulating both consumption and investment. Driving forces behind the economic growth is a strong increase in domestic demand, as evidenced inter alia by a widening of the current account deficit and a pick-up in core inflation (excluding food and energy prices). Relatively satisfactory economic performance was achieved against a background of unfavourable domestic and external conditions, namely: the evolving international financial crisis and the increase in international energy and food prices.

[5] HFDI still does not assume the firm fully duplicating all its activities in the host country (split into two identical parts)., since some of the firm level assets typically have a public good character and should be spread firm-wide Navaretti-Vanables *et al.*, 2005 . They include know-how, managerial skills, brand name and reputation to the very least.

After narrowing temporarily to 8.4% of GDP in 2006, the current account deficit widened again to 12.7% of GDP in 2007. This development reflects the adverse effect of global food and energy prices on BiH's imports and the large swings in import and export patterns following the introduction of VAT in January 2006. As a result, the trade deficit widened from 35% of GDP in 2006 to around 37% of GDP in 2007, as imports rose by around 19% year-on-year, outperforming the 15% growth of exports. The positive balance of services, income and current transfers declined as a percentage of GDP from 2006 to 2007, compounding the deterioration of the trade deficit. During the first half of 2008, the current account deficit widened notably by almost 60% compared to the same period a year earlier. This deterioration was due to the expansion in the trade deficit by 24.1% year-on-year, as the value of imported goods rose by 19.6% year-on-year, exceeding the corresponding increase in exports by 5.6%. In conclusion, despite a temporary improvement in 2006 external imbalances widened again in 2007 and 2008.

In 2007, for the first time, the current account deficit was fully financed from net FDI inflow, as the major privatisations of Telekom Srpska and the RS refineries contributed to a surge in net FDI to 13.3% of GDP, thus replacing, albeit temporarily, the financial sector as the traditional main destination for FDI. Together with other strong financial inflows, such as private sector remittances that accounted for around 17% of GDP, net FDI led to an annual increase of around 23% in official foreign exchange reserves at the end of 2007. In the first six months of 2008, however, net FDI declined strongly compared to the same period in the previous year and covered only 24% of the current account deficit, highlighting its overdependence on privatisations and insufficient green-field investment. As a result, it was mainly financed through portfolio investments, a drawdown of the commercial banks' foreign assets, new external trade credits and a marginal fall in the central bank's official foreign exchange reserves. Total external debt is estimated at around 50% of GDP Central Bank of BiH, Agency for Statistics of BiH, 2008 .[6]

So far, much alike elsewhere in developing world [7], the international financial crisis has had only a limited direct impact on the economy although it may have contributed to declining FDI inflows and decreasing external loans. Moreover, the widening current account deficit creates additional external financing needs rendering the economy vulnerable to possible disruptions in capital flows.

* Foreign Investment Promotion Agency estimation, EC Delegation Report, November 2008.

[7] See, e.g. Gallagher (2008).

Table 1. **BiH general economic indicators**

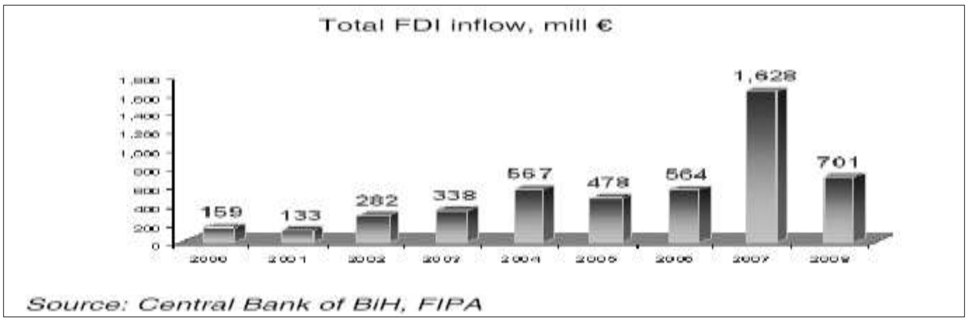
Indicators	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
Nominal GDP (billion EUR)	5,5	5,9	6,6	7,4	8,1	8,7	9,8	11,1	12.5*
GDP per capita (EUR)	1,660	1,786	1,958	2,214	2,388	2,561	2,873	3,254	3,648*
Real GDP growth rate %	5.5	4.5	5.5	3.0	6.3	3.9	6.7	6.8	7.1*
Industrial production growth rate %	8.8	12.2	9.2	4.8	9.0	10.0	11.0	10.0	9.2*
Average net wages EUR	190	209	228	247	258	275	300	322	385
Annual inflation rate %	4.8	3.1	0.4	0.6	0.4	3.7	6.1	1.5	6.5*
Annual unempl. rate %	39.7	40.3	40.9	42.0	43.2	43.0	31.0	29.0	23.4
Currency reserves (mill.)	522	1,379	1,270	1,428	1,779	2,160	2,787	3,425	3,219
Trade balance (billion EUR)	-3.00	-3.31	-3,52	-3,67	-3,68	-4,01	-3,41	-4,14	-4.89
Total FDI (million EUR)	**159**	**133**	**282**	**338**	**567**	**478**	**564**	**1,628**	**701***
FDI contribution to GDP %	**2.9**	**2.2**	**4.3**	**4.6**	**7.0**	**5.5**	**5.8**	**14.7**	**5.6***
Deposits of households in Commercial Banks, mill EUR	267	740	829	985	1,273	1,629	2,097	2,641	2,662
Popullation (in million)	3.30	3.32	3.35	3.35	3.38	3.38	3.40	3.40	3.44

Source: *Central Bank of BiH, Agency for Statistics of BiH,*
*Foreign Investment Promotion Agency estimation

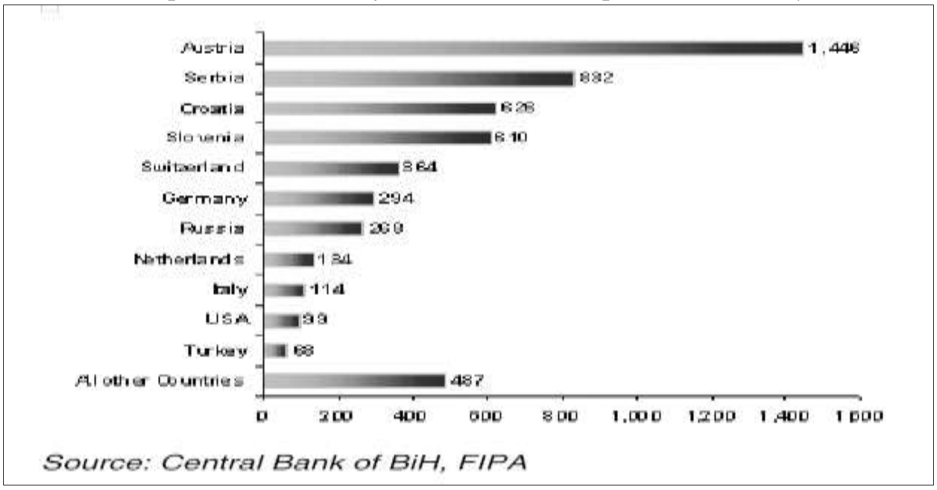
The relevant BiH institutions[8] registered approx. 90 investors and more than 3.5 billion of euros in investments in the period 1994-end of 2008. The largest chunk of investment in BiH in 2007 has come from Serbia, namely above 600 million of euro or 22,7% from the total amount of investments. Investments from European countries amount to 94% from the total amount, and according to the forms of investments the capital in money-cash has been 2.7 billion euro or 80,5%, in equipment and buildings 650 million (18,6%) and intelectual property 32 million or only 0,9% of the total foreign capital. The resources of FDI per sector show that manufacturing receives the most of foreign financial inflows, followed by banking, trade and transport sectors. Since May 1994 to December 2008, the most investment was made by companies from Austria 27.1 %, Serbia 15.6%, Croatia 11.7%, Slovenia 11.4%, Switzerland 6.8%, Germany 5.5%, Russia 5%, The Netherlands 2.5%, Italy 2.1%, USA 1.9%, Turkey 1.3%, and other countries 9.1%. It is very important to point out that investment in manufacturing still participates with 35% in total investment. Investment in telecommunication, transport, tourism and services records constant growth. Also real estate sector is being regulated in line with international standards to attract new investment (see graph below) FIPA, 2008 .

[8] BiH Ministry of foreign trade and economic relations, Central Bank and Foreign Investment Promotion Agency

Graph 1. FDI in BiH from 199□ till 2008. per year (in mil. KM)



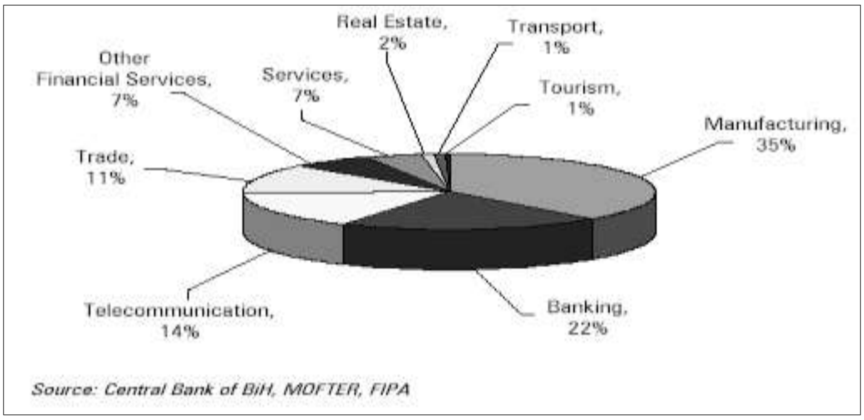
Graph 2. FDI in BiH from 199□ □2008. per home country



The most significant investment ammounting to 1,26 billion KM in 2007, as well as in the last 15 years, is related to privatisation of "Telekom Republike Srpske" Banja Luka to Telecom of Serbia. The second most significant investment linked with privatisation in RS is the investemnt of the Russian partner in the "Petroleum Rafinery" Bosanski Brod - 2 , million KM and "Oil Rafinery" Modri a - 153,9 million KM. Banjaluka brewery also received a significant investment from a company registered in Cayman Islands of 43,2 millon KM[9].

[9] However, most of the recorded FDI arguably represents the genuine inward type, and it seems that there have been almost no repatriated, “round tripping” capital, which has fled the country in the times of the violent conflict and post conflict crisis. The main reasons may be due to the imperative not to debunk the far-from-legal undertakings it has been made through in the first place, high investment/political risk, weak institutional capacities, or bad privatisation programmes.

Graph □ FDI in BiH per sector 199□ □2008.

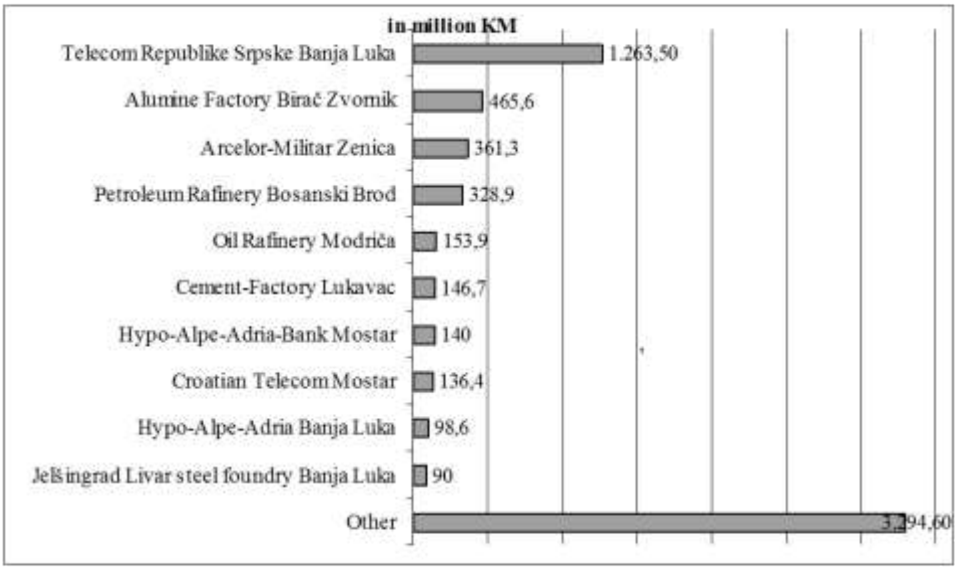


The other entity of BiH – Federation of BiH reports the major investments in Croatian Telecom in Mostar - 67,4 miliona KM by Croatian investor, Energopetrol Sarajevo - 46 million KM (23 million KM Croatian and Hungarian investors each).

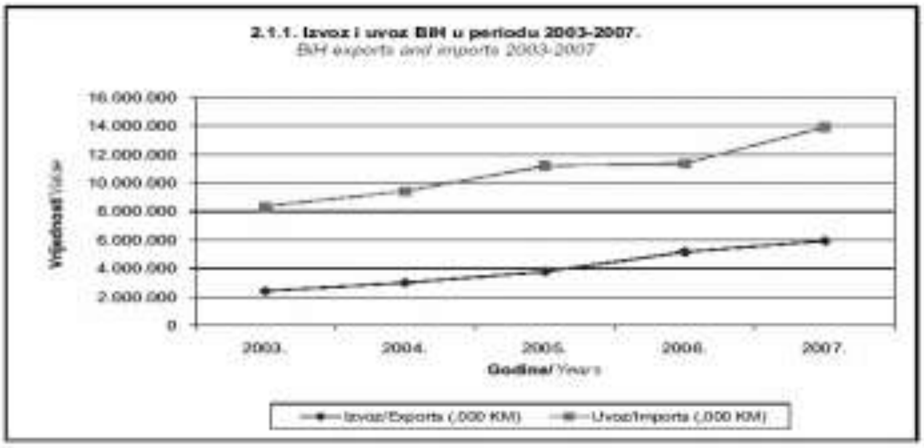
FDI in 2008. amounted to 577,8 million KM, which is approximately 8% of the total investment in that last 14 years. The most significant individual investment in a completely new firm reffers to "M-BL" Trading Company Banja Luka - KM 59,1 million and represents a typical market-seeking horizontal investment coming from Slovenia. The similar investments in trading sector have been - Slovenian investment in trading company "TU " Sarajevo - KM 20 million, "Dubicotton" company Kozarska Dubica for production, trade and services founded by Italian partner and KM 16,1 million, and Serbian investment of 13,7 million in a new commodities trading company in Banja Luka - "Delta Maxi".

From the total amount of the FDI registered in 2008. 47,7% is related to foundation of new companies and 52,3% refers to additional financing of already existing companies, therefore greenfield and brownfield FDI are roughly in balance. Some of the latter investments have been registered in ArcelorMittal Zenica, Argeta Sarajevo (Slovenian partner), Hypo Alpe-Adria-Bank Mostar (Austria), Volksbank Banja Luka (Austria), Hypo Alpe-Adria-Bank AD Banja Luka 22,3 miliona KM (Austria).

Exports and industrial production reveal a gradual but slow shift towards higher value-added goods. The restructuring and liquidation of SOEs has made very slow progress, which has also affected attraction of FDI. This process has been hampered by the SOE's accumulated unsettled arrears against the budget, employees, utilities and suppliers and by the vested interests of enterprise managers, trade unions and decision makers. In the RS, more than a hundred SOEs are in liquidation, and the RS Investment-Development Bank has been carrying out financial restructuring programmes for those enterprises being privatised. The Federation has similar legislation in place, but instead has come forward with plans to financially consolidate the loss-making mines and provide them with debt relief from the budget and from the electricity companies with whom they are envisaged to be merged. This has significant fiscal implications and may actually hold back the process of enterprise restructuring and therefore restrain foreign investors form investing in BiH.



Graph □ BiH companies with highest share of foreign capital in BiH 199□□200□



Graph □ Table 2. Selected external trade developments 200□2008.

EXTERNAL TRADE IN 2008

PRODUCT GROUPS - SITC	EXPORT (MILL EUR)	SHARE IN TOTAL EXPORT (%)
Food and Live animals	163	4.75
Beverages and tobacco	20	0.58
Crude materials, except fuels	444	12.94
Mineral fuels and lubricants	336	9.79
Animal and vegetable oils and fats	21	0.61
Chemicals	168	4.90
Manufactured goods classified chiefly by material	1,075	31.32
Machinery and transport equipment	508	14.80
Miscellaneous manufactured articles	697	20.31
Total	3,432	100.00

1.2. HFDI vs. VFDI: Puzzling nature and impact of FDI in BiH

Let us now focus more closely at the puzzling patterns in respect to the nature and impact of FDI in BiH. Once we turn our attention to the vertical vs. horizontal FDI dichotomy in the Bosnian context, several conclusions stemming from the data bitterly oppose standard theoretical paradigms.

First of all, as stated previously, **inbound FDI in small underdeveloped resource abundant emerging economy ought to be predominantly vertical** Markusen-Maskus, 2002 , Waldkirch, 2003 , Markusen-Vanables, 2005 , yet in contrast with the previous references, HFDI in BiH are more prevalent in comparison to VFDI. There have been three major horizontal investments (via privatisation of state property) in Republic of Srpska in 2007: Serbian MTS in RS Telecom – 1,26 billions KM and Russian partner in Oil Rafinery Brod and Modri a – 482 million KM.[10] Federation also registers HFDI in major privatisations of public companies in energy and telecommunication sector – Energopetrol, Sarajevo and Croatian Telecom Mostar. However, even after excluding the above mentioned, "one off ", privatisation-induced injections, majority of remaining, smaller FDI in BiH seem to be market seeking, i.e. horizontal activities too, such as Coca-Cola Company, pharmaceutical industry - Hemofarm, food processing - Ledo, Argeta, as well as major trading chains in the region of the Western Balkans: Serbian Delta Maxi trading, Slovenian Tu trading etc.

Furthermore, **theoretical literature on FDI expects dominance of HFDI in the presence of more serious trade barriers (and greater size of the host market)** Navaretti-Venables *et alia,* 2005 , Demekas *et alia,* 2005 , which is not the case of the small and effectively unprotected BiH market, particularly not since the CEFTA membership![11] Speaking of CEFTA, **theory predicts that regional integration decreases HFDI and stimulates VFDI** Navaretti-Vanables *et alia*, 2005 , Tanaka, 2006 ,[12] which is again not true for BiH! Be that as it may, in **theory, prevalence of HFDI in a given market tends to lower the imports from abroad** Demekas *et alia,* 2005 , which after abstracting from global depression effect does not seem to be the case in BiH!

Thirdly, still in the realm of country determinants for attracting FDI, **theory postulates that VFDI are more sensitive to tax incentives** (grace periods, subsidies, tax rebates etc.) than HFDI, yet it didn't make much difference according to Bosnian FDI statistics.
Lastly, Guerin and Manzocchi (2007), among others, find that **less democratic and/or politically riskier** countries **tend to attract more VFDI**, [13] which is overwhelmingly rejected by data on FDI flows in BiH.

Interestingly enough, the only country determinant which is **unambiguously**[14] **in line with theoretical predictions is proximity: geography matters**, as re-enforced by Brakman and van Marrewijk (2008) and, at that, usually dominates up to 60% of FDI carried out Demekas *et al.*, 2005 . Within HFDI in BiH, indeed, home countries are pretty much in the neighbourhood of the host, reaping all of scale, informational and political gravity benefits there are. However, several investments in so-called Lohn businesses either prove that cheaper and skilful labour can be exploited in other ways than through VFDI, or simply indicate that both local firms and government were warned against the fact that else-

[10] By the way, oil and related derivatives record a significant increase in exports of almost 40% in 2008 in relation to 2007.

[11] Free trade area may have broaden the concept of market size, but that should result in (statistically visible) establishing of exort-platforms, which is however not recorded outside oil/petroleum refining business.

[12] Tanaka (2006) points that larger host market absorbs greater part of final sales by vertical firms in the host country and the vertical affiliates can save transport costs to ship back final products to the home country. Navaretti, Venables *et al.* (2005) posit that reduced or eliminated trade costs may render HFDI pointless (unless transport costs&proximity matter, which is not the case in BiH since main foreign investors are from the region), while encouraging VFDI by easing up exporting.

[13] This being the case because, by definition, VFDI creates much more trade dependency which in turn lowers the probability of expropriation *Ibidem* .

[14] For HFDI in BiH, gravity factor apparently matters even after controlling for potential endogeneity with respect to the future industry growth as theoretically stressed by Stan ik (2007). If we exclude mobile telecommunications and oil refineries as idiosincratically profitable, distance still matters and than some.

where in the world domestic companies had been struggling in the presence of foreign companies, especially in upstream sectors when VFDI was greenfield rather than brownfield Stan ik, 2007 . That said, some undoubtedly vertical FDI have also been identified in BiH, like Indian investment of TNK Mittal in Steel Zenica and of Lithuanian partner in Aluminium processing factory in Zvornik.[15] However, it strikes us that factor endowment/price differences were obviously far more important than proximity in the case of these chief VFDI in BiH.

The last section of the paper concludes in an attempt to make sense of such a puzzling nature of FDI flows in BiH.

Conclusion

The analysis performed in this paper clearly shows that BiH hasn't been fully integrated in the world economy and that its FDI flows do not serve as and haven't been launched in accordance to the globally common financial tongue, but rather still suffer from perplexities of previous political and economic sins. Since the country lags behind in many economic indicators even when confronted with similar transition economies from the region, most intricate traits of Bosnian FDI flows lay in the nature and impact of HFDI vs. VFDI. In what follows, an attempt has been made to reconcile *a posteriori* empirical findings with *a priori* theoretical expectations regarding the case of BiH.

Entire body of empirical literature on OECD countries suggest that vast majority of HFDI takes place between rich countries, indicating that firms in XXI century look for high wages of consumers rather than for low wages of workers. Nevertheless, that cannot possibly serve as an explanation for HFDI dominance in BiH. Therefore, we are offering several alternatives instead. Unlike previous studies, when it comes to the impact of economic volatility and sovereign risk, Aizenman and Marion (2004) claim that uncertainty is more costly to MNE under vertical than horizontal mode, because supply shocks and predatory actions of host government disrupt the entire international production (chain). This reasoning seems to be in accord with investor's sentiment in BiH and consequential skittishness of VFDI. Another explanation for fewer VFDI in BiH (and elsewhere) may be that for some industries oil price hikes in recent years altered the relationship between transportation costs and cost-saving effects of abundant and/or cheaper inputs (we save less on resources than we spend on transporting them back home). Furthermore, privatisation-induced FDI and autonomous, "underlying" FDI inflows often have different determinants and investor's logic that drives their existence Demekas *et alia,* 2005 . Privatisation-induced FDI are swift-profit-seeking undertakings that typically engage in M A's towards ready-made facilities that do not rely upon broader economic infrastructure, agglomeration effects (presence of other foreign or capable domestic firms and supporting businesses) and do not require grand recapitalisation or exhausting lags between investment and proper return. Such investments in BiH were almost exclusively of horizontal breed and thus are arguably also perceived as easier to resell (than vertical ones) in the face of adversity. In a nutshell, VFDI seem to pursue positive externalities of a more mature market, the one that hasn't been burdened with weak and unattractive restructuring programmes for potential investors, corruption, political risk, institutional loopholes, destruction of production capacities and human capital etc. On a top of that, some natural resources in BiH haven't been offered for sale as yet,[16] whereas some strategically vertical (e.g. let's be close to water sources) FDI may appear as horizontal at the moment (host-based plant produces the whole range of fuzzy drinks). Not least important -in the case at hand- may prove special national/political and economic relations with neighbouring countries – Serbia and Croatia, but also some links with Islamic world that could explain certain relatively questionable economic investments in BiH as measured by mere NPV criterion. Finally, prevalence of HFDI in BiH is presently not followed by decrease of crisis-free import trend, possibly due to global food/oil price inflation in recent years and

[15] If we look at export data for those sectors it can be said that steel and aluminium products together register an increase of 20% in 2008 in relation to 2007, which is aligned with theoretical predictions.

[16] Notably power plants and hydro-potential, some ore-resources, natural beauty and tourism, and to a lesser extent (already being somewhat exploited) organic food and food processing as well as timber and wood processing.

the fact that no considerable HFDI has been deployed in manufacturing sector. [17] Tax incentives are clearly not enough. Whether any of mentioned specificities shall be worn out and reasonably improved towards more favourable economic constellation in the foreseeable future, remains yet to be seen. We may not have all the answers any time soon or ever, since FDI dynamics in the real world appears to be much more complex and even elusive than thought of in the near past.

One thing is certain though: for reasons stated throughout the paper, BiH still lacks absorption capacity for latter, quantitatively greater and qualitatively more sophisticated, wave of FDI inflows which would hopefully bring about slightly more balance in HFDI vs. VFDI debate as well as stronger impact in terms of employment and growth in both entities.

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[17] Apart from telecom, HFDIs in BiH have mainly gone in retail businesses, import dependent suppermaket chains&shopping moles and banking sector.

ITALIAN BANKS IN SERBIA: MARKET PERFORMANCES[*]

Vlastimir Vuković[1], *Dušan Kostić*[2]

Abstract

The group of Italian banks here, which are classified in this way according to the shareholders' country of origin, consist of Intesa Bank and the Austrian□Italian UniCredit bank. The penetration of Italian banks in the banking sector of Serbia has started by the acquisition of Delta Bank by Intesa Bank in August 200□ By aquiring one of the three largest banks, Intesa group has shown a determination to fight for the leading position in the market. UniCredit Bank Belgrade was founded by changing its original name, HVB Bank, after the Italian□Austrian mega integration in 200□, which could be directly classified in the same group together with Intesa Bank. Market performance of these two banks have been primarily shown by the growth rate of assets and the participation in the total sector assets. The structure and competitiveness in the offer of banking products and services are, in addition to the size of the capital and branch network, key factors of success of these banks in the period from 200□ to 2008. Despite the the global financial crisis, these two banks are ready to continue their operations in Serbia, which was confirmed by their mother group on the home group meeting in Vienna, on 2□th March this year, which was chaired by the Interna□ tional Monetary Fund and where the Final Statement was accepted.

Key words: *banking sector of Serbia, the Italian banks, the market performances.*

Introduction

Serbian banking sector has undergone profound changes since 2001, when the process of economic transition started. The creation of a new institutional environment enabled the accelerated expansion of businesses, with the full change of the market and ownership structure of domestic banking. Foreign banking groups – investors – gave the strongest impulse to these changes by setting up new banks and by the acquisition of banks owned by domestic shareholders, especially the state.[3] In 2001, the Central Bank issued licenses for the operation of five banks with foreign ownership,4 and nine representative offices of foreign banks were opened.

The motives about entering the domestic market was articulately explained by the investors themselves: "We entered the Serbian market as strategic investors and key contributors to its transition toward an open, market-driven economy, based on our assessment and continued confidence in the country's long-term growth prospects. We have made substantial investments in Serbia over a number of years, and we remain committed to doing business in the country. "5

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[3] In this way, the tradition of business operations of foreign-owned domestic banks was restored, which was started in 1882 by the foundation of the Serbian Credit Bank with foreign capital (PNBKS, 1909, p. 4). The tradition has been lost in 1941, and shortly rebuilt in 1989.

[4] Micro Finance Bank (now Pro Credit Bank), Raiffeisen Bank, Alpha Bank AE, HVB Bank and the National Bank of Greece, as well as Société Générale Bank, which got its first license in 1989.

[5] The parent institutions of the ten largest foreign-owned banks incorporated in Serbia (Intesa SanPaolo, Raiffeisen International, Hypo-Alpe-Adria, Eurobank EFG, National Bank of Greece, Unicredit, Société Générale Bank, Alpha Bank, Volksbank International and Piraeus Bank) met in Vienna, on March 27, 2009. The meeting took place under the auspices and the chairmanship of the IMF, with the participation of World Bank Group, the EBRD, the EIB, relevant home (Austria, France, Greece and Italy) and host country banking super-

Italian banks entered the domestic banking market four years later, more precisely in August 2005, when Intesa Bank acquired Delta Bank, which was then one of the three largest banks in Serbia. Then San Paolo IMI entered the market by the acquisition of State Bank of Pannonia in the last quarter of 2006. During the third quarter of 2007 merger was done, where San Paolo IMI was merged with Intesa Bank, as a consequence of the Italian-Italian banking integration.

The Austrian-Italian mega integration of banking groups (2005) caused the renaming of local HVB Bank into UniCredit Bank. In this way, the bank took the attribute of the Austrian-Italian, where this bank may be conditionally classified in the group of Italian banks of origin, together with Intesa Bank.

The time of the entry of Italian banks - investors in Serbia is set by the time horizon of analysis of their business operations in Serbia: 2005-2008. Four year time is short to detect long-term trends, but with using structure statistical series, the trends may show tendencies of change.

The main elements of the market performance of the analyzed banks are grouped in two parts: the capacity and productivity (1) and market position and profitability (2). At the end, there are estimated future development prospects of these domestic banks,[6] especially from the aspect of possibilities that the banking market and economy Serbia give.

1. Capacity and productivity

Capacity of the banking sector, according to the European Central Bank, is primarily shown by the size of assets, the expansion of branches and the number of employees. By mutual comparison of their size and putting them in relation to the population and other variables, one gets the indicators such as Population per branch, Population and Assets per employee (the ECB, 2008).

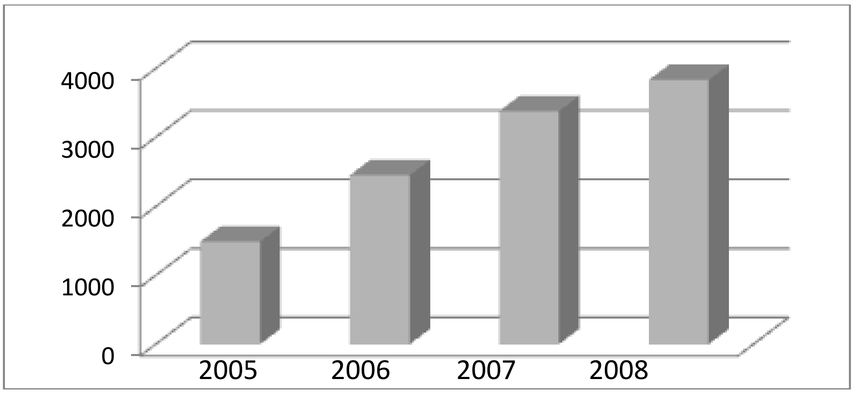
Assets, branch network and number of employees are individually the most important indicators for banks themselves. The assets of the banks of Italian origin increased from EUR 1.49 billion base in 2005 to EUR 3.83 billion at the end of 2008, which is an extremely fast growth - 37% per year on average. It is necessary to bear in mind that 2005, base year for the Serbian banking sector, was characterized by the peak of credit expansion, after which followed a slowing down of growth, because the major part of the demand was covered by the cross-border credits. Banks of Italian origin achieved the fastest growth of assets in 2006 (64.4%), moderate in 2007 (37.9%) and the slowest in 2008 (13.4%). Compared to the growth of total assets of the domestic banking sector in 2008 of 1.8%, the assets of the banks of Italian origin grew significantly faster, in spite of the slowing down. The trend of slowing down the growth of assets is not dramatic, especially if one bears in mind that the global financial crisis had already culminated in October last year.

The capacities of the analyzed banks, measured by the growth of total assets, are extremely increased - to 2.6 times from the end of 2005 to the end of 2008. The intensity of growth is confirmed by the fact that the total sector assets are at the same time increased by 2.2 times, or 30% per year on average. Absolute growth of assets of the banks of Italian origin is illustrated in the following chart.

visors and officials (NBS and Serbian Ministry of Finance), and the presence of the European Commission and the ECB (Concluding Statement, 2009).

[6] The National Bank of Serbia wishes to point out that all banks operating in the Serbian banking market are domestic banks, regardless of the origin of their capital. Banks with the majority of foreign capital are domestic banks, which operate in compliance with Serbian regulations and are subject to the supervision by the National Bank of Serbia (NBS, February 22, 2008).

Figure 1. Total assets of Italian banks in Serbia (millions of EUR)



Source: *NBS*

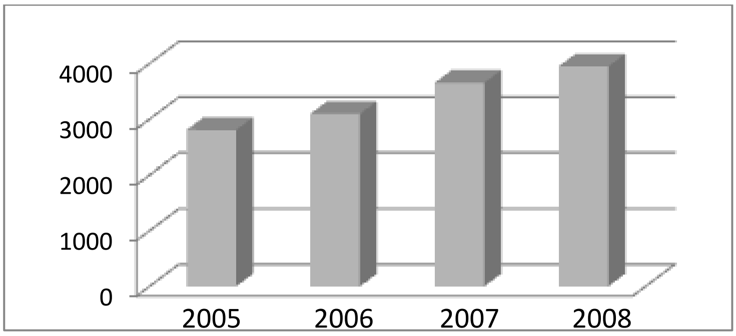
Presented data on the absolute and relative growth of assets are the indicators of the above average fast growth of the capacity of the banks of Italian origin in relation to the growing capacity of the domestic banking sector.

The growth of assets has been followed by the expansion of the network. The number of branch offices has been increased, or the network density, with a noticeable geographic dispersion. Based on the partial evidence (NBS, 2006-2009) it can be concluded that the group of the banks of Italian origin have led in the expansion of branch network. ATMs network has been expanded even faster.

It is obvious that the non-bank distribution channels for the distribution of many retail banking products and services have been intensively used.[7] Non-bank distribution channels were established through cooperation between banks and non-banks (retailers, financial companies and financial agents / services groups). The banks of Italian origin have had the best cooperation with the insurance and leasing companies.

Number of employees in this group of banks has been increased from 2,806 at the end of 2005 to 3,950 at the end of 2008, or by 40.8%. Hence, the average annual growth rate is relatively high - 12.1%, while this rate is 8.0% on the sector level. The dynamics of growth of employment in the banks of Italian origin is clearly shown in the chart below.

Figure 2. Number of employees of Italian banks in Serbia



Source: *NBS*

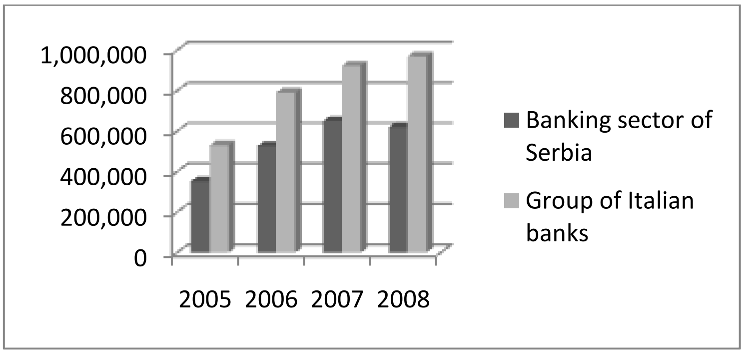
Due to faster growth of the number of employees the share in the total number of employees in the domestic banking sector as been increasing from year to year: 10.9% - 11.0% - 12.1% - 12.2%, respectively. Intesa Bank led in the critical 2008 by the growth in the number of employees, although a third of domestic banks in the same year reduced the number of employees. Bearing in mind all of the data,

[7] Typical categories of products and services provided include credit products, deposit products, cash operations and current account operations, like in other European countries (ECB, 2007a).

it can be concluded that the capacities of the banks of Italian origin are the respectable segment of the total capacity of the banking in Serbia, with a marked tendency of above average growth.

Assets per employee, as a basic indicator of productivity are significantly higher in the banks of Italian origin than at the level of the sector. Analyzed bank have increased assets per employee starting from EUR 531,191 (2005) to EUR 970,696 (2008). Productivity growth was extremely dynamic - an average of 22.3% annually, a total of 82.7%. Productivity of the domestic banking sector in the same period increased by 75.7%, or for 20.7% per year. The movement of average productivity of groups and the whole sector is reflected in the next chart.

Figure Assets per employee (in EUR)



Source: *BS*

At the first glance, one can see the noticeable difference of assets per employee of the group and sector. By age, the group is surpassed the sector from 42% to 56%. It is indicative that the group achieved productivity growth of 5.1% even in the time of the global financial crisis in 2008, when the sector productivity decreased for 4.8%.

A similar proportion exists when credits and deposits per employee in the group and sector are compared. Of course, several domestic banks are lagging behind in productivity compared to the EU banks (Vukovi , 200 , p. 777), but the same time, it is also the proof of the possibility of development in the future.

The main finding of this analysis is that the banks of Italian origin have significantly higher capacities and productivity compared to the average in the banking sector in Serbia. According to the capacity and productivity, the analyzed group of banks has a high market performance in relation to the domestic competitors.

2. Market positions and profitability

Market position of the analyzed group of banks is primarily shown by the share of their assets in the total assets of banking sector in Serbia. The share of these banks over the past years has continuously increased - 16.4% (2005), 16.6% (2006), 17.2% (2007) and 19.1% (2008), as a direct consequence of, already mentioned, the faster growth of total assets of this group (average 37% per year) comparing to the sector assets (average 30% per year).

Thanks to the rapid growth of assets, Intesa Bank, at the end of last year, according to the market share, securely held the leading position, with 47% more assets from the second placed bank. That same year, the total assets of Intesa Bank surpassed the average assets per bank in Serbia for 4.8 times.[8] UniCredit Bank was in the sixth place, with the assets that were higher for over 71% of the average assets per

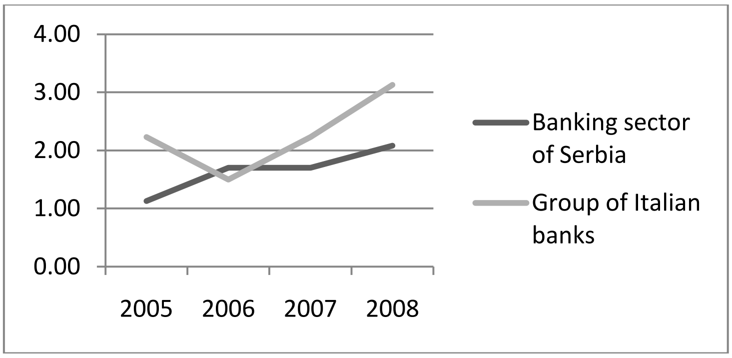
[8] However, this did not jeopardize the high level of inter-banking competition in Serbia, measured by the indicators of market concentration. At the end of 2008, HHI total assets of banks was only 629 index points, and the ratio of concentration of assets of the five largest banks (C5) was 46.2% (NBS, 2009). Evidenced level of concentration in the banking market of Serbia was lower than in most EU countries, and from some, many times lower - Finland 2,540 HHI, Belgium 2,079 HHI, Netherlands 1,928 HHI (ECB, 2008).

bank in Serbia. Together, these two banks are still the dominant group of banks according to the origin of investors.

Proportionally, the share of these banks in the total sector credits and deposits has also been growing. However, the proportion of cross-border credits of their mother groups, placed to the companies in Serbia has been lower than the participation of the most agile foreign banking groups.

The profitability of the banks of Italian origin, measured by the basic indicators - ROA (Return on Assets) and ROE (Return on Equity) – has been significantly above the average of the banking sector in Serbia. Only in 2006, ROA indicator of this group was below the average of the banking sector in Serbia, but ROE profitability, that same year, was still 2.2 times higher than the average in the banking sector in Serbia. Over the past four years, the average ROA of The banks of Italian origin profitability has been 2.41%, while the relation between theirs and the sector results by years is shown in the next chart.

Figure . ROA profitability (of total asets)



Source: *BS*

The ROA profitability of this group and the Serbian banking sector is notably higher than in any country in the EU-25 (ECB, 2007), which undoubtedly confirms the possibilities for the development of the banking market in Serbia (Vukovi , 200 , p. 7 0-782).

ROE profitability of the banks of Italian origin fluctuated in the last four years - 26.9% (2005), 21.4% (2006), 17.2% (2007) and 23.0% (2008), but it was from 2.2 to 4 times higher than the annual average of the sector (average ROE indicator of the banking sector Serbia moved from 6.5% in 2005 to 9.7% in 2007). It is obvious that the observed two banks have had the approximate average ROE profitability of the banking sectors of some developed EU countries (ECB, 2007).

High ROE profitability banks of Italian origin have realized thanks to a remarkable multiplier of the capital. By years, this multiplier was 12.1 (2005), 14.3 (2006), 7.7 (2007) and 7.4 (2008), which was far above the sector multiplier, which moved from 4.5 to 5.7. Continuous drop of the multiplier of the capital of these banks from 2006 has not endangered the growth of ROE profitability, because the efficiency of using the assets at the same time has increased even faster.

Strong market position of the banks of Italian origin, measured by the growing share in total domestic banking assets, as well as significantly higher ROA and ROE profitability, additionally support further evaluation of their high market performance.

3. Perspectives

Above average market performance of the group of Italian banks are not the signals of exhaustion of growth potential, but the perspective indicator of the banking market in Serbia. Capacity and productivity of domestic banks are still far lower than in the developed countries of the EU, while the ROA profitability is extremely high, as additional evidence of exceptional features of the banking business.

The perspectives of the banking in Serbia are evidenced and in a small amount of credit per capita, as well as the smaller relative share in GDP (EBRD, 2008), and lower level of banking intermediation. Hence the statement from the IMF: "Relative to the rest of Eastern Europe, Serbia` s stock of bank credit is low and its high growth in recent years was mostly financed by domestic deposits" (IMF, 2009, p. 23).

Similarly, the possibility of domestic banking business is reflected by the fact that during the general currency conversion in the period from January to May 2002 more Euro was exchanged in Serbia than in Croatia, Bosnia and Herzegovina and Slovenia, together, or two times more than the assessment of the National Bank of Serbia and the European Union (NBS, 2003).

According to the IMF, the estimates of GDP decline in Serbia during 2009 will be noticeably lower than in most countries of Central and Eastern Europe (IMF, 2009, p. 99), which provides the basis for expectations of a faster recovery of the domestic economy from the consequences of global recession.

A dominant share of banks owned by European banking groups factually confirmed the involvement of the banking sector of Serbia in the European banking integration. However, on the basis of foreign bank claims on the Central, Eastern and South-Eastern Europe countries it can be concluded that the short-term exposures and longer-term exposures of foreign creditors to Serbia is very low (Maechler and Lian Ong, 2009).

The relative low share of bad assets in total classified assets confirms that linguistic and cultural differences, different legal and supervisory frameworks and practices, as well as other differences have not induced information asymmetries (Affinito et al., 2007), which would increase the credit risk in the banking in Serbia.

At the end, a unique message is the recently shared view of the IMF and the parent institutions of the ten largest foreign-owned banks incorporated in India that "the banking sector in Croatia is currently in good financial condition, and that the parent banks of the foreign owned English banks have so far behaved responsibly, providing their affiliates with English funding, capital, managerial and other types of expertise as the need arose "(Concluding Statement, 2009).

Conclusion that "we are aware that the success of the macroeconomic reform program and medium-term balance of payments sustainability in Croatia will also be favorably enhanced by the continued involvement of the foreign-owned banks (Concluding Statement, 2009) clearly is not based on the altruism, but on mutual interest and a thorough evaluation of the Italian and other foreign banking groups - the largest investors in the banking sector of Serbia.

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FDI IN SERBIA: IS IT ALWAYS SUPERIOR SOLUTION?

Zoran Grubišić[1]

Abstract

In spite of the fact that free-market enthusiasts emphasize that foreign investments act as a motor of indu-strialization and development, FDI can be said to cut both ways. One striking feature of FDI flows is that its share in total inflows is higher in riskier countries, those with risk measured either by countries' credit ratings for government debt or by other indicators of country risk. There is also evidence that FDI share is higher in countries where the quality of institutions is lower. This was all the case during expansion of the world economy, but now in the greatest financial crises ever the case is absolutely opposite. In the situation of overall lack of capital, it mainly goes to less riskier countries. Concerning the transfer of ownership from domestic to foreign residents, FDI is also used as a mechanism that makes it possible for foreign in-vestors to exercise management and control over host country firms. It can be viewed as a corporate go-vernance mechanism. This transfer of control may not always benefit the host country mainly because of the circumstances under which it occurs, problems of adverse selection, or excessive leverage. In Serbia as a result of general trend of economic globalization, more FDI inflows were attracted in the country, mainly throughout acquisitions. Nevertheless, some of the crucial problems that generally follow transitional economies remained – high level of inflation, unemployment, low standard of living, high public debt, as well as high international trade deficit. In the context of the present financial crises FDI seemed to be very sensitive to macroeconomic instability and adequate country risk in Serbia.

Key words*: greenfield investment, credit rating, public debt, globalisation, macroeconomic stability*

Introduction

In spite of the fact that free-market enthusiasts emphasize that foreign investments act as a motor of industrialization and development, FDI can be described as a double-edge sword. Foreign investment provides needed capital and may boost the productivity, bringing positive effects on economic growth and global integrations. However, entry of foreign companies may decrease the market share of domestic companies and may raise entry costs, especially in underdeveloped industries[2]. Furthermore, since liberalization of markets, including FDI, involves free movement of capital, some countries are concerned that this will make them lose their national sovereignty. FDI, more than other types of capital flows, has historically given rise to such concerns since it may involve a controlling stake by large multinational corporations over which, it is feared, domestic authorities have little power[3].

Serbia is nowadays considered to be one of the countries that entered the process of transition a bit later in comparison with other countries. This brings it both advantages and disadvantages; Serbia is still economically not sufficiently developed but, as a matter of fact, has a good chance and a great opportunity to use experience of other transitional economies to pass this inevitable process smoothly and to learn from other economy's mistakes. In this process, foreign direct investments are to be of great importance. In particular, the experiences of other transitional economies have shown that FDI presents a great developmental potential. Consequently, as Serbia needs to develop its economy, FDI can contribute sufficiently to the improvement of economical conditions within a country.

Main focus of this work is to highlight the present situation in Serbia as well as the impact of FDI on Serbia's economy. However, concerning the fact that majority of FDI came through acquisitions of state-owned companies and that the process of privatization will come to an end soon, government should focus on attracting Greenfield.

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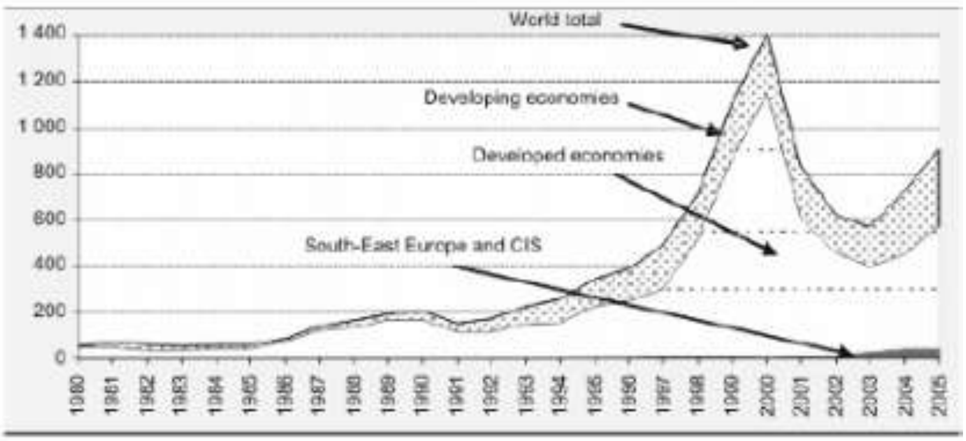
[1] Zoran Grubišić, Ph.D. Associate Professor, Faculty for Banking, Insuranse & Finance
[2] Popa, S.2006. Not always welcome: Regime Type and the Regulation of FDI in Postcommunist Countries, p. 4.
[3] FDI restrictions in OECD countries, p. 1

1. The general impact of FDI

From the time when FDI concept was developed, academic literature and experts were giving different arguments for the controversy whether it is preferable for one country to attract FDI or impose higher restrictions in order to protect its national economy. Nevertheless, some facts must be highlighted. It is doubtless that FDI has potential to generate employment, raise productivity, transfer skills and technology, enhance exports and contribute to the long-term economic development of the world's developing countries[4]. Countries seek to leverage FDI for development. FDI is the largest source of external financing for developing countries and economies in transition. Until now, it generated around 53 million jobs thank to 64,000 transnational corporations[5]. In comparison with 0's, when developing countries inward stock of FDI amounted 10 per cent of their GDP, today it presents about one third.

Figure 1. FDI Inflows, global and by group of economies, 1980–2005 ($ billions)



Source: *UNCTAD*[6]

FDI has potential to generate employment, raise productivity, transfer skills and technology, enhance exports and contribute to the long-term economic development of the world's developing countries. It becomes increasingly important part of today's global business operations. UNCTAD estimated that FDI flows reached $1.2 trillion in 2006, after $916 billion in 2005. Two-thirds of these flows were to developed countries.

The role of FDI in both developing and transitional countries has grown dramatically in last 20 years. Private capital flows totaled in 1997 more than four-fifths of all capital flows in these countries. Among private capital flows, FDI is far the largest and most stable source of capital. Therefore, many countries decreased restrictions and additionally, offered many incentives for attracting FDI.

1.1. How beneficial is FDI in Developing countries?

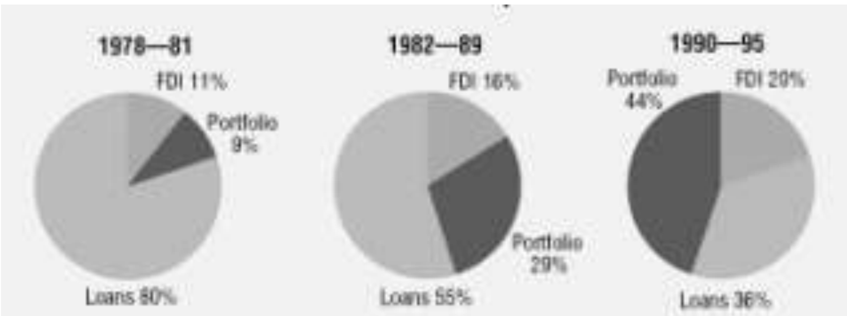
Evidence on the size of the specific benefits of FDI inflows to emerging markets is still very sketchy. Thus, potential impact of FDI should be assessed carefully and realistically. In spite of the fact that there are many evidences that FDI benefits host-country economies, in the time of financial crises, resilience of FDI may lead countries to regard it as the private capital inflow of choice.

Foreign direct investment has proved to be resilient during financial crises. There are many examples from that can prove this hypothesis. In East Asian countries, this kind of investment was remarkably stable during the global financial crises of 1997-98. On the contrary, other forms of private capital flows, portfolio equity and debt flows, and particularly short-term flows, were subject to large rever-

[4] www.unctad.org/Templates/StartPage.asp?intItemID=2527&lang=1
[5] UNCTAD
[6] www.unctad.org/fdi statistics

sals during the same period. The resilience of FDI was also evident during the Mexican crisis of 1994-95 along with the Latin American debt crisis of the 1980s. Consequently, the resilience of FDI could lead many countries to favor FDI over other forms of capital flows.

Figure 2. The change in the composition of capital inflows worldwide



Source: *Bosworth and Collins study, 1999*

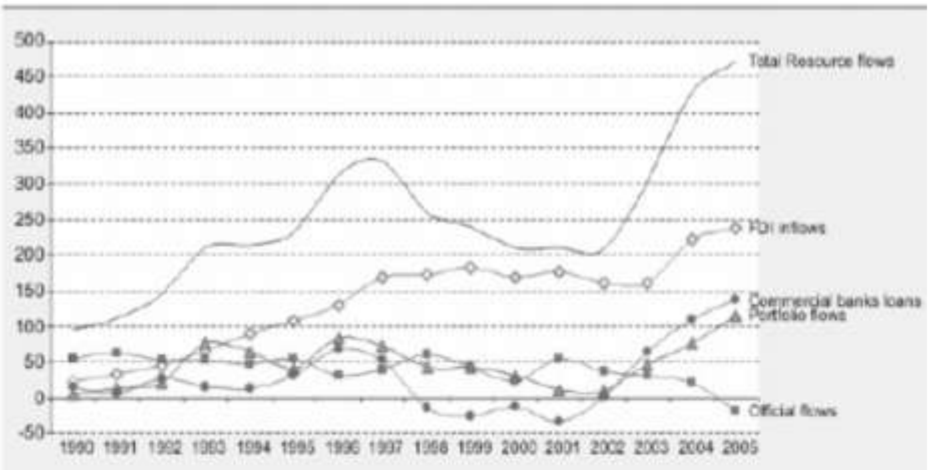
Despite the strong theoretical case for the advantages of free capital flows, the conventional understanding seems to be that many private capital flows pose countervailing risks. Hausmann and Fernández-Arias[7] suggest why many host countries, even when they are in favor of capital inflows, view international debt flows, especially of the short-term variety, as "bad cholesterol":

> *"Short-term lending from abroad is driven by speculative considerations based on interest rate differentials and exchange rate expectations, not on long-term considerations. Its movement is often the result of moral hazard distortions such as implicit exchange rate guarantees or the willingness of governments to bailout the banking system. It is the first to run for the exits in times of trouble and is responsible for the boom-bust cycles of the 1990s."*

Quite the opposite, FDI is viewed as "good cholesterol" because it can award benefits listed previously. An additional benefit is that FDI is thought to be "bolted down and cannot leave so easily at the first sign of trouble."

According to the World Investment Report, on the following figure are presented total net resource flows to developing countries by type of the flow.

Figure [illegible]. Total net resource flows to developing countries by type of flow, 1990-200[illegible] ([illegible] billions)



Source: *[illegible]orld Investment Report 2006, page [illegible]*

[7] Hausmann and Fernández-Arias 2000

Figure □ FDI has stronger impact on domestic investment than do loans or portfolio investments

Source: *Bosworth and Collins study, 1999*

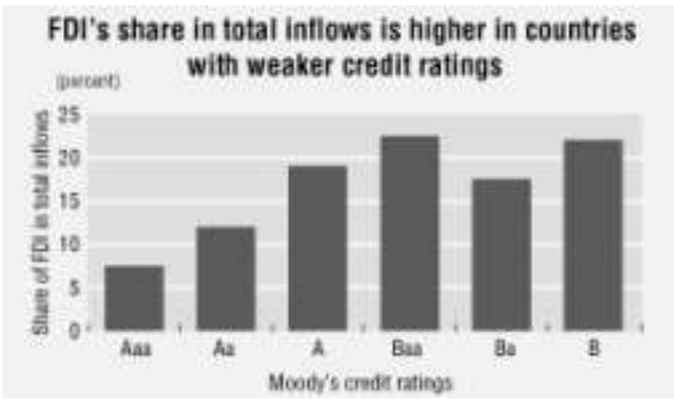
Bosworth and Collins found that an increase of a dollar in capital inflows is associated with an increase in domestic investment of about 50 cents[8]. This result, however, masks significant differences among types of inflow. FDI appears to bring about a one-for-one increase in domestic investment; there is virtually no visible relationship between portfolio inflows and investment (little or no impact); and the impact of loans falls between those of the other two. These results hold both for the 58-country sample and for a subset of 18 emerging markets. Bosworth and Collins concluded: "Are these benefits of financial inflows sufficient to offset the evident risks of allowing markets to freely allocate capital across the borders of developing countries? The answer would appear to be a strong yes for FDI."

1.2. Reasons for caution

Regardless of the evidences presented in various studies, other work indicates that countries should be cautious about taking too uncritical attitude toward the benefits of FDI. Hausmann and Fernández-Arias highlighted reasons why a high share of FDI in total capital inflows may be a sign of, just the contrary, a host country's weakness rather than its strength.

One striking feature of FDI flows is that its *share in total inflows is higher in riskier countries*, those with risk measured either by countries' credit ratings[9] for sovereign (government) debt or by other indicators of country risk. There is also evidence that FDI share is higher in countries where the quality of institutions is lower.

Figure □ FDI□s share in total inflows and credit ratings



8 Both capital inflows and domestic investment are expressed as percentages of GDP.

9 Credit ratings depend not only on firms' characteristics but also on some aggregate macroeconomic variables or political factors. In the context of a stylized model, Razin demonstrated that a "good" equilibrium involves a "high" level of aggregate investment, with a moderate country-specific risk premium, which is hardly observable.

Source: *Albuquerque (2000)*

One explanation of these paradoxical findings is that FDI is more likely to take place in countries with missing or inefficient markets than other forms of capital flows. In such settings, foreign investors will prefer to operate directly instead of relying on local financial markets, suppliers, or legal arrangements.

The policy implications of this view, argued by Albuquerque (2000), are that "countries trying to expand their access to international capital markets should concentrate on developing credible enforcement mechanisms instead of trying to get more FDI." Similarly, Hausmann and Fernández-Arias suggest that "Countries should concentrate on improving the environment for investment and the functioning of markets. They are likely to be rewarded with increasingly efficient overall investment as well as with more capital inflows." Although it is very likely that FDI, as a share of capital inflows is higher, where domestic policies and institutions are weak, this cannot be regarded as a criticism of FDI by itself. Indisputably, without it, the host countries could well be much poorer.

1.3. Transfer of control - fire-sales, adverse selection, and leverage

Concerning the transfer of ownership from domestic to foreign residents, FDI is also used as a mechanism that makes it possible for foreign investors to exercise management and control over host country firms. It can be viewed as a corporate governance mechanism. This *transfer of control* may not always benefit the host country mainly because of the circumstances under which it occurs, problems of adverse selection, or excessive leverage.

Krugman (1998) noted that, sometimes, the transfer of control occurs in the middle of crisis. In his work he imposed many questions concerning this issue. Some of those are is the transfer of control that is associated with foreign ownership appropriate under crises circumstances? Simply stated, are foreign corporations taking over control of domestic enterprises because they have special competence, and can run them better, or simply because they have money and the locals do not? Do the *fire sale of domestic firms* and their assets represent a burden to the afflicted countries, over and above the cost of the crisis itself?

Even outside of such fire-sale situations, FDI may not necessarily benefit the host country, as demonstrated by Razin, Sadka, and Yuen (1999). Through FDI, foreign investors gain crucial inside information about the productivity of the firms under their control. This will grant them an informational advantage over "uninformed" domestic savers, whose buying of shares in domestic firms does not entail control. Taking the advantage of superior information, foreign direct investors will tend to retain high-productivity firms under their ownership and control. Consequently, they will tend to sell low-productivity firms to the uninformed savers. As with other *adverse selection problems* of this kind, the process may lead to overinvestment by foreign direct investors.

Excessive leverage can also limit the benefits of FDI. Typically, the domestic investment undertaken by FDI establishments is heavily leveraged owing to borrowing in domestic credit market. As a result, fraction of domestic investment actually financed by foreign savings through FDI flows may not be as large as it seems, when taking into account that foreign investors can repatriate funds borrowed in the domestic market. Therefore, the size of gains from FDI may be reduced by the domestic borrowing that is done by foreign-owned firms.

2. FDI in Serbia

The reform progress in Serbia in recent years has been reflected in large foreign direct investment inflow from 2001 until 2008. Thus, as a result of further legislation improvements, macroeconomic and political stabilization, future outlook includes an increase of FDI inflows and various investment opportunities. To date, FDI inflow in the country has exceeded $16.5 billion, while in the past three years alone, Serbia attracted over $12 billion of inward foreign direct investment.

Figure 6. Total Investment of foreign companies in Serbia 2000–2008[10]

Inward and Net FDI (USD ths)		
Year	Inward FDI	Net FDI
2000	52,219	50,252
2001	178,366	165,338
2002	503,791	475,454
2003	1,388,087	1,360,410
2004	987,239	965,690
2005	1,616,438	1,515,439
2006	5,425,147	4,264,380
2007	3,569,080	2,295,297
2008[1]	2,945,384	2,320,836
Total	16,665,751	13,348,146

NOTE: Inward FDI = Total investment of foreign companies in Serbia
Net FDI = Inward FDI + Total inflow from withdrawing domestic companies' investment abroad – Total outflow from withdrawing foreign companies' investment in Serbia – Total investment of domestic companies abroad
[1] January – July
Source: National Bank of Serbia

According to National Bank of Serbia stattistics, FDI inflow in Serbia in February 2009. was $ 582 million. This is the fifth biggest monthly value of FDI inflow since 2000. Higher ammount of FDI than this was only in september 2003.(tobacco industries), august 2006. (Mobi063 and Hemofarm), february 2007. and december 2007. (bank recapitalizations).

In terms of the country structure, investors from the European Union lead the way accounting for about 85% of the total FDI inflow. The top spot on the country list is held by Austria, followed by Greece, Norway, Germany and Netherland, while significant investment also stems from the United States, Slovenia, France, Great Britain.

Figure 7. Net FDI in Cash by Countries, 2000–2007[11]

Net FDI in Cash by Countries (2000-2007)			
Country	Investment Value (USD 000)	Country	Investment Value (USD 000)
Austria	2,157,972	Italy	268,058
Greece	1,638,981	Switzerland	223,390
Norway	1,550,565	Montenegro	209,288
Germany	1,389,108	Croatia	153,259
Netherlands	553,357	Bulgaria	112,013
Slovenia	543,250	USA	78,073
France	425,273	Slovakia	66,221
Luxembourg	369,507	Latvia	52,920
Hungary	322,449	Israel	48,867
Great Britain	280,485	Belgium	47,701

NOTE: The National Bank of Serbia reports FDI data by country of payment and not by country of actual investment.
Source: National Bank of Serbia

[10] www.siepa.gov.rs/site/en/home/1/investing_in_serbia/strong_fdi_figures/
[11] www.siepa.gov.rs/site/en/home/1/investing_in_serbia/strong_fdi_figures/

Over the past three years, service sectors have proven to be the most attractive to international investors. The banking sector recorded the biggest FDI inflow of $3.7 billion, with telecommunications holding the second spot with $2.7 billion, while manufacturing sectors ranking third with $1.8 billion.

Figure 8. Inward FDI by Industries, 200□200□[12]

Inward FDI by Industries (2004-2007)	
Industry	**Total Investment (USD ths)**
Financial intermediation	3,850,600
Transport and telecommunications	2,284,276
Manufacturing	2,111,239
Wholesale, retail, repairs	1,454,873
Real estate, renting	1,255,575
Construction	248,943
Hotels and restaurants	66,537
Agriculture	53,342
Mining and quarrying	38,049
Electricity, gas, and water	2,970

Figure 9. Major foreign investors in Serbia, 2002□2009 (million euros)[13]

Leading Foreign Investors (2002-2009)				
Company	**Country**	**Industry**	**Investment Type**	**Investment Amount (EUR mn)**
Telenor	Norway	Telecommunications	Privatization	1,602
Gazprom Neft	Russia	Energy	Privatization	947
Philip Morris	USA	Tobacco	Privatization	611
Mobilkom	Austria	Telecommunications	Greenfield	570
Intesa Sanpaolo	Italy	Banking	Acquisition	508
Stada	Germany	Pharmaceutical	Acquisition	475
AB InBev	Belgium	Food	Acquisition	427
National Bank of Greece	Greece	Banking	Privatization	425
Mercator	Slovenia	Retail	Greenfield	240
Fondiaria SAI	Italy	Insurance	Privatization	220
Lukoil	Russia	Energy	Privatization	210
Airport City Belgrade	Israel	Real Estate	Greenfield	200
Blok 67 Associates	Austria&Serbia	Real Estate	Greenfield	180
Holcim	Switzerland	Construction	Privatization	170
OTP Bank	Hungary	Banking	Privatization	166
Carlsberg	Denmark	Food	Acquisition	152
U. S. Steel	USA	Metal	Privatization	150
METRO Cash & Carry	Germany	Wholesale	Greenfield	150
Coca-Cola	USA	Food	Acquisition	142
Lafarge	France	Construction	Privatization	141

Source: SIEPA

A list of top investors that transferred $1.5 billion in Serbia features blue–chip companies and banks, such as Microsoft, Coca Cola, Metro Cash & Carry, Michelin, Banca Intesa, Alpha Bank, Piraeus Bank and Credit Agricole. Serbia's strong FDI track–record is substantiated by internationally recognized awards given to the foreign investors. In 2005, German Metro Cash & Carry was named the Investor of the Year in South East Europe by OECD for the largest Greenfield investment in the re-

[12] www.siepa.gov.rs/site/en/home/1/investing_in_serbia/strong_fdi_figures/
[13] www.siepa.gov.rs/site/en/home/1/investing_in_serbia/strong_fdi_figures/

gion. The year before the winner was the US Ball Corporation's for their Greenfield project (the only real Greenfield until now). In 2006, Israeli Africa-Israel Corporation/Tidhar Group was the winner for their Airport City Belgrade real estate project.

Concerning major investors, the greatest FDI was attracted by Mobi 63, followed by Gazpron Neft, DIN and Mobilkom. As notable from the following table, most of the FDI were made through privatizations of state-owned companies and through acquisitions.

2.1. Intellectual property rights

Intellectual property rights (IPR) and regulations are of great importance for attracting FDI. Therefore, it is crucial for every country not just to have them but also to implement them efficiently, if it has serious intentions to attract foreign capital.

The history of protection of IPR in Serbia rests on European roots of this law. In 1883 the Kingdom of Serbia was one of the founders of, so called, Paris Union – one of 11 countries that signed Convention on the Protection of Industrial Property. However, many things have changed since the time when Serbia was signing down the Paris Convention. Not much time ago, Serbia, as a country in transition that experienced enormous problems during last 15 years, had plenty of laws that needed to be changed.

Serbia invested a lot of effort in raising IPR protection in last 6 years. Domestic rules concerning certain issues were not in compliance with international standards (i.e. WTO standards) and some of them did not even exist. Today, harmonization of IP legislation have already occured.

Today, Serbia has all the laws concerning the IP that are required and accepted internationally. According to PLAC[14], this situation is becoming better and more consideration is devoted to IPR. However, some of the old problems concerning the implementation of these laws, particulary infrigement, did not dissapear. Unfortunately, by stressing these facts out, Serbia is facing again deeply rooted corruption issues in society.

Figure 10. Progress in structural reforms (in grades)

Scores range from 1 (pure central planning) to 4+ (fully functioning market economy)

Source: *SIEPA*

[14] Policy and Legal Advice Centre, Belgrade. www.plac-yu.org

In addition, one of the greatest problems that Serbia faces is corruption, at all levels. This creates unfavourable business environment, not sufficiently stimulating for conducting business activities. Counter-corruptive strategies are underway but non-transparent methods of conducting certain affairs at home can reduce country's attractiveness to foreign investors[15].

2.2. Why focus on Greenfield?

A large number of studies assessing the impact of FDI on a host country suggest that entry of foreign-owned companies is associated with higher wages in local industry/economy, increased export orientation, industrial development and, under certain conditions, with higher growth[16]. As it is argued from the World Bank, the experience of transitional economies confirms the critical role of FDI in boosting export competitiveness.

Despite the difficult situation, considerable progress in macroeconomic stabilization in Serbia is accomplished. Prices, external trade and foreign exchange have been liberalized. Reintegration into the international system has been achieved. Fiscal transparency and modern budgetary planning have been introduced. The reform steps have enhanced public confidence and provided better investment environment. However, despite positive first generation reforms, Serbia still lags behind other transition economies in terms of trade openness and structural transformation. In order to foster additional reforms, it could use experience of other countries and further expand the scope and depth of its global integrations.

Additional foreign investments, particularly Greenfields, are very important for Serbia's future development. During last few years, Serbia had steadily inflows of FDI. However, there has been little Greenfield investment. Majority of FDI came from privatization and acquisition processes. Acquisition of local companies by foreign investors implies restructuring, which leads to increased productivity and exports. Higher productivity in any of foreign-owned firms is reflected onto higher wage levels in an industry. Consequently, attracting any form of FDI is more than important for development of Serbian market and economy[17].

Nonetheless, according to SIEPA[18] data, 77% of Serbia's state owned companies were privatized in 2005. Reforms in banking sector, which contributed a lot to amount of FDI, will rapidly come to an end. All this indicates that Serbia will have an absence of attractive investments soon. Based on the fact that citizens decided their self towards EU integrations, government should think in longer-run. Restrictions to FDI should be minimized in order not to loose precious time when all attractive companies will be privatized. In addition, focusing on attracting Greenfield would be crucial in near future.

Actually, Greenfield investments can be seen as FDI start-up. Consequently, they attract more capital in certain country, based on the fact that new facilities, plants, offices, warehouses are being built. This will generate more jobs and add to production capacity. Greenfield can also contribute to development of new industries within a country and open new opportunities for further investment in the value chain of the new industry. This kind of FDI has been essential for enterprises to increase the efficiency of their operations, modernize their production technology and expand stable commercial and production links with the supply chains of production and marketing, particularly those of EU[19].

Conclusion

Serbia`s example strongly supports the case that FDI can be described as a double-edge sword. In the period of great expansion (2004-2007) it shows the feature of FDI flows that its *share in total inflows*

[15] Sergi, Bruno. 2003. South-East Europe Review. Page 14.

[16] Popa, S. 2006. Not always welcome: Regime Type and the Regulation of FDI in Postcommunist Countries. P. 8.

[17] Ibid, page 8.

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[19] Kaminski, Bartlomiej and Francis Ng. 200 . "Trade and Production Fragmentation: Central European Economies in EU Networks of Production and Marketing," World Bank Policy Research Working Paper 2 .

is higher in riskier countries, those with risk measured either by countries' credit ratings for sovereign (government) debt or by other indicators of country risk. It also shows that FDI share is higher in countries where the quality of institutions is lower.

In the context of the present financial crises FDI seemed to be very sensitive to macroeconomic instability and adequate country risk in Serbia. It suggests that countries should be cautious about taking too uncritical attitude toward the benefits of FDI. It is the reason why a high share of FDI in total capital inflows may be a sign of, just the contrary, a host country's weakness rather than its strength. However, it is not the criticism against FDI itself. It is just the reason more for Serbia to concentrate on improving the environment for investment and the functioning of markets. In that way, FDI inflow would be more stabile during financial crises.

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DOING BUSINESS IN RESPONSIBLE MANNER: THE CASE OF ITALIAN INVESTORS ON THE SERBIAN MARKET[*]

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Abstract

The assumption of this project is that in addition to the profit and benefits for owners, corporations also affect the society and its development. Concurrently, the common concept is that socially responsible business positively affects corporation's financial results. However, management is not always aware of the correlation between corporation's long-term performance and respect for ethical standards and is often oriented to achieving short term goals. The question of ethics in business is especially present in the times of crisis, the crises we are facing now. In developed market economies, questions of ethical business are the focal points of interest, leading to creation of certain rules and standards. However, in an underdeveloped and societies in transition ethical business is often in the shadow of questions about profitability. Therefore, we believe that it is very important to discover how social responsible business is seen by corporations from developed countries that are operating in Republic of Serbia. Since Italy is one of the leading investors in the Serbian market, our goal is to explore relationship of Italian corporation towards their employees, natural environment and society.

Key words: *corporate social responsibility, stockholder theory, stakeholder theory, Italian investors, Serbia*

Introduction

Although *corporate social responsibility (CSR)* theme was a subject of many debates, especially in the last 0 years, idea of companies' social responsibility is as old as the concept of a *company*. The word *company* has its roots in Latin words *cum* and *panis* that mean "breaking bread together"[3], and shows that the original idea about company had social connotation. Since one overall definition of corporate social responsibly is not known, we will quote some of them.

Wikipedia, online encyclopaedia defines this concept as: "Corporate Social Responsibility (CSR), also known as corporate responsibility, corporate citizenship, responsible business, sustainable responsible business (SRB) and corporate social performance is a form of corporate self-regulation integrated into a business model. Ideally, CSR policy would function as a built-in, self-regulating mechanism whereby business would monitor and ensure their adherence to law, ethical standards, and international norms. Business would embrace responsibility for the impact of their activities on the environment, consumers, employees, communities, stakeholders and all other members of the public sphere. Furthermore, business would proactively promote the public interest by encouraging community growth and development, and voluntarily eliminating practices that harm the public sphere, regardless of legality."[4]

The World Business Council for Sustainable Development defines CSR as "the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at

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[3] "A Guide to Corporate Social Responsibility", Miami University

[4] **Source:** *http://en.wikipedia.org/wiki/Corporate_social_responsibility*

large"[5]. As per United Nations, "CSR can be defined as the overall contribution of business to sustainable development".

International Financial Corporation defines corporate social responsibility as fallowing: "Corporate social responsibility is the commitment of businesses to contribute to sustainable economic development by working with employees, their families, the local community and society at large to improve their lives in ways that are good for business and for development"[6].

However, term corporate social responsibility is not related only to big corporations, but also entrepreneurs, small and medium sized companies also should operate socially responsible. Then, the term responsible entrepreneurship[7] means implementing company's economical success with taking into consideration benefits of broader society and controlling effects on environment. In the other words, companies should satisfy customers' needs while respecting expectations of other interest groups such as employees, suppliers and local community. Responsible entrepreneurs and small and medium companies bring direct benefits to the company and insures its long term competitiveness[8].

We can conclude that corporate social responsibility demonstrates self regulation mechanism – the way companies manage their economical, societal and ecological influence and their relations with all interest groups[9]. This term does not imply only what companies' do with their profits, but also how they make profits. It outgrows the concept of philanthropy or respect of low and rules, and also implies company's contribution to sustainable development. In addition, social responsibility is not expected only from big corporations, but also from small and medium-sized enterprises. Finally, activities we find socially responsible not only benefit interest groups, but also have positive effects on the company itself.

1. Corporate responsibility

The question that comes to the mind when we are talking about corporate social responsibility is: "What for and to whom are the companies responsible " there are two main answers that can be fined in the relevant literature. One was given by the classical theory of social responsibility - stockholder theory. According to this theory the primary responsibility of the company is the responsibility towards owners (stock holders), and profit making which increase the value for owners/ stock holders is the main business goal. On the other hand, representatives of the theory of interest groups (stakeholder theory) believe that the company has responsibility towards everyone included in its operations, or individuals and groups who carry certain risk (stake)[10] in the business.

Milton Friedman is known for its understanding that profit increase, made while respecting "rules of the game"[11] and low regulations, is the only social responsibility of companies, and managers, as the representatives of stockholders, have the responsibility for their financial benefits[12]. The government should be responsible for resolving social problems. He believes that the requirement for companies to participate in achieving "social goals" (after they paid their taxes) would be unnecessary burden for company which management cannot be competent for solving social problems. Under the conditions of the free market economy, the biggest responsibility for a company, or a manager that manages it, is profitable business. Every other goal is in the shadow of the main goal and can be justified if it is in function of profit increase.

5 **Source:** *http: www.wbcsd.org templates Template BCSD layout.asp?type p MenuId MTE0OQ*

6 **Source:** *www.ifc.org*

7 "Introduction to Corporate Social Responsibility for Small and Medium Sized Enterprises", European Commission Directorate General for Enterprise, pg. 2.

8 The same as above

9 Interest group or stakeholder is everyone who affects or can be affected by a corporation's actions

10 "The amount of mony which you risk on the result of something such as a game or competition", Cambridge Advanced Learner's Dicrtionary

11 Under "rules of the game" Friedman alludes customs with binding power irrespective of their lawful formality.

12 Friedman, M: "The Social Responsibility of Business Is to Increase Its Profits", *ew ork Times Magazine*, September 13, 1970.

On the other hand, R. Edward Freeman[13] thinks that owners, as well as customers, suppliers, managers, employees and local community have a certain "stake" in the company and because of that they take some risks. Therefore, when setting company's goals the interests of every mentioned group need to be taken into the consideration. The company is responsible towards each of the interest group (stake-holder)[14]. Also, every interest group can positively or negatively influence the company and in some moments could be of the crucial importance for company's success and survival. Therefore, none of them should be the instrument for achieving the end goal (especially not consumers, employees, suppliers and local community), and the needs of all of them should be incorporated into company goals.

Although they seem on the different ends of continuum, two presented approaches to social responsibility could bridge their differences. Followers of the stakeholder theory emphasise good relationships with all interest groups as crucial for company's competitiveness and long term success. They don't minimize the importance of profitability and long term financial success, but emphasise that corporate social responsibility is the way to secure financial results and at the same time responsible relationship with stakeholders. As it is mentioned above, Friedman stated that company have to operate according to the "rules of the game". We could say that in four decades time after Friedman wrote his article, "the rules of the game" have changed. Although in modern business world companies that do not make profit cannot survive on the market (making profit is still the ultimate goal) the concept of profitability is changed. Today profit seen as the goodwill, credibility and trust given to the company by the society is more valuable then the profit in terms of money and return on investment. The company's image depends on people's satisfaction – costumers, suppliers, employees and the local community etc., and long term success and survival is enabled when company's activities are balanced with the society's interests, or what Peter Draker says, every company is the part of the society and has a function in the society[15].

Today is quite clear that companies are not isolated entities in society that have only purpose to bring the profit to their owners with respecting low (or on the edge of the low). Their operations need to be purposeful to the people who are using their products in order for the company to survive. That means companies have responsibility towards their customers who are the part of the society. Furthermore, companies employ people who are parts of the society and whose lives are happening outside of the company. The ways companies treat their employees affect employees' families, their security, health, knowledge, skills, relations, value systems and culture, which makes the basis for social capital. In addition, companies in their operations use resources of the society and they are required to behave responsible towards current and future generations. Companies affect local community's development and stability as well as social peace and government stability. Other interest groups (suppliers, creditors, investors, managers) have long term interest for social responsible operating, because it provides increased level of trust as the requirement for longer, cheaper and more successful business relationships. Finally, companies are not abandoned and isolated islands but are interconnected and dependent on the society. Consequently, they cannot look at the social environment without care. To conclude, companies are social entities that have the huge capacities (knowledge, money, technology) and could influence the society and its development, for its own and the benefit of the broader society.

In the modern discussions about corporate social responsibility, the benefits of social responsibility for businesses are often emphasised. Therefore, it seems that corporate social responsibility is, said in Friedman's words, only "cloak" under the companies "hide" their main motive –profit, however we define it. Hence, it is important to clarify if the companies act socially responsible because this is their

[13] Freeman R.E.: A Stakeholder Theory of the Modern Corporation, printed in „Ethical Theory and Business", prepared by: Beauchamp T. & Bowie N, Prentice Hall/Pearson 2004 pg. 67.

[14] It should be mentioned than in literature exist more developed stakeholders' schemas other than Freeman's six interest groups. Donaldson and Preston emphasize eight interest groups: investors, employees, consumers, managers, suppliers, community, government and political groups, while J. R. Lucas mentions eleven interest groups: shareholders (owners, employers), employees and managers, shoppers/clients, suppliers, creditors, competition, industry branch or whole professions, local community, government, international community, mankind, and environment (cited from: J. Babi : "Corporate Social Responsibility", Faculty of Philosophy, Belgrade)

[15] Cited from: Paliwal M.: Business Ethics, New Age International Publishers, 2006, pg. 64.

moral obligation or because they are securing profit increase? In answering this question we can use analogies from psychological and sociological research, which show us in what instances the altruist is the best person for cooperation[16]. If we are in the relationship with someone, we would want that person to be reliable and ready to fulfil responsibilities regardless of opportunistic behaviour obtaining more benefits (for example, an employer wants his employee not to cheat even when they have opportunity to do so without consequences). However, if someone behaves altruistically because he/she can gain something, his/her partner would know that he/she would behave opportunistic if there is no gain. Therefore, the best business partner is not someone who behaves altruistically because of the personal gain, but someone who behaves ethically and altruistically regardless of consequences for this behaviour. Hence, we could conclude that the company that behaves socially responsible because it expects positive effects of that behaviour would be seen as cynical and would sustain positive effects of the behaviour, while the one that truly maintains stakeholder's interests would be rewarded.

2. Responsible business and multinational companies

Term socially responsible business is mostly connected with companies from which we expect certain social responsibility and engagement. The question of social responsibility is raised in correlation to international corporation businesses. From 1990 to 2001 the number of multinationals almost doubled and their franchises quarrelled. The size and the wealth of individual companies also boosted. Some companies increased their profits using their host countries weak lows, low wages, possibility of breaking human rights and endangering survival of natural environment. All these influenced on the different activists to undertake certain measures, from boycotts to demonstrations.

While in the western world non profit organisation and consumer groups pressured companies to take certain social responsibilities, in countries that went through transition practice of socially responsible business had a different history. In post- communist societies, belief that companies have social role is not new. In the period of socialism government was the owner of companies and business was seen primarily from societal and social angle. Companies were seen as the main protagonists of social development and they built cultural and sports centres, social housing and provided other benefits to local communities. Those activities were the part of ideology that guaranteed social wealth and security, but were not lead by economical efficiency. When during the 90s they transitioned to the market business model and privatisation of government/societal companies took place, new owners were lead by private interests and market calculations. Often, they neglected social context and the needs of interest groups. In addition, privatisation process was followed by corruption and non- transparency, which led post- transitional society to loose trust in new companies and their management.

Unlike West, where the companies were watched by civil sector and under their influence had to take different responsibilities and activities, in post-socialistic societies, foreign investors were the leaders in initiating socially responsible businesses. Entering the counties in transition, western companies took on leading roles in developing not only new technologies but also new values and culture. Furthermore, starting the initiative for the global agreement (The Global Compact) whose members agreed to respect international criteria for protecting natural environment, respecting human and workers rights and to fight against corruption, Untied Nations have been significant contributor to developing companies' conciseness regarding social responsibilities since 2000. Many countries that are going through or went thorough transitions accepted Global Agreement - the Republic of Serbia also became a member in 2007. This is a very important step towards strategic approach to socially responsible business. Because the core of the responsible business concept is not known to the companies in transitioning economies, they need to be educated through programs and project provided by international and government organisations[17]. However, it should be stressed that the investors coming from the countries where the corporate social activities are the common practice implement this concept into the frontier markets, such as Serbian.

[16] Cited from: Bowie N.: "New Directions in Corporate Social Responsibility", printed in "Ethical Theory and Business", prepared by: Beauchamp T. & Bowie N., Prentice Hall/Pearson 2004 pg. 101.

[17] One of them is a regional project "Corporate social responsibility setup in Southeastern Europe", which Serbia joined 2007 with financial help of the German government.

3. Italian investors in Serbia and corporate social responsibility

One of the leading investors in Republic of Serbia is Italy. Italy is also the main Serbian partner in international trade. From the small textile companies to the big banks, numbers of Italian companies are operating in Serbian market[18]. Italian economic partnership is especially important if we take into consideration geographic, historical and cultural relations with Serbia. At the same time, Italy is the member of European Union with accepted European business standards that include social responsibility. Therefore, our analyses, on this occasion, were focused on the companies which are partially or completely owned by Italian companies or individuals.

The "Awareness-raising questionnaire" suggested by the European Commission Directorate General for Enterprises[19] was used in this research. Although, we got informed that there are around two hundred Italian investors operating in Serbia[20], we succeed in finding seventy e mail addresses on which the questionnaires were sent. Ten companies of different size – ranging from big international companies (with more then 250 employees and several million revenue) to medium-sized companies and small entrepreneurs, which operate in various sectors – ranging from transportation and construction to industry and financial sector, were willing to participate in this research. The questionnaire included five groups of questions related to the workplace, environmental, marketplace and community policies, as well as company values. The respondents were asked to evaluate their attitudes and practices regarding corporate social responsibility. The results of the analyses are summarised in the text that fallows. Since our sample included relatively small number of companies, the answers are provided in the tables in absolute numbers.

3.1. Workplace Policies

The long-term success of any business often depends on the knowledge, skills, talent, innovative creativity and the motivation of its employees. Although complying with legislation covering employment, workplace health and safety issues can ensure that an enterprise provides for its workers' basic needs, visible commitment to the improvement of their job satisfaction, career development and personal welfare will demonstrate that the company really values them as individuals – and that values their contribution to the business success. Involving the employees will allow the company to get more from them in terms of ideas, commitment and loyalty, enhancing the effectiveness. Employees are the frontline troops of most businesses and may often see problems and solutions even before the management does. Effective internal partnerships also create relationships that improve the business' flexibility, responsiveness and ability to share knowledge between workers. Motivated staffs often lead to a stable, contented workforce and help to build a good reputation for the company.

[18] "International Business Sector in Serbia", Alliance International Media, March 2009, pg.78.

[19] **Source:** *http://ec.europa.eu/enterprise/csr/index_en.htm*

[20] Fabio Corsi, director of Italian institute for international trade, states that to this day there are two hundred Italian companies on the Serbian market, Alliance International Media : "International Business Sector in Serbia", March 200

Table 1. Workplace policies of the Italian investors operating at Serbian market

	Yes	No	In part	Don know	Other
1. Do you organize any kind of training and education for your employees?	2	1	7	/	/
2. Do you consult with employees on important issues?	6	/	4	/	/
3. Does your enterprise have suitable arrangements for health, safety and welfare that provide sufficient protection for your employees?	8	/	2	/	/
4. Does your enterprise actively offer a flexible working hours or allow employees to work from home?	3	5	2	/	/

According to the results of our research, almost all sampled Italian investors operating in Serbia give particular attention to the employees'' education and training. All companies quoted that they organize some kind of training for their workers – two company's do that on regular bases and seven provide training occasionally, which could be noticed in the Table 1.

It could be concluded, based on the answers provided in the questionnaire, that Italian investors practice participative management, in other words, their managers consult the employees on important issues. Care for the suitable arrangements for health, safety and welfare that provide sufficient protection for the employees, is another important aspect of the company's reasonability towards its workers in which Italian investors show particular concern. Flexible working hours show the willingness of employers to adapt to the needs of employees and enable a good work-life balance for them. The analyses indicate that, regardless of the good experience of developed countries, these practices are not yet present in wide range in our conditions. In some work processes the flexibility is not possible and that could be one of the reasons why so many of our respondents do not offer this kind of opportunities to their workers. However, we also believe that due to certain habits and the need for control over workers in the transition period, the companies do not actively offer flexible working hours or allow employees to work from home.

3.2. Environmental policies

All companies, regardless of size or sector, can have positive and negative impacts on the environment. Negative impacts arise through the direct or indirect consumption of energy and resources, the generation of waste and pollutants and the destruction of natural habitats. Every enterprise can help by reducing energy consumption, by minimising waste and by recycling materials. Even modest improvements can make a profound difference when aggregated with the efforts of other businesses.

Environmental degradation is both a global and a local problem of increasing concern throughout society, and therefore also among the companies' customers and good environmental performance often makes financial sense. Energy efficiency, pollution prevention, waste minimisation and recycling can all result in significant cost-reductions for the business, as well as other benefits such as ensuring compliance with environmental regulations, improving the relationship between the enterprise and the local community, motivating the employees and making the customers more loyal. All of these benefits clearly contribute to the long-term sustainability and success of the company.

According to their responses, more that most of the Italian investors at the Serbian market have tried to reduce their companies' environmental impact in terms of: sustainable transport options (5 respondents), protection of the natural environment (7), pollution prevention (7), waste minimisation and recycling (9), as well as energy conservation (6), which could be seen in the Table 2. Six companies think they can save money by reducing its environmental impact and the same number consider environmental impacts when developing new products or services. Four of the respondents supply clear and accurate environmental information on its products, services and activities to customers, suppliers, local community, etc, while four of them provide partial information. Finally, a half of the respondents can think on the ways in which their enterprise could use the sustainability of its products and services to gain an advantage over competitors at Serbian market and two of them can partly think of them, while three of them do not see any ways for using products/services sustainability as a market advantage.

Table 2. Environmental policies of the Italian investors operating at Serbian market

	Yes	**No**	**In part**	**Don know**	**Other**
. Have you tried to reduce your enterprise's environmental impact in terms of:					
a) energy conservation?	6	2	2	/	/
b) waste minimisation and recycling?	9	/	1	/	/
c) pollution prevention	7	/	/	1	2
d) protection of the natural environment?	7	/	1	/	2
e) sustainable transport options?	5	1	4	/	/
2. Can your enterprise save money by reducing its environmental impact?	6		4		
	Yes	**No**	**In part**	**Don know**	**Other**
3. Do you consider the potential environmental impacts when developing new products and services?	6		3	1	
4. Does your enterprise supply clear and accurate environmental information on its products, services and activities to customers, suppliers, local community, etc?	4	2	4		
5. Can you think of ways in which your enterprise could use the sustainability of its products and services to gain an advantage over competitors at Serbian market?	5	3	2		

3.3. Marketplace policies

Enterprises are basically human' organisations that rely on a web of internal and external relationships which are vital for mutual prosperity. The way in which these working relationships are managed is often vital for the enterprise's success on the market. Good relations with customers and suppliers bring gains for both sides. Sharing the experiences with business partners is a good example of networking, which is usually critical to success. Furthermore, the reputation is crucial to ensure success in the marketplace. An enterprise could achieve a good reputation by satisfying customers, settling invoices on time and remaining committed to ethical business practices.

Table 3. Marketplace policies of the Italian investors operating at Serbian market

	Yes	No	In part	Don know	Other
1. Does your company have a policy to ensure honesty and quality in all its contracts, dealings and advertising?	9	/	1	/	/
2. Does your company supply clear and accurate information and labelling about products and services, including its after-sales obligations?	7	1	2	/	/
3. Does your business ensure timely payment of suppliers' invoices	5	/	5	/	/
4. Does your company have a process to ensure effective feedback, consultation and/or dialogue with customers, suppliers and the other people you do business with?	10	/	/	/	/
5. Does your company work together with other companies or other organisations to address issues raised by responsible business?	5	2	3	/	/

Nine of the sampled Italian companies have a policy to ensure honesty and quality in all its contracts, dealings and advertising and one have it partly. Seven of them supply clear and accurate information and labelling about products and services, including their after-sales obligations, while one do not provide any clear and accurate information and labelling. A half of the respondents ensure timely payment of suppliers' invoices, and the other half ensures it partly, while all the respondents have a process to ensure effective feedback, consultation and/or dialogue with customers, suppliers and the other people they do business with. Finally, a half of the companies work together with other companies or other organisations to address issues raised by responsible business and three partly work with others regarding corporate social responsibility. These results are presented in the Table 3.

3.4. Community policies

We pointed out in this paper that there is a clear connection between a healthy and profitable business and the wellbeing of the community around it. Most businesses are an integral part of their communities and have an active involvement with local aspirations and activities. Such enterprises enjoy benefits like: valuable networking and links with other local enterprises; increased customer recognition and esteem; enhanced company reputation; and improved staff recruitment and retention. However, being a good neighbour is not just about having respect for others in the immediate vicinity. Community support can include anything that benefits the community, such as sponsorship or the provision of time and expertise. It might cover participation in local sporting, educational or cultural initiatives. Helping to tackle social issues such as crime-prevention or long-term unemployment in the local area may also help the long-term financial success of the business. Being positively engaged in the local community can also help in identifying new markets, customers or business opportunities, building contacts with local authorities and opinion-leaders, and facilitating new partnerships with other businesses on community projects.

Only three of the analysed Italian companies offer training opportunities to people from the local community (e.g. apprenticeships or work experience for the young or for disadvantaged groups) and three do that in part, while four of them do not offer any training to people from the local community. One half of the respondents have an open dialogue with the local community on adverse, controversial or sensitive issues that involve the company. Three of the companies try to purchase locally and five of them do that in part. Four companies encourage their employees to participate in local community activities such as providing employee time and expertise, or other practical help, while three do not actively support their employees to participate in local community activities. Finally, eight respondents give financial support to local community activities and projects.

Although activities and attitudes of the Italian investors regarding the local community could be seen as socially responsible, from the data presented in the Table 4 it is evident that the most negative answers are given for this aspect of responsible behaviour. Therefore, we can conclude that these companies do not have significant influence on the development in their local communities.

Table 4. Community policies of the Italian investors operating at Serbian market

	Yes	No	In part	Don know	Other
1. Does your company offer training opportunities to people from the local community (e.g. apprenticeships or work experience for the young or for disadvantaged Groups)?	3	4	3	/	/
2. Do you have an open dialogue with the local community on adverse, controversial or sensitive issues that involve your company (e.g. accumulation of waste outside your premises, vehicles obstructing roads or footpaths)?	5	3	1	/	1
3. Does your enterprise try to purchase locally?	3	1	5	1	/
4. Are your employees encouraged to participate in local community activities (e.g. providing employee time and expertise, or other practical help)?	4	3	2	1	/
5. Does your enterprise give any financial support to local community activities and projects (e.g. charitable donations or sponsorship)?	8	/	2		/

3.5. Company values

A company's core values and principles, and its commitment to them, are inextricably linked with its reputation. People like to work for and with others who share their values, so setting company values may help the company attract employees, customers, suppliers and investors who approve of its principles. Therefore, the company should promote high standards in the workplace and deal positively with the interests and concerns of its employees, customers, suppliers and the local community. The values should provide clear and consistent guidance on how to handle situations that pose dilemmas or conflicts of interest.

According to our research, most of the respondents have clearly defined their values and rules of conduct. Moreover, the companies communicate their company's values to customers, business partners, suppliers and other interested parties and believe that their customers are aware of the company's values and rules of conduct. Furthermore, most of them think that their employees are aware of the company's values and rules of conduct and they train employees on the importance of the corporate values for the company's success. The data presented in the Table 5 indicate that not only do foreign investors implement new technology or invest money, but they also bring their corporate values and culture.

Table 5. Company values of the Italian investors operating at Serbian market

	Yes	No	In part	Don know	Other
1. Have your company clearly defined its values and rules of conduct?	8	/	2	/	/
2. Do you communicate your company's values to customers, business partners, suppliers and other interested parties (e.g. in sales presentations, marketing material or informal communication)?	7	1	2	/	/
3. Are your customers aware of your company's values and rules of conduct?	7	1	2	/	/
4. Are your employees aware of your company's values and rules of conduct?	8	/	2	/	/
5. Do you train employees on the importance of your enterprise's values and rules of conduct?	8	1	1	/	/

Conclusion

In this paper, we pointed out the importance of responsible business both for the natural and social environment, and the company which want to survive and make progress in such an environment. We briefly presented the various debates on corporate social responsibility, which have been in the focus of concern in the West for several decades. Regardless they are small business or big multinationals, the western companies are aware of the necessity of compliance with ethical norms for their economic success and they undertake different socially responsible activities.

It is known that countries that have passed through the processes of transition towards market economy have experienced numerous violations of ethical norms and that they lack adequate principles of business and rules of conduct. Therefore, the presence of investors from developed markets, where high ethical standards have to be obeyed and where costumers, employees and other stakeholders expect some kind of corporate responsibility, is essential for the frontier markets, such as Serbian.

As significant investors, Italian companies are recognized as an important factor in introducing new "rules of the game" on the Serbian market and therefore the subject of our analyses were the companies which are partially or completely owned by Italian companies or individuals. On the basis of the answers to the different questions about their relationship with employees, natural environment, business partners and the local community, as well as corporate values, we can conclude that the Italian companies that operate at Serbian market are aware of the importance of compliance with ethical standards, and that they practice a variety of activities that are considered socially responsible. Although we must be careful regarding the objectivity of the assessment since the analysis is based on companies' self-evaluation, we think that the fact that companies were interested to participate in our research and information that we received through the questionnaire, indicate that the Italian investors are aware of the importance of corporate social responsibility.

In particular, we can point out that companies that were the subject of our analysis have recognized the importance of corporate values for their market success and that they communicate them with their business partners. Furthermore, we can conclude that the majority of companies have the responsible attitude toward the natural environment, as well as employees and business partners, and that they practice some kind of socially responsible activities. However, the number of companies that provide an active support to the local community is relatively small, with the exception of financial support which is provided by the majority of companies.

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