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# **EMPLOYMENT, EDUCATION AND ENTREPRENEURSHIP**

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## **ENTREPRENEURSHIP: FACTORS AFFECTING SMALL- SCALE BUSINESS PERFORMANCE AND DEVELOPMENT**







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## **CONTENTS**

<b><i>I PART. ENTREPRENEURSHIP DEVELOPMENT &amp; FIRM PERFORMANCE .....</i></b>	<b><i>13</i></b>
<b><i>THE DIGITALIZATION ERA CHALLENGES FOR THE ORGANIZATION OF XXI CENTURY .....</i></b>	<b><i>15</i></b>
SASA TRANDAFILOVIC, PhD IVANA CVETKOVIC	
<b><i>THE ROLE OF FREE ZONES, TECHNOLOGY PARKS AND BUSINESS INCUBATORS IN THE DEVELOPMENT OF SMALL AND MEDIUM ENTERPRISES .....</i></b>	<b><i>30</i></b>
MOMCILO ZIVKOVIC, PhD VUK BEVANDA, PhD	
<b><i>DOWNSIZING AS A MEASURE FOR THE INCREASE OF EFFICIENCY AND FLEXIBILITY OF AN ENTREPRISE.....</i></b>	<b><i>50</i></b>
NENAD RAVIC, MA VLADO RADIC, PhD	
<b><i>MARKET ORIENTATION AND BUSINESS PERFORMANCE .....</i></b>	<b><i>67</i></b>
VLADO RADIC, PhD, JOVANKA POPOVIC, PhD	
<b><i>BUSINESS IMPROVING WITH CLOUD COMPUTING TECHNOLOGY .....</i></b>	<b><i>98</i></b>
DJORDJE ILIC, MA, MARIJA MARKOVIC BLAGOJEVIC, MA	
<b><i>APPLICATION OF BUSINESS INTELLIGENCE AND OLAP TECHNOLOGY IN BUSINESS DECISION-MAKING.....</i></b>	<b><i>118</i></b>
JOVAN ZIVADINOVIC, PhD ZORICA MEDIC, PhD	
<b><i>LEAN LEADERSHIP AS A PRECONDITION FOR SUCCESSFUL BUSINESS OPERATIONS OF ENTERPRISES .....</i></b>	<b><i>140</i></b>
SAVETA VUKADINOVIC, MA JOVANKA POPOVIC, PhD	
<b><i>THE RESEARCH OF THE ECONOMIC EFFECTS OF STANDARDIZATION.....</i></b>	<b><i>159</i></b>
MILAN KRSTIC, PhD ANA SKORUP, PhD	
<b><i>COMPANIES RESTRUCTURING - MYTHS AND MISCONCEPTIONS .....</i></b>	<b><i>184</i></b>
SLAVICA ANDJELIC, PhD NEMANJA DAMNJANOVIC, PhD	

<b><i>BUSINESS NEGOTIATION.....</i></b>	<b><i>204</i></b>
VLAJKO PETKOVIC, PhD ZORANA PETKOVIC	
<b><i>AMICABLE FINANCIAL RESTRUCTURING OF COMPANIES IN REPUBLIC OF SERBIA.....</i></b>	<b><i>225</i></b>
VLADIMIR KOZAR, PhD ANA OPACIC, PhD	
<b><i>THE ADOPTION OF OPEN INNOVATION PRACTICES IN SERBIAN ICT INDUSTRY.....</i></b>	<b><i>241</i></b>
JELENA LUKIC, MA	
<b><i>II PART. SOCIOLOGICAL AND SOCIAL PSYCHOLOGICAL ASPECTS OF ENTREPRENEURSHIP .....</i></b>	<b><i>259</i></b>
<b><i>ROLE STRESSORS AND ORGANIZATIONAL COMMITMENT: EMPIRICAL RESEARCH .....</i></b>	<b><i>261</i></b>
PLAMA HRISTOVA, PhD ALBENA KRUMOVA, PhD JULIKA NOVKOVA	
<b><i>DEVELOPING BUSINESS CULTURE THROUGH MOTIVATION AND CONFLICT MANAGEMENT .....</i></b>	<b><i>275</i></b>
ZARKO PAVIC, PhD MARIJA CUKANOVIC KARAVIDIC, PhD	
<b><i>THE TRANSFORMATION OF TRADITIONAL ORGANIZATIONS TOWARDS A MODERN APPROACH BASED ON QUALITY MANAGEMENT AND EMPLOYEE MOTIVATION .....</i></b>	<b><i>295</i></b>
MARINA GASIC, MSc	
<b><i>ENABLING EMOTIONAL INTELLIGENCE: EXPLORING THE SOURCE OF MOTIVATION.....</i></b>	<b><i>307</i></b>
VAIBHAV BIRWATKAR, PhD	
<b><i>THE MORAL VALUES OF BUSINESS IN VIRTUAL ORGANIZATIONS .....</i></b>	<b><i>325</i></b>
KATARINA MAJSTOROVIC, MA DEJAN RADULOVIC, PhD	
<b><i>ORGANIZATIONAL DIAGNOSIS AND MANAGEMENT OF CHANGE IN ORGANIZATIONAL CULTURE OF BANK INSTITUTION.....</i></b>	<b><i>338</i></b>
MIRYANA STANCHEVA, PhD SNEZHANA ILIEVA, PhD	
<b><i>STAFF MANAGMENT AND EVALUATING THE STAFF EFFICACY.....</i></b>	<b><i>349</i></b>
BORKO SOMBORAC, MA DEJAN ILIC, PhD	

<b><i>EMPLOYEE PERFORMANCE AND DEVELOPMENT: ALCOHOL AND ITS EFFECT ON ORGANISATIONAL PERFORMANCE.....</i></b>	<b>368</b>
SAMUEL OSEI-NIMO, PhD IMANI SILVER KYARUZI, PhD	
<b><i>REFORM OF THE HUMAN RESOURCES MANAGEMENT FUNCTION IN THE MINISTRY OF INTERIOR OF THE REPUBLIC OF SERBIA - THE STRATEGIC BASIS, KEY ACTIVITIES AND CHALLENGES .....</i></b>	<b>379</b>
MILAN KLISARIC, PhD SINISA DOSTIC, PhD	
<b><i>III PART. PART CASE STUDIES.....</i></b>	<b>401</b>
<b><i>INNOVATIVE GLOBAL COMPANIES – SOME CASE STUDIES.....</i></b>	<b>403</b>
MIRJANA RADOVIC MARKOVIC, PhD SLADJANA VUJICIC, MA	
<b><i>PROFESSIONAL EDUCATION AND YOUTH EMPOWERMENT THROUGH ENTREPRENEURSHIP FOR SOCIO-ECONOMIC DEVELOPMENT IN NIGERIA .....</i></b>	<b>418</b>
ISAAC ELIJAH ESEMA, PhD SASA STEFANOVIC	
<b><i>FEMALE ENTREPRENEURSHIP AND THE WOMEN CHAMBER OF COMMERCE AND INDUSTRY: ECONOMIC EMANCIPATION AND CLOUT FOR PAKISTANI WOMEN .....</i></b>	<b>431</b>
IQBAL KHAN	
<b><i>IMPORTANCE OF OWNERSHIP TRANSFER PLANNING FOR FAMILY BUSINESS ENTITIES.....</i></b>	<b>458</b>
DRAGAN MILOSEVIC, PhD DRAGICA JOVANCEVIC, PhD	
<b><i>THOUGHTS ON ENTREPRENEURSHIP AND ITS LINKAGE WITH INTRAPRENEURSHIP: IMPLICATIONS FOR ECONOMIC DEVELOPMENT.....</i></b>	<b>482</b>
MUHAMMAD OMOLAJA, PhD ANA ALEKSIC	
<b><i>JOURNEY OF A SMALL TOWN ENTREPRENEUR : AN INDIAN CASE STUDY.....</i></b>	<b>498</b>
REENA AGRAWAL, PhD	
<b><i>THE APPLICATION OF THE EU PUBLIC SERVICES GUIDELINES IN SERBIAN PUBLIC ENTERPRISES.....</i></b>	<b>507</b>
DALIBORKA PETROVIC, PhD TIHOMIR GLIGORIC, PhD	
<b><i>NEW SYSTEM OF ASSOCIATION CORNER SHOP'S IN SERBIA... </i></b>	<b>523</b>
NEMANJA DAMNJANOVIC, PhD, SLAVICA ANDJELIC, PhD	



## ***FOREWORD***

This book is the fourth in sequence, and it relates to issues of entrepreneurship. It was preceded by the following books Entrepreneurship (2012), Entrepreneurship: Economic Development & Finance (2013), and Gender, IT and Marketing Issues in Entrepreneurship (2013). For the past few years, in this way, we have been forming and expanding the existing library in this multidisciplinary field, to which we permanently add new aspects and develop existing concepts.

National and international experts are participating in creating the entrepreneurial library. With their research papers, they always open some new topics and inspire us to focus and dedicate our special knowledge to those topics, which is also the case with this new monograph. Namely, this one is different from the previous publications from the field of entrepreneurship where the role of entrepreneurship in economic development and financial, gender, marketing and informatics aspects were considered. Publication Entrepreneurship: Factors Affecting Small-Scale Business Performance and Development joined economic, psychological, social and other factors which influence the characteristics and development of entrepreneurship, as well as entrepreneurial behaviour.

Monograph has three parts:

I Part. Entrepreneurship development & Firm performance

II Part. Sociological and socio-psychological aspects of entrepreneurship

III Part. Case Studies.

The first part analyses the possibilities of measuring and improvement of business results of small enterprises. Effects of different factors on achieving the ultimate business results are taken into consideration. Considering that improvement of organizations' performances in modern business is more important than ever, this issue rightfully takes the central place in this publication. The remaining parts are in its function and represent a connected whole.

The second part of the monograph considers the issues connected to socio-psychological aspects of entrepreneurship (motivation, emotional intelligence, stress management etc.).

The third part consists of case studies, which are original researches done from the aspects of various kinds and categories of entrepreneurs put into global, regional or national context. They give us a special insight in these issues and possibility to understand and solve the problems existing in Europe, Asia or Africa. At the same time, this enables us to understand the differences and similarities, which exist in certain countries and parts of the world through the vision of development and management of entrepreneurial activities.

It is our opinion that this concept of the book will at the same time be useful and interesting to readers. Because of the limited number of pages, we reached some of the factors and analysed them, which only sets the discussion into motion and invites new opinions and analyses regarding this edition's topic. Enriching this field, from year to year, can be seen as our obligation, which is one of the basic of the Faculty of Business Economics and Entrepreneurship (BEE) from Belgrade – publisher of all previous editions.

August, 2014.

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***I PART.***  
***ENTREPRENEURSHIP***  
***DEVELOPMENT & FIRM PERFORMANCE***





# **THE DIGITALIZATION ERA CHALLENGES FOR THE ORGANIZATION OF XXI CENTURY**

*Sasa Trandafilovic, PhD<sup>1</sup>*

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## **ABSTRACT**

*In today's business environment, and under the influence of globalization and advances in the field of information technology, organizations are facing increasing demands for information processing. In order to respond to the demands of the current business context, modern organizations are finding the solution in creating adequate capacity and infrastructure to support the establishment of harmony between the external and internal factors of the design of organization. The phenomenon of "Big Data" is the most important creation of the modern environment that pervades and influences all the elements of organizational design. That is why the importance of creating a digital business function that represents the core of experts in the field of modern technology is more and more emphasized. These experts affect the company to keep pace with the new environment through finding new ideas, sharing knowledge and experiences and applying them in the organization.*

**Key words:** *Big Data, Digitization, Organizational Processes, Organizational Design, Digital Skills and Knowledge*

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## ***INTRODUCTION***

Business context for modern organizations becomes more and more dynamic, complex and heterogeneous, due to the increased interdependence at the global level and taking advantage of improvements in information technology.

Modern environment is bringing the creation of new phenomena that affects all the elements of the organization and that changes its characteristics. In such circumstances, companies must constantly adapt to changes in order to establish a balance between internal (strategy and organizational design) and external (environment) organizational factors.

Starting with the key challenges of the Digital Era and with the need for adaptation, the aim of this paper is to identify: 1. Which is a key phenomenon of the Digitization Era and its features; 2 How and in what manner the phenomenon of "Big Data" influences the definition of the strategic orientation of modern organizations, as well as the process of organizational design; 3. What is the role and place of digital functions in the modern organization.

Characteristics of the "Big Data" as a key phenomenon of the Digital Era are presented in the first part of this paper. Then, changes in the strategic orientation of the company, formed under the influence of the phenomenon of "Big Data" are defined. Also, it presents the key changes in the organizational design in the Era of Digitization, viewed through the prism of Galbraith's *Star Model*. In the end it emphasizes the role of digital functions in terms of the sustainable development of the modern organization, with presentation of appropriate conclusions.

## ***BIG DATA - CURRENT CHALLENGE***

The changes that marked the end of the XX century had a great impact on modern business organization. New global markets have become highly competitive, with demand for continual adjusting the strategy and structure of the organization to external business environment. The basic characteristics of modern environments become: complexity, dynamism, heterogeneity, and hostility (Petkovic, 2011). In such an environment a key competence of the organization becomes the ability to anticipate and implement future changes. Successful companies increasingly develop the ability to create a stable environment for continual changes at any time and as such are called flexible organizations (Overholt, 1997). Following the changes in the environment and on the basis of their needs for adjusting, flexible organization continually develop new strategies and in accordance with that, change their elements of the organization in order to achieve coherence between environment, strategic orientation and organizational design.

In the extremely competitive global economy, inadequate elements of the design of the organization that are chosen by the top management cost very much, and delayed reaction of management can be even more damaging for the company's position on the market, given the pace of implementation and adoption of innovations, as well as complex technological and market knowledge. In these conditions, organizational design becomes a key instrument for anticipating and not only for monitoring and responding to the demands arising from changes in the environment (Miles, Scaringella, 2012:69).

One of the most important factors of a modern environment is globalization, so today we are talking about global companies, global consumer and homogenization of consumer needs around the world, global manager, and global industries as the basic creations of globalization. The global business environment brings greater risks but also greater opportunities for the success of a company. The main challenge that organizations of XXI century are facing is how to avoid threats of the modern environment, and take advantage of the benefits it brings. Keeping in mind the growing importance of the development of information technology and innovations, the key challenge for modern organization is constant acceptance of changes due to technological progress and alignment of strategic orientation and design of organization with updates in the field of information and communication technology.

Information technology requires new infrastructure of organizations, new skills and knowledge while defining new roles and positions in the organization. It increases the flexibility of the organization and facilitates coordination, and also leads to changes in the decision-making process. The information in the Age of Digitalization is available to everyone and is the primary source of competitive advantage for modern companies. Successful management and use of information from different sources become an essential way of creating value. Proceeding from this, Galbraith (2012) predicts adding the new dimension to the structure of organization for the future called "Big Data" which is defined as an independent comprehensive database that includes data of all dimensions of organizational structure (for example, information about customers, regions, business functions and business units). These data are centrally collected and used by corporate leadership in order to take real actions. Also, the strategic importance of the term "Big Data" means adding analytical capabilities to existing organizations.

For many years, organizations have been taking advantage of databases, gathering, and storing, analyzing and using information for making decisions. But what is new about the phenomenon of "Big Data" is a large amount of information, speed and variety (McAfee, Brynjolfsson, 2012:62-63). These innovations affect changes in the organization and analysis of data in two ways (Galbraith, 2014), as follows: 1) more varied data appear in quantitative and qualitative sense, which in the past were clearly structured in rows and columns, and today it is stored unstructured and if necessary, can be digitized, stored and analyzed 2) the new data is available in real time, which basically means that the data that is related to the previous actions is replaced by the information that is connected to the future actions and that may affect the final results.

Possession of the information in real time is one of the basic conditions for achieving positive results of today managers. Also, very important condition involves the creation of organizations whose processes will be designed to support real-time decision-making in order to enable rapid response to changing conditions. Organizations must take into account that the risk of inaccuracy and unreliability of information increases due to the increased availability and visibility of information and data transfer rates (Berner et al., 2014:15).

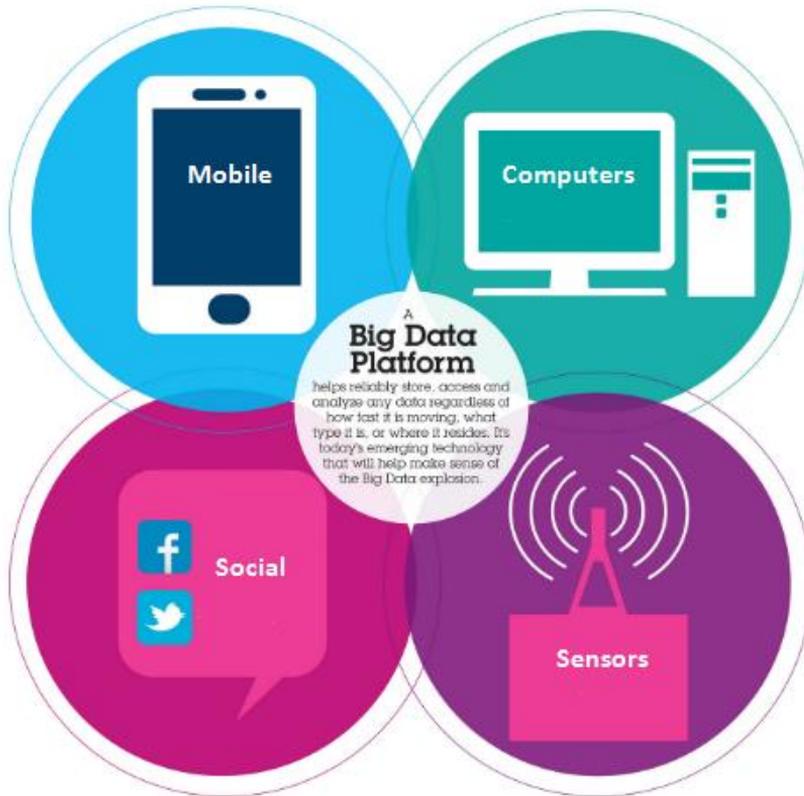
Basic characteristics of the Big Data Era, and comparison of these properties with the Smart Machine Era, that preceded it, were presented in Table 1.

*Table 1: Comparison of information visibility in the past and the future*

Characteristic	Smart Machine Era	Big Data Era
Information Timeliness	Historical data	Real-time data
Information Sources	Self-created, high-quality datasets	Large amount of data including unreliable external datasets
Information Reach	Strategic level	Strategic and operational levels
Information Relevance for Decision Making	Low (experience-driven decision making)	High (data-driven decision making)

*Source: Berner M., Graupner E., Maedche A., (2014), The information Panopticon in The Big Data Era, Journal of Organizational Design, 3(1) pp.15.*

Starting from the need for innovative solutions in the field of data acceleration and in order to speed up process of reporting and analysis, the IBM company uses a special system for data processing that functions on the foundation of open-source software solutions, which are used for analyzing and organizing large amounts of structured and unstructured data. Using the platform, the IBM company receives data from various sources (posts on social networks, digital pictures and videos, online transactions, data obtained using the capabilities of modern mobile phones), and then uses for decision-making and making the necessary analysis (Figure 1).



*Figure 1: Platform of the IBM company*

*Source: <http://turbotodd.wordpress.com/2013/04/03/big-moves-in-big-data-ibm-new-data-acceleration-hadoop-capabilities/>*

Modern global companies are under constant pressure to analyze more data, increase the speed and reduce costs in order to create deeper customer relationships as well as to avoid threats and identify new opportunities for revenue creation. To address these challenges, the IBM company introduced the implementation of “BLU Acceleration” software that combines various techniques to improve analytical performance and simplify administration by: 1. providing the ability for users to have faster access to information and make the right decisions; 2. allowing the use of, so-called, “data skipping” in order to exclude unnecessary and duplicate data from the analysis; 3. providing an analysis of data simultaneously between the two processors and 4. performing data compression which means that data would not have to be decomposed to be analyzed.

In the following text we analyze the influence of "Big Data" on defining the business strategy, the process of organizational design, as well as the role and place of analytic function in the structure of modern organizations.

## ***BIG DATA AND STRATEGY***

Organizations that manage to respond to the challenges of the Digital Era and ensure a successful market position previously have defined strategy that will monitor changes in the modern business environment, and which incorporates phenomena from external sources. Modern authors (Galbraith, 2014; Miller, 2014; Berner et al., 2014; Grossman, Siegel, 2014; Korhonen, 2014; Gabel, Tokarski, 2014) place an emphasis on the concept of the "Big Data" as the most important phenomenon of the environment of the XXI century and its impact on the strategic management of the company by introducing a number of changes in the strategic orientation and defining strategies of modern organizations.

By analyzing the research and opinions of many authors in the field of strategic management and organizational design we can distinguish the following changes:

- the time of the decision making process speeds up
- the consumer needs are put in the foreground as the main condition to create value
- there is a constant need to innovate
- the procreation of a need to create a complex organizational structure
- changing the characteristics of human resources through the emphasis of new skills and knowledge necessary to perform new tasks.

Modern organizations have large databases in order to make adequate decisions and properly react to changes in the environment. Communication channels permeate all the elements of business activity and derive information from them, whether it is about internal channels within the organization or external, related to communication with stakeholders outside the company. Information is becoming easily accessible to everyone, to both, strategic management and operational managers, and this contributes to real-time decisions making which is used as an instrument for facing immediately without delay and responding to the demands that are imposed by the external world (Berner et al., 2014). The Nike Company applies Software Developmental Processes that occur in the continued and iterative cycles. New products is set on the company website with minimal features, and then the visitors learn about the characteristics of the product, present their experiences and propose appropriate adjustments which the development team immediately consider for modification of the product in accordance with the desires of potential customers (Galbraith, 2014:7).

This indicates that the main goal for the organizations of XXI is creating value for their customers in order to sell their outputs in the market successfully, and consequently increase their results and projected values. Constant communication with customers using a variety of tools, especially social networks (Facebook, Twiteer, Instagram, LinkedIn) is becoming increasingly important due to the availability of instantaneous information about modern market trends and the possibility of making optimal decisions in order to meet customer needs.

Therefore, the availability of information provides opportunities for companies to innovate continuously and to improve products and services.

In the current conditions the modern environment has been shifting the locus of innovation outside the boundaries of a firm, considering that entities outside the traditional boundaries of the organization have specific knowledge and solutions that can be used to create value for consumers, and for the organization, which contributes to improvement of market position of the company. These innovations are called open innovation (Gulati et al., 2012). The most important actors with whom organizations share knowledge and skills apart from other organizations (direct or indirect competitors, educational institutions, institutes, etc.) are consumers themselves.

Visibility and accessibility of information to all organizational levels increases the requirements for the creation of new capacity for processing information, and the decentralization through the lateral forms of coordination (Berner et al., 2014). Creating a new form of organization is the result of the needs of a company to align its internal (strategy and structure) with external factors (environment). This creates a multi-dimensional matrix model, an innovative model and horizontal structure. Today only the most advanced and most successful companies (IBM, Procter & Gamble) reached the most complex four-dimensional matrix structure (dimensions: function, business unit, region, customer). Galbraith (2012) goes a step further by envisaging the introduction of the fifth dimension, and thus creating a fifth-dimensional matrix structure. This new dimension is the "Big Data".

In modern environment circumstances data becomes essential strategic assets, the need for specialists in the new fields and new professions are much wider than the needs of people who only know how to manage and use databases. Under the influence of "Big Data" existing jobs are increasingly redefining, and therefore the need for entirely new occupations. Modern operating systems require analytical skills, complex knowledge related to finding software solutions, top professionals in the field of data management and definition of information strategy.

Today, there is a lack of digital experts, experts in finding software solutions, experts in social media, IT strategists, professionals in the field of database management and analysis at the labor market. Therefore, there are more frequent suggestions for coordinated and mutual cooperation of universities and modern organizations from different sectors (for-profit or non-profit) which create conditions for proper respond to requests for needed skills in the Era of "Big Data" (Miller, 2014).

## BIG DATA AND ORGANIZATIONAL DESIGN

When it comes to organization, changes that the phenomenon of "Big Data" causes can be best illustrated by using Galbraith's Star Model shown in Figure 2 (Galbraith, 2014:11-12). In this model, Galbraith (2002) identifies five organizational components to be matched with each other, and they include: 1) Strategy - defining a clear vision, goals, values and sources of competitive advantage; 2) Structure - defining structural elements (training, distribution of authority, departmentalization) and relationship; 3) Processes - refer to the teams, informal networks and integrated roles that are designed to allow the connection of all elements of the organization; 4) Reward system - a special element that has the aim to align individual goals with organizational goals and 5) People - defining strategy in the field of human resources with an emphasis on skills, abilities and competencies required of employees, except that the different strategic orientations of company means adjusted human resources strategy.

Galbraith (2014) predicts that the use of dual strategy will be increasingly important in the Information Era. The first strategy refers to the developing of digital skills in order to make the best possible decisions and reduce the time of their adoption. The second strategy assumes the use of data and analytical skills to create appropriate analysis and preparation of data structured reports for the specific needs of different stakeholders of the organization. In this regard, there is a need to create special digital organizational unit that has the characteristics of a profit center.

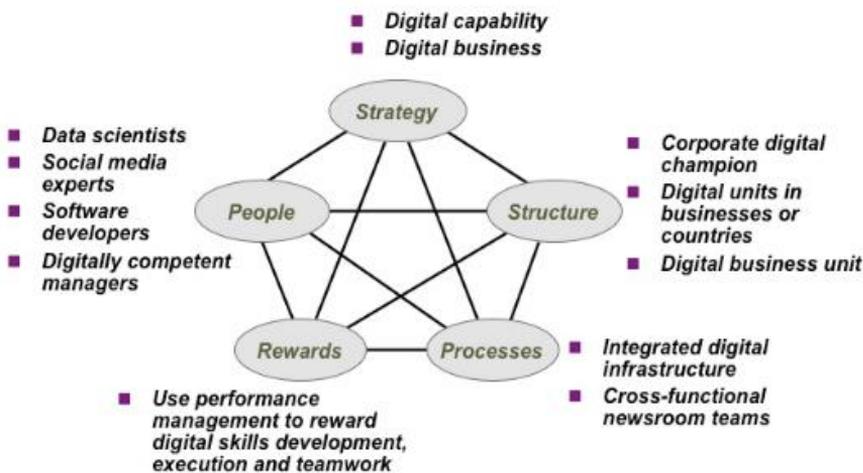


Figure 2: The impact of the Big Data phenomenon to the organization through the prism of the Star Model

Source: Galbraith J. R., (2014), *Organization Design Challenges Resulting from Big Data*, *Journal of Organizational Design*, 3(1) pp.12.

When it comes to organizational structure, the existence of digital corporate officer, whose function is to promote the importance of analytic functions and the digitization of management process can be noticed. In essence, this person has a leading role, with the aim to show the importance of information and databases, as a strategic asset of modern organizations. It is also assumed that the need for the introduction of digital officer will be much wider, and that each dimension of modern organization (regions, functions, business units, consumers) will require digital business unit.

Despite the Galbraith's projections that the Big Data will become the fifth dimension of complex matrix structure, this matrix is still not implemented in practice. However, with the further development of information and communication technology and the increasing computerization and digitization of business processes, it is reasonable to expect its establishment in a relatively short period of time. We could also expect that experts in the field of the most advanced technology (software engineers, database experts, professionals in the field of modern digital systems, etc.) will be implemented in the process teams that will be formed for finding the most effective solutions.

One of the crucial consequences of the increasing importance of information and the use of databases, as well as gaining the new knowledge and skills that are necessary in order to meet up with the changes in the environment in which the company operates is the transfer of power to the digital units (Galbraith, 2014). They have not only the core of digital experts but also a huge number of updated information about the market trends and internal processes, which significantly increases the importance of their role in terms of making the best decisions.

Organization of XXI century must create processes that are consistent with a changed structure and strategy. Digitization process involves the use of analytical models, analytical infrastructure and analytical operations (Grossman, Siegel, 2014:22-23). Analytical models contain large amounts of data that are collected, tested and structured using different methods. Analytical infrastructure includes adequate software solutions, applications and platforms for data management and data processing, as well as the creation of models and their implementation. It also assumes creation of an infrastructure that can support the harmonization of requirements for information processing with the requirements of capacity for information processing. For example, the use of internal social networks as a way of communication in the organization as well as the tools for communicating with stakeholders in the external environment, creates cross-functional digital teams which aim to share data from their domain in order to take joint measures and come up with creative solutions through the exchange of knowledge, experience and ideas. Finally, analytical operations are various processes undertaken to produce the final outcomes of the model, which will be further used in the decision making process and taking further actions in the business.

The last two elements of Galbraith's Star Model are very closely connected. Performance management system must be designed to be compliant with the other elements of the Star Model, but primarily to reward those people in the

organization that have the most advanced skills and knowledge in different areas, then the proper implementation of that knowledge, and teamwork. Due to the frequency and intensity of change that organizations are facing, it can be noticed that the need for new professionals who are specialized in different fields of modern technology is becoming more frequent. Also, if we look at the today's labor market, we can notice the lack of digital experts and specialists for implementation of the most advanced technology. As a main solution for this issue Miller (2014) suggests the cooperation between Universities all over the world and modern companies. In this manner, the educational institution may, depending on the current trends, in collaboration with modern business entities predict new jobs and improve the existing occupations, and in this way make it possible to create an adequate supply of labor, both in qualitative and in quantitative terms.

A major challenge for modern Universities involves the acquisition of the necessary skills through appropriate programs of education and professional development, that can create the "T shaped professionals" (Miller, 2014). Here the vertical line of "T" is considered the foundation and depth of knowledge that should be possessed by a professional, and a horizontal line is its breadth of knowledge, or more precisely, the knowledge that a student gains in collaboration with experts from other parts of the organization, through teamwork, and exchanging creative design solutions. In order to become an outstanding expert, besides the narrow specialization, it is necessary to acquire knowledge from other disciplines such as mathematics, statistics, engineering, analytical discipline, management and decision-making, organizational science, computer science and programming, the ethics of data usage, legal sciences, data security, visualization and communication. According to the author mentioned above a recommendation for closing the gap that exists between the need for certain skills, knowledge and supply in the labor market includes the following: 1) create a formal definition of priority tasks; 2) develop curricula that will produce the required knowledge and skills; 3) set the minimum standards of literacy in the field of database management which must be possessed in digital age; 4) create an open "online community" that will discuss topics of interest, which connects government, academia and the business world; 5) provide the literature that will enable learning from this area; 6) develop a working group to identify key issues in the field of digitization of the organization, such as data security, individual privacy and the ethical use of data.

## ***BIG DATA AS AN INDIVIDUAL ORGANIZATIONAL UNIT***

Considering the growing importance of the impact of modern technology on the organization of the XXI century, certain questions should be asked: 1) Is it necessary to create a digital business function as a separate function in the organization? 2) Where is digital business function located in the company? 3) What is the degree of its independence? 4) What knowledge must digital experts possess? In the following, special attention is given to these questions.

Correlation between digital functions in the organization and other parts of the organization can be viewed through the prism of the theory of information processing introduced by Nedler and Tushman (1978). This theory presupposes linking the requests for information processing, on one hand, and the capacity for information processing, on the other hand. The greater the complexity of tasks and environment, as well as the interdependence of organizational units, the greater the demands for information processing and decentralization. The capacity for the most effective way to respond to requests for information processing could be created through the implementation of digital infrastructure in modern organizations. In this context, it can be assumed that the digital functions are increasingly gaining in importance, and their primary basis represents the core of professionals and experts in the field of software engineering, database management, digital and social media experts. As the need for real-time decision-making is growing, the role of digital decision makers is also growing. These decision makers are seen as digital managers who have a mediating role in the process of implementation of the "Big Data" (Galbraith, 2014).

Modern companies are constantly facing with the challenge of whether to implement different types of digital functions in existing functions or to create a new, separate, digital function. For example, a digital marketing and social media experts can be included in the group for marketing. The Nike company decided to create a separate digital unit, NikePlus.com. This unit is not fully independent, but it is interdependent compared to other and play a mediating role in the organizational structure of the Nike company. Functional digital structure of the Nike company is shown in Figure 3.

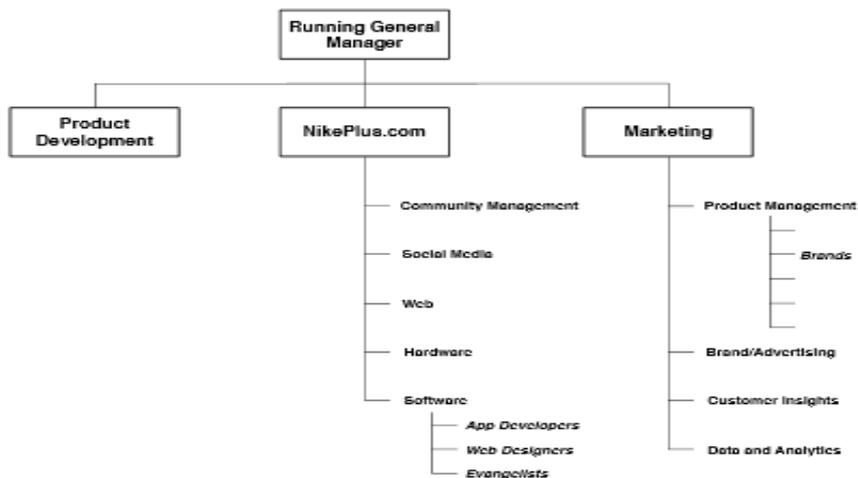


Figure 3: Digital functional structure of Nike company

Source: Galbraith, JR (2014), *Organization Design Challenges Resulting from Big Data*, *Journal of Organizational Design*, 3 (1) pp.8.

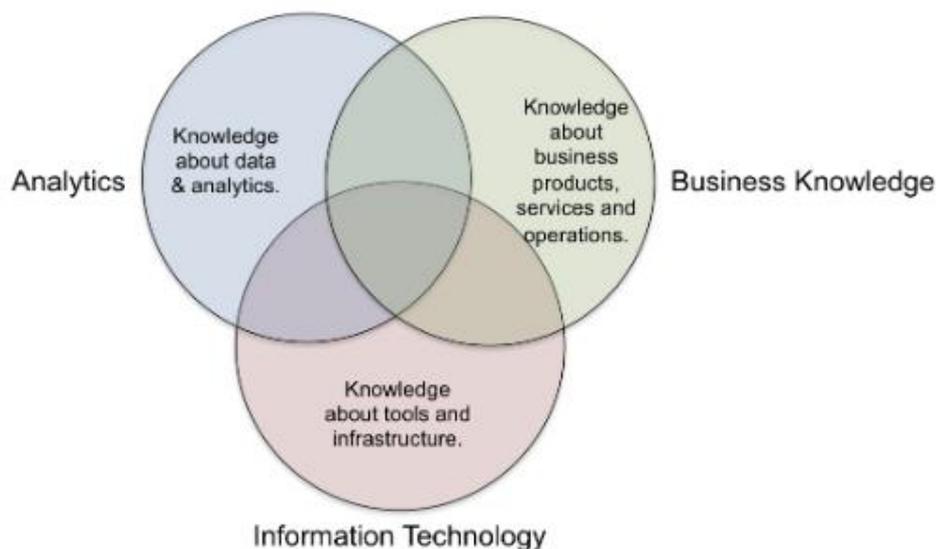
The next question to be answered is where the digital business unit is located in the company. In this sense, there are three models of locating, and each of them represents a settlement between centralization and decentralization (Grossman, Siegel, 2014:22): 1) Model of centralized digital function involves setting up all of digital experts into a single unit. In this way it is easy to achieve a critical mass of experts, to get the necessary data, to lead integrated infrastructure and to provide an adequate expertise for the efficient use of statistical models. On the other hand, this model emphasizes the distance of digital experts from other business units, and therefore the lack of understanding of business units and their needs; 2) Model of decentralized digital function implies the existence of digital experts in each business unit. In that way the understanding of the needs of units is achieved and models are created in accordance with their requirements. A shortcoming that is associated with this model is the lack of a critical mass of professionals who will work for the welfare and improvement of the system as a whole, and not just at the level of business unit; 3) A hybrid model of locating digital function is a combination of the previous two models. The critical mass of experts realizes their concentration in the central unit, except that there are also digital experts who are located in different business units. This model primarily aims to achieve the benefits of both centralization and decentralization.

In general, it can be concluded that the perfect model does not exist. Managers need to identify the most appropriate model to match the requirements of an organization.

Reports, analysis, reviews and other analytical materials which can be used for the purposes of internal organizational units, as well as for external stakeholders could be made by combining and processing of relevant information. Some companies have

recognized this opportunity, so they created the foundation for the creation of profit centers, by assuming that digital organization units can sell their products to external customers, and using that as a basis to generate their own income (Galbraith, 2014). In this way, the level of independence of digital organization units extends, and each unit has the opportunity to create "a small company", which could compete with other companies in the same industry in the market through production of its output. It should be noted that full autonomy of digital unit compared to others in the organization is not a solution that will give the best effect, because of the fact that each organizational unit requires maintenance and support of top management in order to start with its own business. Constant harmonization of the pace of work with other organizational units is also required because the effects of the organization as a whole are greatest when there is the interdependence between organizational units, and their work together is achieved and coordinated.

Finally, we need to answer the question of what knowledge a digital expert should have. Grossman and Siegel (2014) have developed a model that distinguishes: analytical knowledge, knowledge of the business and the use of information technology as the primary knowledge (Figure 4).



*Figure 4: Required knowledge of digital experts*

*Source: Grossman RL, Siegel KP, (2014), Organizational Models for Big Data and Analytics, Journal of Organizational Design, 3 (1) pp.21.*

This model supports the hypothesis that it is necessary for the modern experts to possess much broader knowledge that is not exclusively related to the area of database management and knowledge of analytical models. Digital experts must, above all, know how to implement successfully and be familiar with information infrastructure of organization, and then the company's business, product and service, as well as the characteristics of organizational parts.

## ***CONCLUSION***

The modern business environment is heavily influenced by the increasing interdependence of the global development and information technology. The most important creation of the environment of the XXI century is the "Big Data" phenomenon, which involves the establishment of the comprehensive and independent data base in the organization that is essential for real-time decision making.

Under the influence of the creations of the Digitalization Era, modern companies are changing their strategic orientation, and these changes are reflected in accelerating the timing of the decision making process, the growing importance of consumer needs as one of the condition to create value, then, a constant need to innovate, the creation of complex organizational structures, changing the characteristics of human resources through emphasizing the new skills and knowledge necessary to perform new tasks.

Using contemporary and comprehensive databases by modern organizations is becoming a key challenge for managers. In the future it can be expected that the role of digital business units are increasingly gaining in importance, creating more complex forms of organizational design. This function permeates other organizational units and contributes to more effective job performance and the creation of new values. Therefore, it is more certain that the next step in the process of organizational design and strategic orientation will be inclusion of the "Big Data" phenomenon as the key constructs of the Digital Era in the dimensions of the matrix model and creating a fifth-dimensional matrix structure. Although no company has reached this level of complexity, according to the modern trends in the field of development and use of information-technology, creating the model is realistic in a relatively short period of time.

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# **THE ROLE OF FREE ZONES, TECHNOLOGY PARKS AND BUSINESS INCUBATORS IN THE DEVELOPMENT OF SMALL AND MEDIUM ENTERPRISES**

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## **ABSTRACT**

*Necessities of contemporary business environment in about past ten years have created sudden expansion of free zones, technology parks, business incubators and other modern forms of running business in the world. They could be differentiated by types and structure, but all have common mission – speeding up of the development of small and medium sized enterprises and improvement of the entire business environment of the country where they exist. Experiences of developed economies, as well as countries in transition, justify the fact that the private entrepreneurship is of great importance for the economic development and that it represents an essential part of the process of economic reform. In our country these forms of running business are still at the beginning, however considering the possibilities they offer in the encouragement of local economic development, their progressive increase will be expected in the following years.*

*Subject of this research are: entrepreneurs, entrepreneurship, SMEs, local economic development.*

*The aim of this research is to analyze the relevant data, processes and relations in the theory and practice of entrepreneurship, understand the role and importance of modern instruments of business support to small and medium-sized enterprises - with special emphasis on the role of free zones, technology parks and business incubators in encouraging entrepreneurship and entrepreneurial initiatives, development of small and medium enterprises and local economic development. In the framework of the work will be considered different modalities to help businesses and entrepreneurs in starting and realization of new business, during the initial period of operations that are critical for the survival and further development of the company.*

**Key words:** *Entrepreneurship, Entrepreneurs, Business Operations, SMEs, Local Economic Development.*

**JEL Classification:** *M 21*

**UDK:** *334.713(497.11) 005.5:[004:007 339.543.624  
332.122:338.45 332.146.2:334.012.64*

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## ***INTRODUCTION***

Small and medium-sized businesses and entrepreneurs are the most efficient segment of the economy in almost all countries of the world. Individually, these enterprises make the largest contribution to the increase in employment, gross value added and turnover therefore considered to be the backbone of the growth and development of the national economy. Their role is particularly important in countries in transition that are faced with problems of high unemployment, low level of economic activity, lack of competition and lack of investment, and with still present large and inefficient state-owned enterprises. As a reliable source of job creation, small and medium enterprises make an important social function by absorbing surplus labor incurred in the process of transition and transformation of state and socially-owned enterprises (Group of authors, 2012).

Small and Medium Enterprises (SMEs) are also a key factor in the economic development and innovation. The core of the political and economic transformation of any country is the creation of the private sector, the development of entrepreneurship and creation of SMEs. They are considered to be one of the principal driving forces in economic development. SMEs stimulate private ownership and entrepreneurial skills, they are flexible and can adapt quickly to changing market demand and supply situations, they generate employment, help diversify economic activity and make a significant contribution to exports and trade. SMEs also play an important role in innovation and the high-tech business, due to their flexibility and creativity many of them became large businesses (Stikić, 2008).

These enterprises have a very important role in local and regional development in a country. They are often the main source of new employment. Small businesses can also have a significant role in the foreign trade of a country, as subcontractors of multinational enterprises and companies (Group of authors, 2014).

As companies whose competitive advantage is reflected in the speed, flexibility and sensitivity to the needs of consumers, small businesses can contribute significantly to the development of a market economy. New, small companies are creators of new products and services, which have essentially changed people's lives, significantly contributing to changes in economic structure. Nowadays they represent the most flexible forms of business and they are most sensitive to consumer needs. In this sense, they represent the most sensitive part of any economy. The development of small enterprises is vital to a healthy economy of every country and the development of entrepreneurship, because they provide greater business initiative, employment and income (Bevanda, 2011).

In all sectors where a larger number of participants is involved, their connection, compliance and coordination are essential. Entrepreneurship, as an activity of creative combining of entrepreneurial initiative, risk and available factors in an enterprise, represents the driving force of companies and activities that arise, grow and develop in the market. In the domestic economy, the focus is on development of the private sector and entrepreneurial activities of small and

medium-sized enterprises in order to create a climate and business environment in which it will be possible to transform existing enterprises according to requirements of the market economy.

Free zones, technology parks, business incubators and other modern business and organizational forms, as tools of a local economic development, have expanded in Europe in the 90s of the 20th century, and that is the reason why we know very little about them and why we have made poor use of them. This paper represents additional effort in spreading the information and knowledge about the possibilities of these forms for stimulating entrepreneur's initiative, as well as support to small new businesses in first years of their growth and development. Through the provision of new workspace or the renewal of older industrial premises, they provide a further contribution to the development of the local economy. This basic concept has been adopted and applied in many different countries all over the world.

It has already been recognized that these instruments could make a valuable contribution to the development of the SME sector. All those currently involved in exploring the possibilities for the creation of free zones, technology parks and business incubators, will find the information included in the paper of great help in determining the approach that would be most relevant in the context of the current stage of development of the Serbian economy in general, as well as the needs of different localities.

## ***SME SECTOR IN SERBIA***

The economy of Serbia in 2012. has entered a new phase of the recession that has slowed the reform of the implementation of the new growth model based on export demand, increasing investment and reducing public consumption, strengthening the industrial sector in parallel with the development of the service sector. The consequence of growth based on domestic demand is reported budget deficit (6.4% of GDP in 2012.), deficit in current account balance (10.5% of GDP), and high external debt (85.9% of GDP). The economy is still faced with low level of investment (18.0% share of GDP), inflation risk (inflation of 12.2%) and low employment (unemployment rate of 23.9%) (Report on SMEs, 2013).

In 2012, from total number of 317.668 companies, the entrepreneurial sector accounts for 99.8% (317.162 companies). SMEs generate 65.1% of employees (782.026), 65.4% of turnover (5.690 billion RSD), 55.8% of GDP (977.1 billion RSD) and engages 45.5% of the investment of non-financial sector. SMEs employ 45.3% of total employment, 39.1% of total investments, it has realized 49.8% of exports, 58.2% of imports, generating 70.8% of the trade deficit of the Serbian economy and accounts for about 33% of the GDP of the Republic of Serbia. Regarding the size, the structure of the SME sector consists mostly of micro-enterprises (305.321), while small and medium-sized enterprises (11.841) dominated in all observed indicators (53.8% employment, 60.7% of turnover, 61.6% of GVA, 77.0% of exports, imports 74.5% of SMEs). (Report on SMEs, 2013)

To a weak level of recovery of the SME sector in 2012, decisive influence had a medium-sized companies. Rather than develop into a driving force in the development of the entire sector, recessionary crisis in largely affected this segment of the economy. In comparison to 2011, medium-sized companies have expressed above average reduction in the number of companies (-3.4% to -0.7 in the SME sector), employment (-3.5% to -0.6%), investments (-59.8% vs. -29.4%) and below-average sales growth (0.1% vs. 1.5%). Although medium-sized enterprises are the largest exporters and importers of the SME sector and have an above average coverage imports (67.5% versus 51.3% in the SME sector), in 2012, they formed a ¼ deficit of SME sector (Report on SMEs, 2013).

The main positive business trends in the SME sector compared to 2011 (Report on SMEs, 2013):

- Increase business - turnover in real terms by 1.5%,
- Dynamic growth in exports (15.7%), and take a leading role in the export of non-financial sector of the economy (share of 51.1%), and held sufficient coverage of imports by exports above (the rate of 51.3%),
- Achieved above-average growth rates of GDP (3.2%) and profits (6.5%) compared to the non-financial sector (2.1% and 4.3%, respectively),
- Increased productivity, which in part can be attributed to the decrease in employment. realized the growth rate of GVA per employee of 3.8%, which is higher than in the non-financial sector (2.4%) and large companies (0.4%),
- Above-average earnings growth - 6.5% versus 4.3% in the non-financial sector and 2.1% in large companies, and
- Poor level of reduction of the total number of businesses and shops, the ratio of established and closed companies is much more favorable than in the previous year (1.2:1 versus 0.6:1), although it retained unfavorable net effect of the establishment of new operations (0.9:1).

The most important adverse effects are (Report on SMEs, 2013):

- Reduction of employment in the SME sector by 0.6% (to 4,847 employees),
- Reducing the number of active business entities at the end of 2012, by 1.3% compared to late 2011, year (for 4,287 companies and shops),
- Above average increase in the trade deficit (20.6%) and imports (18.0%), which led to increase of the total deficit of the nonfinancial sector from 66.7% to 74.0%, respectively,
- At the end of 2012, the number of active business entities was 1.3% lower (4.287 for companies and actions),
- Retain the unfavorable trend of sectoral concentration of SMEs with absolute dominance of manufacturing sector and the wholesale and retail,
- Regional imbalances are still exaggerated - the level of development of the SME sector as measured indicator of GVA per employee in the City of Belgrade, in relation to the underdeveloped area Pčinjska is 2.3:1.

## ***DIFFICULTIES IN THE OPERATIONS OF SMES***

The most important difficulty in the operations of small businesses, according to the study of the economic sector and the OECD are: lack of consumer purchasing power, increase input costs, lack of working capital, unfavorable credit, intense competition, high taxes, etc. Entrepreneurs in Serbia and small businesses are faced with many problems in business, both in the start-up, daily operations, and in the case of termination. Among the many obstacles to SMEs, there are:

- Unresolved issues: gray economy, still relatively high tax burden, unreliable and slow legal process of debt collection and bankruptcy,
- Lack of funding - according to the owners of SMEs, it is the main problem in this sector,
- Credit financing is still the only solution for the vast majority of SMEs (in addition to personal savings),
- Banks can not provide sufficient resources, even though interest rates and credit conditions are not favorable for SMEs,
- Other issues: poor functioning of the insurance system and the claims collection, lack of mortgages and the unsettled state of the land registers, which limits the possibility of using a mortgage, and so on.

The business of the SME sector, in the opinion of their respective owners burdens (The working group Small and medium enterprises and entrepreneurship, 2009):

- Advanced payment of taxes, high tax rates, as well as unfavorable costs of electricity, telephone, etc.,
- Pending legal aspects, the slow process of obtaining the necessary permits and long legalization procedures,
- Tariff barriers, etc.

To create a higher level of competition among local entrepreneurs, conditions for the survival of competitive businesses, and to strengthen the entrepreneurial and creative skills of local businesses, it is necessary to develop modern instruments of business support and local economic development. Promotion of SMEs primarily involve creating environments to support SMEs, which includes the provision of services and lobbying for SMEs. This includes promotion of both existing and new businesses, providing advice, support and resources of local government. Legal requirements are often barriers to SMEs, so the activities that a municipality may take are working to improve procedures and processes that companies must go through.

## ***THE ROLE OF FREE ZONES IN THE DEVELOPMENT OF SMES AND LOCAL ECONOMIC DEVELOPMENT***

Free zones are areas or parts of the territory which are especially physically identified and marked, which perform a variety of activities, and where is applied incentive regime of business that is primarily reflected in the preferential tariff treatment, tax exemptions and simplified administrative procedures. In other words, free zones include the specific area with the special conditions, a special regime of economy, significant benefits, allowances and incentives to produce goods, which is primarily intended for export (Law on Free Zones, 2006).

The concept of free zones began to develop in the fifties, as a tool that created the perfect environment for business, especially for companies who seek low-cost export base. Free zones are formed from the free ports and port cities, and their development and the transformation to the legal institute began in the late nineteenth and early twentieth century. In another half of the last century, their number in the world is measured in hundreds, and their share in world trade was around 20% (Serbian Chamber of Commerce, 2012).

*Table 1: Free zones in the world*

<b>REGION</b>	<b>Number of zones</b>
North America + Mexico	320
Central America	41
Caribbean	51
South America	41
Europe	81
Middle East	39
Asia	225
Africa	47
Pacific	2
<b>TOTAL</b>	<b>847</b>

*Source: WEPZA and ILO - World Associations of Free Zones: World Export processings Zones, The National Association of Foreign-Trade Zones, 2012.*

In business practice, free zones have proven as prosperous and profitable institutions with numerous specific businesses. Economic and administrative reasons for the existence of free zones, that allow their profitability, are reflected in the fact that they allow savings in different areas: customs (default or deferred payment), fees, taxes and other measures and decisions of an economic nature. One of the reasons for developing free zone is a concentration of services and needs in one place. They are logistics center for shipping, customs, transportation and storage services, transshipment, treatment etc. Free zones significantly encourage and stimulate investment in the economy of a

country, thus it faster integrates in international division of labor. Also, within the free zones, economic activities are taking place in order to encourage export and thus increase the intensity of foreign exchange of the country, and the realization of positive indirect effects on the domestic economy. In addition, investment motives of foreign partners in the free zone must be supported efficiently by the legal framework that ensures the stability of laws and regulations, and therefore legal security and the role of business (Serbian Chamber of Commerce, 2012).

The Free zone is a comfortable ground for effective ways of business development, ie. economic prosperity. It shows statistics of economically developed countries, due to the fact that the development of business and entrepreneurial infrastructure is grounded way of overcoming underdevelopment and poverty. The free zone is the one that provides a number of benefits for the development of entrepreneurship. On the other hand, entrepreneurship is a fundamental driving force for economic development and at the same time entering into a market economy (Sućeska, 2006).

The fundamental starting point of free zones is to create conditions for development of entrepreneurship, considering free zone as a large and complex company from which economic development of the country will arise. Designing the zone should incorporate economic policy with far-reaching views of the future. This policy allows entrepreneurial infrastructure, proper marketing and financial policy. Zone creation is based on the investment thinking - to gather an attractive profit sector with high employment, low capital investment, short period of activation and return of capital, while preferring manufacturing and service industries. Most often business in the zone is done with less risk in relation to the environment, but in fact there is no ideal concept. Behind every success there are difficulties, requiring perseverance and willingness to take risks. Less risk is certainly implied in fact that there are greater tax, trade, customs and financial benefits, all in favor of reducing costs and increasing competitive advantage.

The Free zone is to be arranged legally and practically to encourage business and controlling action in the direction of developmental effects. Companies that are placed in the zone are available to choose from programs in several fields of manufacturing and service businesses, that can comfortably adjust to the possibilities and the available funds. Doing business in free zones refines entrepreneurial spirit, encourages creative thinking in the direction of continuous improvement of business performance, and that intensifies local economic development.

Free zones are guided by owners of capital that have incentives to develop business, increase profits and property values through reinvestment. Such motivation can become a decisive factor in the development of the economy on the principles of increasing and improving performance. It is the lever of faster and more efficient economic development of the countries flooded with economic and social problems. This means that the free zone introduces new elements to the economic development, enhancing the creative process of creating new economic values, especially in SME sector. This process is driven by invisible force that reduces the risk of failure that follows each company.

The most important reason for establishing a free zone is to increase the employment of the labor force of the host country. It has been shown that free zones model increases the number of workers, if it is properly implemented. A large part of the workforce in such areas are women, that provide better income than, for example, in agriculture or domestic service industries. In some areas female labor force counts 90% of the total number of employees, especially in zones that have implemented production programs of electronic parts and apparel. In any case, the type of business, as well as high-tech in zones develops change of the profile of the workforce. Research shows that one employee in the zone affects/provides employment for up to four workers outside the free zone (Kostić, 2008).

Free zones improve the laws and regulations of the host country, giving contribution to streamlining the process of exchange in the wider context. They also support the development of infrastructure and human resources development. Hereby free zone take on the role of flexible development strategy with positive effects on disturbed economic and social situation in developing countries, and a catalyst in the mobilization of resources, especially manpower. According to many researches, zones successfully help in stopping the downward trend of the development. As a source of growth appears additional energy arising from the restructuring of business entities in the form of the free zone, offering benefits to reduce costs and accelerate the revitalization of the economy and overall life.

Practice in the world shows that the free zone, established in any geographic and economic area, enable fast direct investment and increase the level of employment of labor. Free zones have contributed to a significant increase in employment of low-skilled population, thus solving big problems of unemployment in many developing countries. Statistics show that about 42 million workers are currently directly and indirectly employed in the free trade zones, of which 30 million in China, 2 million in Mexico, 700.000 in the Middle East, 300.000 in America and about 250.000 in countries in transition. In past few years foreign direct investments have recorded a smaller decline in countries with a developed network of free zones.

A comparative study, carried out between countries of different income, support the notion that countries that have established free zones in their territories have achieved a higher growth of exports comparing to the countries of similar rank without free zones. Export in countries that have established a free zone is tens of percent higher.

Within the European Union, 74 Free Zones are defined under the Community Customs Code. Exemptions beyond customs arrangements can include services such as grants offered for research and development and advanced infrastructure. But tax incentives may also be offered and these may, especially on a regional level, distort competition. As such, the tax regime applied needs to be compliant with internal market and State aid rules. As for customs regulation, the Modernised Community Customs Code, that took effect in June 2013, also have an effect on those Free Zones in which there is currently no physical control of goods leaving and entering the zone. A measure mostly meant to streamline customs procedures amongst Member States but also underlining the importance of sufficient regulatory oversight in such zones to avoid institutional problems and organised crime (European Parliamentary Research Service, 2013).

*Table 2: Examples of European Free Zones*

	Shannon Free Zone	Madeira Free Trade Zone	Katowice Special Economic Zone
Country	Ireland	Portugal	Poland
Year of establishment	1959	1980s	1996
Size (km <sup>2</sup> )	2.43	798	20
Number of companies	> 100	≈ 2 900	> 200
Number of employees	≈ 7 200	≈ 1 600	≈ 9 000
Main tax incentives	10% Corporate income tax (applicable until 2005, now Irish 12.5%), VAT exemption	Maximum 5% Corporate income tax, maximum VAT of 22%	Tax relief up to 40% of investment costs and labour costs of first 2 operational years
Type of zone	Type II	Type I	Type I

*Source: Regional development companies sites and tax consultancy research, 2013.*

The recent development of free zones in Serbia was inadequate and did not meet expectations. Free zones in the Republic of Serbia based their business on service warehousing and operated as free trade zones. The exception is a positive example of the economic effects of the use of regime of free zones in Subotica and Pirot. Free Zone "Pirot" currently has eight manufacturing programs, one of which is dominant - section for the production of tires (Michelin), enabling the use of free zones as export production zone (Export processing zone). This enabled testing of operating mode with production activities in free zones in the Republic of Serbia, and thus provide an answer that free zones in function of the production for export gives good results (Development strategy of free zones in the Republic of Serbia for the period from 2011th to 2016th year, RS Official Gazette, no. 22/2011).

### ***TECHNOLOGY PARKS AS A MODEL OF IMPROVING THE EFFICIENCY OF BUSINESS AND ECONOMIC DEVELOPMENT***

Technology park is the term used to describe a variety of efforts to stimulate the development of entrepreneurial, knowledge-based small and medium-sized enterprises (SMEs) within a country. The term has at least 16 synonyms, with the most common being "science park," "research park," and "technopole." As much as there is no consistent definition for technology park, there is also no consistent term for the functions that a technology park provides. While in the United States, "technology park," "research park" or "research and technology park" are frequently used, "science park" is popular in Britain and Europe and "technopole" is widely used in France. New terms are constantly arising as technology parks attempt to distinguish themselves from the considerable competition of at least 295 technology parks worldwide (Briggs, Watt, <http://www.american.edu/>).

Originally, the term technology park had a very limited definition, focusing on the real estate aspect of the park concept, in which universities typically leased real estate, office space or research facilities to businesses. Sometimes these arrangements are referred to as "industrial estates" or "firm hotels." The term, however, has evolved to include a much broader range of functions, including economic development and technology transfer.

The most commonly used definition of a technology park (TP) is: "Technology park is management organization of specialized professionals, whose main task is to increase the well-being of the community by promoting the culture of innovation and competitiveness of associated entrepreneurs and research institutions. To achieve these goals, TP stimulates and manages the flow of knowledge and technology amongst universities, R&D institutions, SMEs and markets; It facilitates the creation and growth of the innovation-based companies through incubation and spin - off processes and provides maintenance services in order to increase the added value together with high-quality environment and equipment in TP." (International Association of Science Parks - IASP).

The most important characteristics of the technology park are (Briggs,Watt, <http://www.american.edu/>):

- It is linked with educational or research institutions,
- It provides infrastructure and support services for businesses, particularly real estate and office space,
- It performs a technology transfer function,
- It performs an economic development function.

However, not all technology parks will meet all of these characteristics and some may contain additional functions.

While each country or municipality may have different reasons for creating technology parks, generally the primary goal of a technology park arrangement is to increase the number of entrepreneurial, knowledge-based small and medium-sized enterprises (SMEs) in an economy. SME's have been recognized as a driving force of the private sector as they help diversify the economy. Developing countries with no local expertise in technology, may use technology parks to attract foreign direct investment to create jobs and increase tax revenues. An important reason, in terms of the Western Balkans, is certainly the retention or return of the best young professionals in the country, providing the ability to obtain attractive jobs in their own country. Another important factor is the establishment and encouragement of so-called transfer of technology from research institutions in the economy, because research and development are key functions of TP.

Based on practical experiences, TP is inevitably associated with higher education and research institutions. Companies are adopting new technologies from its own research and development activities or the work of these educational or research institutions, that facilitate technology transfer through spin-off companies. Spin-off is a new company that was created by people who are former employees of major companies (parent), by transferring the core technology from the parent to

the company. It is usually created to apply and commercialize technology, which was created by state, university or other publicly-funded research. In recent years, many spin-off companies in the European TP have been a result of undergraduate and graduate research of candidates.

Technology parks and incubators vary in the way they are established and managed. They can be founded as independent legal organizations by state and local governments, universities and research institutes, development foundations, private corporations or any combination of those. Depending on the institutional character of their founders, parks and incubators can be public or not-for-profit, private, academic-related, hybrid, and other. This classification is used by the American National Business Incubation Association in Athens, Ohio, in relation to incubation facilities, but can be extended, in principle, to include technology parks. (Petree, Petkov, Spiro)

Establishing the park on the basis of existing facilities is much less costly than building new premises. As in the case of a university-based science park, those university institutes and laboratories that are at an advanced stage of developing commercially suitable products and services can become the first tenants of the park. A young IT-service firm can also serve as a major attraction to software development and information technology-related companies. The research personnel and faculty of the host university (or the Academy of science), as well as its students will be encouraged to participate in the park as consultants and interns. Another major component of the park can be a high-technology incubator that will provide professional and business support to software development and hi-tech R&D projects (Petree, Petkov, Spiro)

The organisational structure of the technology park can vary in complexity depending on the size and concept of the park. With the development of the park its structural parts can be changed, because it is basically a flexible organization.

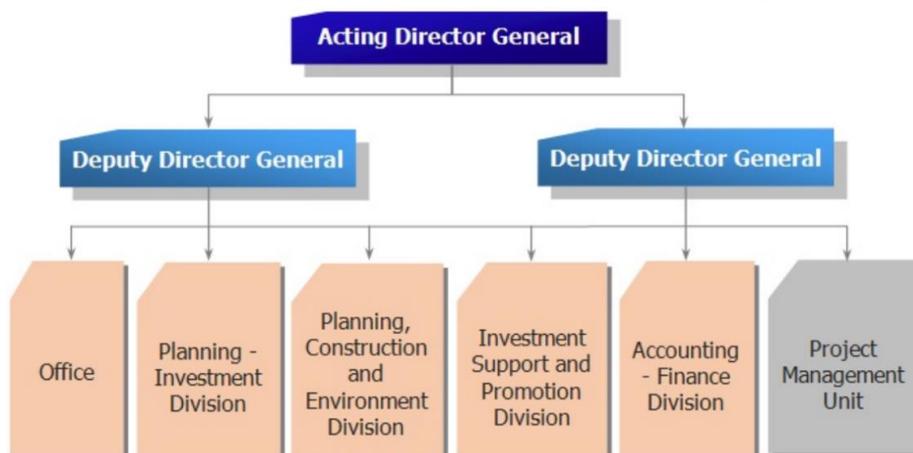


Figure 1: Example: Organisational structure of Danang Hi-Tech Park, Vietnam

Source: Danang Hi-Tech Park, Vietnam, [dhtp.gov.vn](http://dhtp.gov.vn), visited 09.06.2014.

The distribution by sector in technology parks is usually dominated by ICT companies. Industrial technologies, environmental energy, chemical & pharmaceutical, and other different types of services also participate in its sectoral distribution. (Castilla y León, cordis.europa.eu)

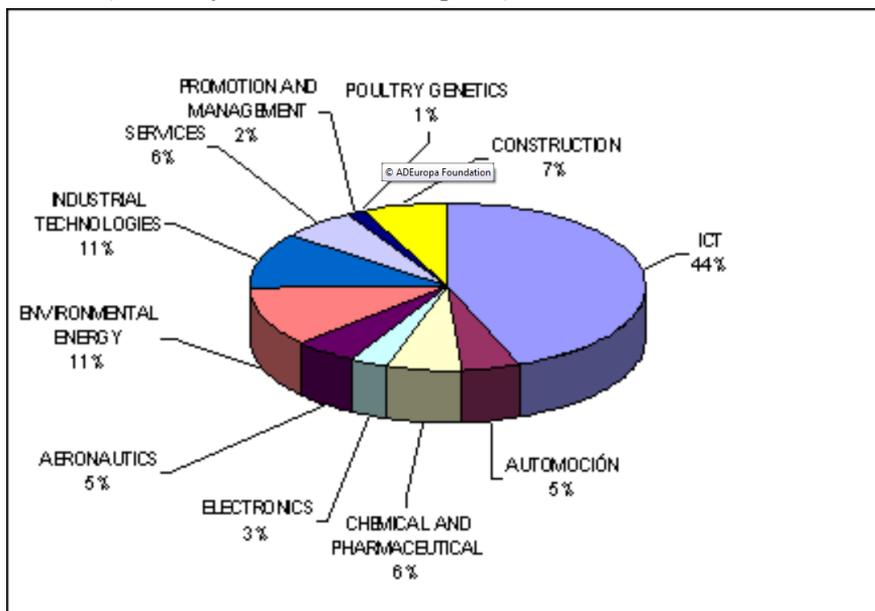


Figure 2: Example: Employment distribution by sectors in the Technology Park of Boecillo, Spain

Source: Technology Parks of Castilla y León, Spain

Numerous studies indicate the fact that technology parks have a number of advantages that are reflected in the following:

- TP is the fastest and best way of restructuring the regional economies and towards a more flexible economic activities,
- TP is the engine of growth of SMEs,
- TP is the best place where private entrepreneurs solve their production, management, design, legal and other problems,
- TP is a place where scientific thought is practically applied and implemented,
- TP attack weaknesses that characterize an area; In the case of the Western Balkans that are insufficiently developed market mechanisms of economic activities and operations, inadequate design and redesign of products, poor development and the implementation of new technology, undefined legislation, lack of managerial and marketing skills, non-existence of defined clusters, undeveloped market, and so on.

Technology park, in the constellation of new organizational forms that encourage entrepreneurship and appearing at the present time, takes one of the strategic places. The field of operation is the same as other forms that support the development of SMEs, but the activities of the TP are much more sophisticated and complex. The TP is intended to be a place in which will be created:

- Motivation and climate for the development of enterprises,
- Promotion of self-employment and the development of their own business as a modern social trend,
- Positive image of entrepreneurs,
- Detailed information and solutions for business people,
- New jobs and businesses in the region,
- Support for the conversion of regional potential in commercial enterprises,
- Profile on the market for technology companies in the region and their clusters by providing foreign partners and international network of contacts.

### ***BUSINESS INCUBATORS AS A MODERN INSTRUMENT OF SUPPORT FOR SMALL AND MEDIUM-SIZED ENTERPRISES***

Business incubation is a business support process that accelerates the successful development of start-up and fledgling companies by providing entrepreneurs with an array of targeted resources and services. These services are usually developed or orchestrated by incubator management and offered both in the business incubator and through its network of contacts. A business incubator's main goal is to produce successful firms that will leave the program financially viable and freestanding. These incubator graduates have the potential to create jobs, revitalize neighborhoods, commercialize new technologies, and strengthen local and national economies ([www.nbia.org](http://www.nbia.org)).

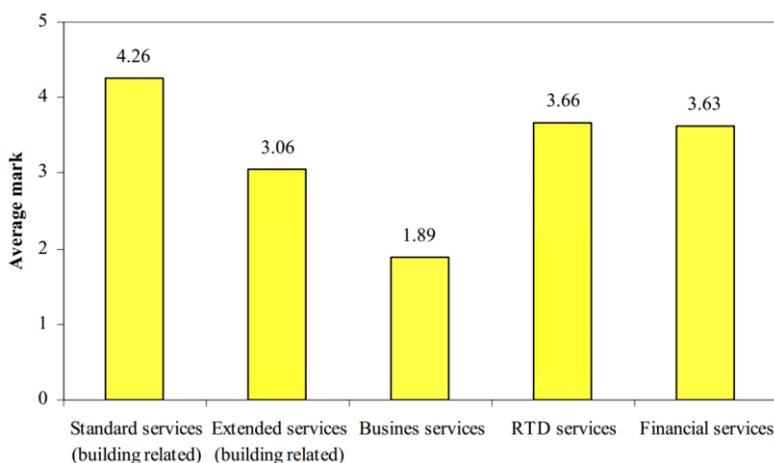
Critical to the definition of an incubator is the provision of management guidance, technical assistance and consulting tailored to young growing companies. Incubators usually also provide clients access to appropriate rental space and flexible leases, shared basic business services and equipment, technology support services and assistance in obtaining the financing necessary for company growth. ([www.nbia.org](http://www.nbia.org))

Term incubation involves ensuring good conditions for starting new businesses and achievement of business ideas, innovation in stimulating the entrepreneurial spirit, as well as taking concrete steps to preserve such conditions and resources required for the survival, growth and development. Business incubators are tending to create favorable conditions to enable interested entrepreneurs starting their own businesses, establishing, maintaining stable performance in several years, and train them to leave the incubator and perform independently on the market after few years (<http://www.mrrls.gov.rs/>).

The first step to establish and develop business incubator is to finance infrastructure by state and local governments, and later continued with entry of private investment (donors, other economic organizations, profit organizations, academic institutions). After the construction is done, there comes the phase of filling incubator with tenants (enterprises) with predefined criteria for their selection, and defined criteria for getting out of incubation.

The goals of creating a business incubator are: creating jobs, reducing the number of failed SMEs, strengthen SMEs in the region (local development), retention of young people in local communities, supporting the process of privatization and restructuring, connecting enterprises in the region and beyond with large enterprises. Business incubators provide opportunities for the development of new services, implement new technologies, and new business, technical, organizational structures and marketing methods.

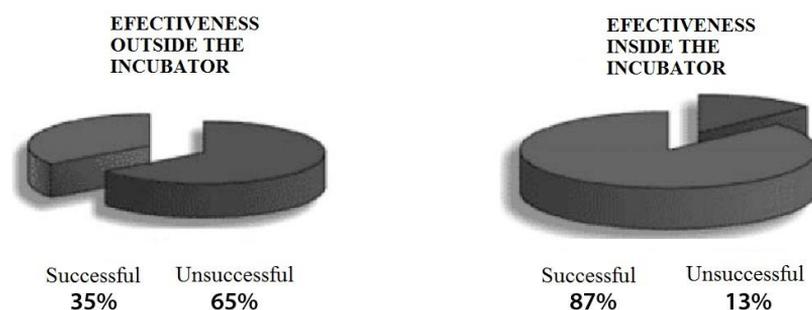
The range of services provided by business incubators varies considerably in different countries depending on the tradition and financing models, as well as the needs and problems faced by local businesses. The key element is to provide an environment in which entrepreneurs and enterprises can quickly begin to work and expand their business. Within the business incubators are usually facilities in which national or local governments, municipalities or groups of large companies provide office and administrative services, as well as assistance in various areas, such as technical support, access to financial resources, advice, marketing services, equipment and assistance in management, in the key (early) stages of business life. Usage of incubator space, shared services such as common secretary, office equipment, networking - commercial space, counseling, mentoring, and so on at subsidized prices, increases the probability of success of the enterprise that operates in the incubator, in relation to a company which operates independently.



*Figure 3: Services provided inside the incubator*

*Source: United Nations Industrial Development Organization, Technology Business Incubators and Technology Parks, [www.unido.org](http://www.unido.org), visited january 2014.*

The most important segment of the support that business incubators provide, is access to start-up capital needed to start and grow new businesses. When a company finds itself in an incubator, the way to potential investors is more accessible and direct, due to a fact that free capital looking for profitable investment opportunity, can recognize new entrepreneurial initiatives more easily. Simply belonging to a business incubator is a favorable sign for potential investors, as they are considered that members of the business incubators already passed the conformance test of business ideas when entering the incubator. With good price lease, joint service service, providing professional business support and training at subsidized prices, investors get a sense of security and a sense of equity significantly less risky than would be the case in a pure market business environment. Statistical reports provide confirmation of this view, by showing that business incubators increase the degree of success of the company from 20% to as much as 87% (Avlijaš, 2010).



*Figure 4: Comparison of effectiveness of the enterprises inside and outside the incubator*

*Source: National Business Incubation Association - NBIA, [www.nbia.org](http://www.nbia.org), visited January 2014.*

Most of the studies dealing with the analysis of the success of business incubators used as an indicator of the success its impact survival rates in the initial stages of development of the company, while it is located in the incubator, and their survival rate after leaving the incubator. Studies show that about 90% of companies that have started operating in the business incubator, do business 3 years after that. Available data confirm validity of the constitution of business incubators as a form of organizing social protection of entrepreneurial ventures.

In evaluating the success of the incubator were used various criteria, among which the following are the most common (Tables 3 and 4) (Stikić, 2008):

- The number of newly established enterprises - who survived the critical period of 3 years,
- The number of newly created permanent jobs - where the indicator of "permanence" take into account the companies that have crossed the limit of 6 years of existence,

- The economic activity of companies - members (evaluated using a variety of indicators, depending on the type of activity - usually a total revenue),
- Number of implemented and market-acclaimed innovation,
- Answers of surveyed companies about the impact of business incubators on their development and competitiveness.

*Tables 3 and 4: Performance indicators of business incubators*

Performance indicator	Total	Average value
Number of start-ups and other entrepreneurial projects during the year	7891	75
Number of business plans implemented during the year	7468	74.68
Number of start-ups created during the year	2678	26
Companies survivability	/	87.55%
Number of companies (tenants) in an incubator	2916	29.76
Number of employees in enterprises tenants	17940	188.84
Number of new jobs	5909	79.85
Number of participants in the various events aimed at encouraging entrepreneurship	69131	652.18
Number of participants in training programs for the improvement of business skills	51930	570.66

Process indicator	Total (Network)	Average value
Number of existing companies	15244	148
Number of projects based on technological innovation expressed as a percentage	54.01%	/
Number of events organized to promote entrepreneurship	1884	17.61
Number of organized business skills training during the year	10567	114
Number of employees in a business incubator	/	7-9

*Source: Stikić, D., Business incubators as a tool to support the development of innovative enterprises, 35th National Conference on Quality, Kragujevac, 2008.*

Business incubators have a direct impact on the local and wider community. It is reflected, above all, in increase of employment, restructuring, growth in production and an increase in GDP. Using the "input-output" method for measuring the total income and the impact on employment, research has shown that business incubators increase employment and income in greater amount than the number of directly employed and paid workforce within the incubator. For example, research conducted in one region showed that employment and income increase, on average,

with a coefficient of 1.35 to 1.43, compared to the direct effects produced by companies within the incubator. This means that in addition to direct effects, indirect employment and income grow at the rate of 35% to 43%. (<http://www.unece.org/indust/sme/incubator>).

Business incubators are associated with the growth of state and local revenues. Taking into account the increased state and local tax revenues at the same rate as personal income, can be accomplished by increasing estimates of tax revenue caused by the existence of a business incubator. There was also evidence that the social costs of job creation, support for start-up businesses through business incubators, are much lower than those needed to implement various other programs to create new jobs. Research, which was conducted within the European Union, showed that 900 existing business incubator helps in opening productive 40,000 new jobs each year in companies that are more stable than those arising out of business incubators.

The main income of the local and social community from the business incubators are healthy companies. The companies that emerge from the business incubators are often on the leading line of the development of new, innovative technologies, which will progressively affect the environment, especially the quality of its products and services. For these reasons, in the last 3-4 years in our country there is a growing awareness that business incubators can make a significant contribution to the development of entrepreneurship of small and medium enterprises. Using already developed models and their adaptation to the existing conditions in the country, provides us the opportunity to catch up with developed countries.

Therefore, business incubators appear as an increasingly popular way of encouraging entrepreneurship and reduce unemployment in Serbia. The purpose of business incubators as a business association in Serbia is to provide good conditions for starting new businesses and translating business ideas into practice, and to prevent the departure of educated young people abroad due to lack of conditions. There is about ten operational business incubators such as incubator of engineering faculties in Belgrade, business incubator Knjaževac, Niš, Kruševac, Užice, Prokuplje, Bor, Senta, Subotica, Zrenjanin, Pančevo, Beočin and Rača.

## ***CONCLUSION***

Many companies and entrepreneurs in the beginning are facing the problem of lack of capital, lack of experience in managing the company, and the lack of the market, both in terms of demand for the products offered, as well as in terms of new, unfamiliar markets. The result is a very small number of newly established companies and, indirectly, fewer new jobs at a local level. Accordingly, the possibilities of development of private sector and small companies in the initial periods of their business, as well as mechanisms to help companies and entrepreneurs in starting new businesses, are not yet sufficiently developed and efficient. In this regard, it is necessary first of all to raise awareness about the need to establish free zones, technology parks, business incubators and other modern instruments of business support to the creation of new businesses and new jobs.

Free zones, technology parks and business incubators are among the most important instruments that can help the development of new, sustainable enterprises at the local level. These instruments are one of the solutions to this problem in the sense of support start-ups in many aspects of their business, thereby encouraging the development of entrepreneurship and local economic development.

Free zone programmes should target a wide assortment of economic sectors, including commercial and manufacturing activities and professional services, such as warehousing and trans-shipment. To reduce the burden placed on public resources and increase the efficiency of zones, the private sector should be encouraged to help develop them and be allowed to operate under market mechanisms. „Free zones have many merits and have boosted investment in many countries. More zones are in the pipeline and still more will emerge in the years ahead. However, bringing in investment is only one, albeit vital, step in a long journey. The ultimate goal must be to make those investments work to the benefit of the wider economy“ (Fodor).

With plenty of business hatchlings growing bigger every year via incubators, it's clear that technology parks are more than just commercial neighbourhoods. They can offer small companies resources beyond their wildest imagining or ability to finance for themselves. Planned settings of development of technology parks in the regions of the Western Balkans are based on the presented premises and determinants of research and development. These parks should be a complement to the planned commercial zones, entrepreneurship centers or business incubators. They should be a joint effort of all to create a business environment where there are early-commercial-industrial zones, institutes, universities, teams for local economic development, regional development agencies, and other governmental and non-governmental organizations with the same goal. TP create an environment with suitable conditions for the establishment and management of companies based on technologies, or products and services that require a little higher knowledge.

Business incubators are effective instruments of helping entrepreneurs and companies in starting new businesses, supporting start-ups and providing a variety of assistance in order to survive during the initial operating period. As a flexible organizational forms, which are able to effectively adapt to the needs and changes in the environment, business incubators are trying to activate all of the company's resources, putting them in the function of the realization of entrepreneur and small business development. Way of doing business in the business incubator represents a reform of private businesses, contributing to the strengthening of small and medium-sized enterprises, but also easier access to modern technology. Technology parks and incubators are the important bridge between taking existing knowledge and markets and expanding them, by supporting new businesses that have the energy and agility to move industries to the next level.

However, one should be kept in mind – these instruments must be viewed in the broader context of economic development, and must be an integral part of the overall strategy for economic development. As such, they can not afford to contribute to local economic development itself, and can only support the development of entrepreneurship and job creation in a particular union, by systematic provision of the stimulating environment that will enable the faster development of the SME sector.

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## ***DOWNSIZING AS A MEASURE FOR THE INCREASE OF EFFICIENCY AND FLEXIBILITY OF AN ENTREPRISE***

*Nenad Ravic, MA<sup>5</sup>*

*Vlado Radic, PhD<sup>6</sup>*

### ***ABSTRACT***

*The growth of an enterprise (size wise) leads to lowering of flexibility, innovations and creativity of an organization because of standardization and introducing the formal organizational structure. The consequences can be seen in the fact that the large enterprises become slow, too large and slowly adjust themselves to changes. One of the possible solutions is downsizing, which represents organizational reconstruction whose result is the decrease of the size of an organization with the purpose of attaining greater flexibility and efficiency. This can be realized through the following methods: narrowing of the management level, programs and output, eliminating specialized functions, decrease in the number of employees etc. In the modern business practice it is often the case that downsizing removes the middle level of management which provides greater flexibility and “flatter“ organizational structure.*

*Hypothesis of this paper is the following: Downsizing represents an effective measure for increase in efficiency and flexibility of an enterprise.*

*This paper applies the method of analysis of contents of documents in printed and electronic form, which deal with this topic. The purpose of the research is to prove or disprove the hypothesis. Based upon the research results, we can conclude that the hypothesis is confirmed, that downsizing does represent an efficient measure for increase in efficiency and flexibility of an enterprise, but only if it is done in a planned and systematic way. The recommendation to the managers is to use this measure very carefully and thoughtfully, because in another case it can cause various counter effects and deepen the crisis in an enterprise.*

***Key words:*** *Organization, Efficiency, Flexibility*

***JEL Classification:*** *M 21*

***UDK:*** *005.591.47 005.336.1*

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## ***INTRODUCTION***

By enlarging the size of an enterprise the advantage is given to the control of the business activities over creativity and new ideas, this decreases the entrepreneurial spirit of an enterprise and flexibility to adapt to the changes. Instead of focusing on the further development of their competencies, large enterprises focus more on the control of their business activities. Formalization of the process limits the creativity and innovations in the organization. This is why large organizations become rigid, slow and slowly adapt to changes. Such organization finds it difficult to answer to the demands and the needs of the consumers. On the other hand, the expenses of doing business grow, because the growth of an enterprise demands greater investments in supply, so management has to find a way to make an enterprise flexible and efficient again. One of the ways is to solve that issue is to change the organizational structure of an enterprise, like for example, switching to division organizational structure. If that measure does not give the adequate results, management of an enterprise can think about conducting downsizing, which represents organized reduction of the size of an enterprise.

The subject of the research is planned and organized reduction of the size of a large enterprise at the level of SME, which is called downsizing in literature.

The goal of this paper is to prove that downsizing can be an effective way to increase flexibility and efficiency of an enterprise, but only if implemented in a planned and systematic way.

Authors have found the motive for writing this paper in the fact that in Serbia downsizing is done in a completely wrong way, unsystematically and without previously done thorough analyses. Employees are let go in a linear way, through the entire organizational structure and there is no care for the ones that are let go, which creates numerous negative consequences for the enterprise. Another motive for writing this paper is the fact that downsizing is not present enough in domestic literature, so the wish of the authors is to contribute to the research of downsizing in domestic framework and to encourage other authors to deal with this sensitive topic.

This paper will use the methods of deduction and content analysis of relevant professional literature in printed and electronic form.

The hypothesis of the research is the following: Downsizing represents an effective measure for increase in efficiency and flexibility of an enterprise.

## ***DOWNSIZING***

In professional literature there are various definitions and interpretations of downsizing. One of the most precise definitions is the following: “organized reduction of the size of an enterprise with the goal of achieving greater level of efficiency” (Milošević, Vujičić, 2013, p. 107). We are talking about the organizational reconstruction which results in reduction of the size of an enterprise with the goal of achieving greater flexibility and efficiency. Through realization of downsizing the reduction of an enterprise to the level of SME is done, which facilitates its functioning. In modern practice, downsizing usually includes eliminating of the middle level of management which leads to “flatter organization”.

Many large organizations in the period of stable growth, when the organizations dominated their environment and changed the bureaucratic organizational structure (Xerox, Exxon, IBM, GM, GE, etc.), have become slow, too large and inefficient, so they had to think about how to once again become efficient and flexible and to react to the changes in the environment at the adequate speed. Downsizing has become the strategy of choice of many large organizations. Almost all organizations from the list of the magazine “Fortune”, in the period of 1985-1990 opted for downsizing, and in those processes thousands of people were left unemployed.

There are numerous reasons for conducting downsizing. The most often are the following (Milošević, Vujičić, 2013, p. 107):

- Inability to use enough the entire number of employees,
- Insufficient competences of employees related to new technologies,
- Purchase of modern technologies that make the existing number of employees obsolete,
- Large expenses of labor force,
- Stagnation of economic branch that organization belongs to,
- Recession of the overall economy.

Inability to use enough the entire number of employees is present when in an enterprise it is not possible to use all employees, so certain employees do not work effectively during the entire working hours. The cause of this can be large number of employees, so one of the possible solutions is letting go certain number of employees.

Insufficient competences of employees related to the new technologies. In the modern age the technologies are developed in high speed, so the employees are forced to follow technological innovations in their professions and to acquire new knowledge. Those employees who do not do this, become useless for the organization in which they work, so this can be the reason why the management has to let them go and to bring new competent employees.

Purchase of modern technologies that make the existing number of employees obsolete. If an enterprise gets the modern technology that can successfully replace a certain number of employees, there will no longer be any need for those employees, so they will be let go. In practice there are a large number of machines in various branches of industry that replace people in their jobs, because they realize much more productive results than humans (e.g. difficult, dangerous or monotonous jobs).

Large expenses of labor force. If the expenses of the labor force burden the budget of an enterprise, management can reach a decision to let go a certain number of employees, save the money and liberate the budget. The alternative is to lower the wages to the employees if they agree. If not, the termination of employment is inevitable.

Stagnation of economic branch that organization belongs to. Stagnation in the branch leads to decrease of demand. In order to attract the consumers, the companies are forced to lower the prices of their products, which leads to the decrease of the sales income. In order for the enterprise to keep the lower prices in the long run, it is necessary for the management to react and find the way to lower the expenses. One of the ways to accomplish that is to let a certain number of employees go.

Recession of the overall economy. If the entire economy of a country is in crisis, the enterprises must try to lower the expenses wherever it is possible to keep the liquidity and to do business profitably. In this sense, one of the most common measures is letting employees go based on the thorough analysis.

## ***KEY CHARACTERISTICS OF DOWNSIZING***

Key characteristics of the concept of downsizing are (Cameron et al.,1995, p.25):

- Downsizing is done intentionally. That is not something that is happening in the organization, but it is planned and organized reduction of the size of an enterprise. That is the difference between downsizing and the loss of market share or unintentional loss of employees because of the poor labor organization or poor results.
- Downsizing is usually realized through reduction of the number of employees, although that is not the only method. The reduction of the number of employees can be realized through allocations, transfers, early retirement etc.
- Downsizing is focused on improvement of the efficiency of an organization. It can arise as reactive (as the consequence of poorer performance of an enterprise) or proactive (wishing to improve the performances of an enterprise, even though there has not been any drop in it).
- Downsizing influences the work relations, consciously and unconsciously. Measures of downsizing result in specific form of redesign.

## ***APPROACHES TO DOWNSIZING***

There are two typical approaches to downsizing: reinforcement and reorientation. These approaches are developed by Freeman (1992) in his doctoral dissertation. These principles represent the reflection of management's relation to changes.

Enhancement comprises the group of activities that manager does and directs towards the proceeding the existing mission, strategy and system. The essential thing is adapting to the existing economic conditions. Changes in business operations are introduced gradually and in the incremental form – little by little.

Reorientation implies the perseverance of the management to bring in the radical changes into the business operations of an enterprise in the form of change of mission, strategy and system. This makes the discontinuity, that is, the termination of current business activities.

In the first case, the management introduces the incremental changes in the business activities. The goal is to make the enterprise continue to do business in the existing way, with gradual improvements.

In the second case, management introduces the radical changes that realize the turning point in business activities. In order for the management to opt for reorientation, the existence of important reasons is essential, as proofs that an enterprise can no longer do business successfully in the existing way and that it needs to introduce the radical changes.

The characteristics of the mentioned approaches to downsizing are shown in the chart 1:

*Table 1: Overview of the characteristics of the approaches of reinforcement and reorientation*

<b>Reinforcement approach</b>	<b>Reorientation approach</b>
Incremental downsizing	Discontinuous downsizing and redesign
Lower level of encouragement (less radical downsizing approach)	Higher level encouragement, more radical downsizing approach
Stability of TOP management, technology and systems.	Changes in TOP management, technology and systems.
Changes in work instead of structure	Changes in structure instead of work
Reinforced mission and strategy	Redefining of mission and strategy
Downsizing comes before redesign	Redesign comes before downsizing
Less extensive communication needed	Demands more extensive communication
Less usage of internal relations of an organization	More usage of internal relations of an organization
Orientation towards internal constituents	Orientation towards external constituents
Emphasizing of efficiency	Emphasizing of effectiveness
Focus on „do things better“	Focus on do various things

*Source: Mašic, 2009*

Some organizations apply downsizing reactively, as a reaction to the decrease of market share and profitability. That is when downsizing represents defense strategy. This approach is known in theory as convergence. Downsizing of labor force is used as lowering of expenses. In this way management is trying to keep profitability as a defense from the share prices' fall and eventual "hostile" acquisition. However the problem with this approach is that it is often the case that management does not count the expenses that follow the downsizing of labor force, which significantly decreases the savings on the account of smaller number of employees (e.g. severance pay or early retirement). Also, the significant problem of this approach is the lack of wider redesign of an enterprise. One should also take into consideration that the crisis can last for a while, especially if it is caused by extreme factors and leads to new cut backs on the number of employees. This is how an organization falls into the "downsizing spiral" that most certainly leads to bankruptcy (Slavković, 2006, p.5).

On the other hand, some organizations consider downsizing to be an opportunity for improvement of performance so they react proactively, they implement downsizing even though there is no crisis. Compared to the previous approach, the downsizing of labor force is a planned activity and an integral part of the general strategy of an organization. Downsizing is in the function of balancing the structure of an organization with the expected changes in the future, with the goal of keeping the existing profitability. Proactive approach offers to the managers much more of the manoeuvre space for realizing their decisions about the reduction of labor force. By doing this, the mistakes are minimized and the pressure of having to reach a decision in the short period of time, removed of the managers.

## ***METHODS OF DOWNSIZING***

There are the following methods of downsizing (Milošević, Vujičić, 2013, p. 108):

- Decrease in management level;
- Decrease of programs and the scope of production;
- Reduction of the number of employees;
- Eliminating the specialized functions;
- Linear letting go of the employees;
- Early retirement and voluntary leavings.

Decrease in management level. By this method the activities, accountability and responsibility of managers of middle level are transferred on other managers. There are two options here:

- activities, accountabilities and responsibilities of the managers of middle level are taken by the higher managers. This decreases the specialization at

higher levels of organization, the centralization and range of control is increased, which can burden the higher managers;

- activities, accountabilities and responsibilities of the managers of middle level are taken by the lower executives, which brings decentralization. Having this goal in mind, managers of the lower level get additional trainings, in order for them to be capable to efficiently do the additional activities.

Decrease of programs and the scope of production. This implies that the enterprise decreases its production capacities and the scope of production. Before that, it is necessary for the management to analyze the production program and to identify which products are profitable enough in order to keep them in the production range, and which should be withdrawn from that range. The result can be the closure or selling certain parts of an enterprise.

Reduction of the number of employees. This is present in the situations when the management decides to leave a certain market, so it lets all employees, whose business activities are connected to that market, go or transfers them to other positions.

Eliminating the specialized functions. This implies that an enterprise will terminate certain number of business functions in order to save money. These can include legal department or accounting department or cleaning etc. For doing these jobs an enterprise can hire special organizations as external associates (outsourcing) like for example the accounting agency which will take over keeping of the books of an enterprise. In this way an enterprise saves means because it is not paying for employees at the positions that are eliminated. Savings is also realized through the economy of scope of special organizations that cooperate with multiple enterprises, so in this way they invest more money in equipment. Management of an enterprise should assess which businesses an enterprise can do on its own efficiently and to keep them. The jobs which cannot be done in an efficient way by an enterprise should be given to special organizations.

Linear letting go of the employees. This is all about the reduction of the number of employees because of the decreased demand at the market or because of high personal income. Letting go is realized through the entire organizational structure of an enterprise and every department lets several people go.

Early retirement and voluntary leavings. This implies the stimulating of employees to go to an early retirement, which is the first phase in letting employees go. Some of employees can be motivated to take this step by stimuli that are not of financial nature, and others can be offered financial means in the form of severance package. The kind of severance package depends upon the years of their service. In any case the employees are not forced to take this step. Those employees that reject the early retirement with the severance package, risk to be let go in the future without any compensation.

According to Cameron, Freeman, Mishra, there are three downsizing strategies:

1. strategy of the reduction of labor force;

2. strategy of organizational redesign;
3. system strategy.

Strategy of the reduction of labor force that the management will offer certain benefits to a certain number of employees in order for them to leave the enterprise. This can be in the form of early retirement, severance packages, transfers, allocations etc. Management has to think very carefully who to let go because of the employees' experience. Because if they do not, the damage could be far greater than the benefit. The main point of this strategy is to "shake" an organization (as a positive shock therapy), for employees to realize in what kind of situation an enterprise is, to motivate them to work more productively and to encourage the measures of saving. This can be seen as a short-term strategy, because it can be realized very quickly and because the effects are visible right after the implementation.

Strategy of organizational redesign implies the tendency of the management to eliminate the work before they let people go. Most often measures of this strategy are: eliminating of positions, decrease in number of hierarchical levels, terminating of certain parts, withdrawal of certain products from the product range etc. Implementation of this strategy demands extensive analysis of an organization with the identification of process or entity that should be eliminated. The benefits of this measure are: simpler organizational structure, higher efficiency, lower expenses, less burdened labor force etc. We can say that this is a middle-term strategy when we think about the time necessary for its implementation and the appearance of first results.

System strategy is fundamentally different from the previous two. It implies the change of organizational culture of an enterprise, the change of core corporate values and attitudes. This is a radical and long-term strategy, so it usually takes a longer period of time for the positive effects to be seen. Implementation of this strategy is very slow, because a lot of time is required to change the core values of the company. Application of system strategy is possible in situations in which, there is no time pressure, when the structure of labor force is dominated by older staff and when decrease in the number of employees is not great. This strategy is consistent with the reorientation approach to downsizing. The tactic of "freezing" the admission of new staff and retiring the existing enables the realization of this strategy. Continuous improvement is the imperative.

From the three mentioned strategies, in Serbia the strategy of the reduction of the labor force is most often used. Managers in the domestic enterprises (organizations) rarely take care of the fact that they should treat the employees, who are let go, in a humane and just way. The letting go is not done systematically and it is done without previous analysis or planning. Such relation is detrimental for the employees and for the companies.

The table 2 gives the overview of the basic characteristics of the three downsizing strategies:

*Table 2: Basic characteristics of the three downsizing strategies*

	<b>Reduction of labor force</b>	<b>Organizational redesign</b>	<b>System strategy</b>
Focus:	employees	jobs and units	organizational culture
Time needed for implementation:	short	medium	long
Disadvantages:	Does not solve the problem in the long run	Lack of short-term result	Lack of short-term reduction of expenses
Measures:	No new employments, early retirements, leaving, letting go.	Decrease of the number of business functions, merging of units' redesign of jobs.	Including all employees in the change of organizational culture and basic values.

*Source: Gandolfi, Neck, 2003.*

## ***EFFECTS OF DOWNSIZING***

Planned and systematically done downsizing realizes numerous positive effects. Benefits of downsizing for the organization are the following (Dulanović, Ondrej, 2005.):

- increase in efficiency and flexibility,
- increase in the ability of an enterprise to respond to the market demands,
- decrease of fixed expenses,
- more efficient usage of the remaining staff,
- simplification of the systems of communication and control.

The researches have shown that the majority of profitable organizations (81%) that realized downsizing in a planned way accentuate the significance of the strategic motive (Dewettinck, Buyens, 2002). The absence of profitability can be explained by the usage of convergent approach or unplanned conducting of the entire process.

Large enterprises, because of their largeness, often have a problem with the lack of flexibility and innovation. The formal procedures and strict rules of behavior are defined and all employees as well as the management have to obey them. Without these procedures, large enterprise would soon turn into a chaotic system. Negative side of the formal procedures is that they decrease entrepreneurial spirit and the flexibility of an organization. Because of these reasons, large systems find it more difficult to adapt to the changes in environment. Internal and external factors usually force an organization to move to other markets, change its structure and the way of doing business in order to

survive and provide to their owners the return of the invested capital. The life of an organization constantly moves and changes. The ability of changing and adapting to changes is the precondition for survival and the success of an organization (Stojanović et al., 2013, p. 71). SMEs and entrepreneurs have a much greater ability to adapt. There are two kinds of entrepreneurs: social and commercial. The difference is seen in the value that they create and whether it is social or commercial, while the entrepreneurial characteristic is common for both categories (Zare, 2013, p. 90).

The ability to adapt to changes influences whether the management of an enterprise defined an adequate organizational structure. Organizational structure is hierarchical organization of the levels of authority, lines of communication and responsibility of an organization. Organizational structure of an enterprise is seen in the way the roles, power and responsibility are allocated, controlled and coordinated, as well as the way an information flows among the levels of management (Milos, 2013, p. 84).

For the increase in flexibility the strategy of organizational redesign is especially useful. It “flattens” the organization by decreasing the number of organizational levels. You get a “shallow” organization in which the information is distributed faster. The connection of the strategic top and the first line of an organization are direct. Lower hierarchical levels get authority to decide, which increases the speed of decision making. For debureaucratization of the structure the best strategy is system strategy. In debureaucratic structures there is a promotion of team work, which increases the productivity and efficiency.

Large number of organizations in the world that did the downsizing leaves to other organizations the possibility of learning at their mistakes. It is real to expect that the organizations have become “more intelligent” in conducting the downsizing and bad practice will repeat rarely.

## ***LIMITATIONS OF DOWNSIZING***

Besides positive, downsizing has negative effects like:

- decrease of the number of employees represents a socially unpopular measure;
- creating the negative atmosphere in the company ( the rest of the employees feel fear and insecurity, which can result in the fall of productivity);
- when because of the crisis the management starts to let go the employees, the most experienced and skilled employees can choose to leave the company, because they do not want to work in an unstable environment;
- possible decrease in developmental potential of an enterprise because of staff leaving;
- besides the savings, downsizing creates certain expenses, like severance packages;

- because of the letting go certain number of employees, there is an increased intensity and the scope of work for the rest of employees, with possible longer work hours, in order to make up for the lower number of employees.

Decrease of the number of employees is opted for with the goal of the decrease of expenses of employees' wages. First step in the decrease of the number of employees is usually the termination of cooperation with the employees employed for a specified period of time by not prolonging their contracts. Then the decision not to hire new staff instead of those who are at sick-leave or are retiring is reached (Jaško, 2001).

From the aspect of system approach, one can say that these beginning steps are correct. However it is usually the case that the decrease in the number of employees is not realized in a systematic way. For example, it is usually the case that the employers terminate the contract on their own, with a certain number of employees and give them a severance package. These actions can result in long-term negative consequences for an enterprise, and is usually in the form of leaving of the most skilled and most hard-working employees. They will find another job more easily than others, so that is why they are prone to leaving an organization that is having problems (Milošević, Vujičić, 2012, p. 110).

With the goal of the decrease of employees the often decision is to enable early retirement for older staff, which leads to not being able to change the employees with the valuable long-term working experience. Another popular measure is the decrease of the number of business functions, which can lead to destabilization of an organization if it is not done in a planned way. Linear letting go, which is an even dismissal of employees in the entire organization, can decrease the developmental potential of an enterprise if this measure is not based upon thorough analysis of staff (Milošević, Vujičić, 2013, p. 107).

In order for the process of decreasing the number of employees to be considered justified, it is necessary to fulfil several terms (Jaško, 2001, pp. 29-34):

- not to be done in a linear way throughout an entire organization;
- not to be done without previous considering of the consequences for the keeping the employees with the key competencies;
- not to make decisions of letting go generally, according to general criteria, but individually;
- for the criteria and the flow (depth and dynamics) of letting go to be public even before the letting go begins;
- that the economic feasibility analysis takes into consideration the cost of letting go and the cost of redistribution of jobs;
- that there is a cooperation of middle and lower management during this process and in the period of adjusting to the lower number of employees;
- that there is cooperation with the trade unions or at least the exchanging of information etc.

Organizational crises during downsizing are underestimated. We should have in mind that downsizing can be the way into a crisis, and not a way out of it.

Direct expenses of letting go are the following <http://proorg.fon.rs/Files/MuksDown.pdf>:

- separate payrolls for the currently let go;
- remaining vacations and sick leaves;
- additional severance payments;
- assistance in finding a new job;
- pension payments and premiums;
- administrative costs of processing;
- the costs of re-employment of laid-off workers.

Indirect expenses of letting go are the following (<http://www.proorg.fon.rs/Files/MuksDown.pdf>):

- the costs of seeking and hiring new people;
- low morale and insecurity among remaining employees;
- lack of staff when the company recovers;
- possible claims of employees;
- reduction in productivity due to fear and uncertainty of the remaining employees;
- loss of organizational knowledge and confidence in management.

Impacts for the organization during downsizing (<http://www.proorg.fon.rs/Files/MuksDown.pdf>):

- over burn of the employees (reduction of the commitment at work, reducing the positive feelings towards the job, fitting the crisis of the individual and his work);
- increase of cases of domestic violence;
- a significant number of companies have shown that after the layoffs they did not increase profit;
- according to one research, employees worried about their family finance spend 13% of working hours telephoning to bank concerning loans or other business.

## ***JOB INSECURITY AS A RESULT OF DOWNSIZING***

Application of downsizing strategies in practice, has led to changes in the field of employment. Model of life employment in one company is outdated. Earlier, in practice it was popular to have the so-called silent agreement of employees and the management, which basically meant that the employees were spending entire careers in one organization (“from the internship to retirement”), but they were obliged to be loyal and dedicated to the company. However wide usage of downsizing strategies changed this practice. Mass letting go have created the climate of general job insecurity.

Old model of employment is substituted by a new model that does not offer to employees “life employment” in one enterprise in exchange for their loyalty and dedication to an enterprise, but they are offered to learn and develop their skills in an enterprise for a while. In return employees are expected to be completely dedicated to their job. It is no longer expected for employees to be dedicated to an enterprise as a whole but only to the job (Stojanić, 2012, p. 39). Employees are interested in being completely dedicated to the job while they have the possibility to learn and develop in that company. As soon as that is no longer an option, they will try to change an employer and to find a job at some other enterprise where they will be able to continue learning and developing professionally. This model of employment is useful to employers and employees. Employers have workers who are productive and devoted, and employees get the opportunity to acquire new knowledge, which increases their chances for future employment. In developed countries this model of employment is so developed that the “situational” employment arose. This implies that employees realize short-term employment in some company, e.g. while a certain project is realized. After that their employment at that company stops and they are looking for another job.

Job insecurity in an enterprise exists only if in the past there have been letting go that had nothing to do with the work performance of employees. In that case, employees have no possibility of controlling their employment in the company. They feel powerless, because it is not up to them whether they will keep their job. If the management decides to proactively realize downsizing with the goal of improving of performances of an organization, some employees can be let go, even though they have realized satisfactory work results and had a good relationship with the colleagues and superiors. Every employee can make his own subjective assessment of job security based on various sources of information.

The most important sources of information about the loss of jobs are (Same, p. 38):

- official notification that employees receive from management;
- Unpublished information that are highly presumed to be true (e.g., assumption on the closure of certain parts of the company);
- rumors that occur when the official notifications are scarce.
- Lack of possibility of control of employment especially increases in the case of (Same, p. 39):
- lack of protection (e.g., in case of contract breach, disobedience of unions’ demands etc.);
- vague expectations (employees do not always know exactly what is expected of them in order to keep their jobs );
- authoritarian organizational culture ( authoritarian cultures increase the awareness of the inability to influence and control the job security);
- lack of objectivity of management while solving the issue of excess employees.
- The researches have shown that the following reactions to job security are the most common:
- tendency to leave the company;

- resistance to change and
- reduced work engagement.

The results of empirical research done by J. Brockner have shown that with the increase of job insecurity to a certain level, work efforts and engagement of employees are increased. After that, further increase in job insecurity, the work efforts and engagement of employees is reduced.

## ***EXAMPLES OF WELL-DONE DOWNSIZING***

Example 1: Consulting company „Charles Schwab&Company“

This company had a crisis in 2001. At the end of the second quarter of 2001 they had the following negative indicators:

- Turnover fell by 57% in relation to the period from 15 months ago;
- Loss was 19 million dollars, and the value of shares fell by 75%

The situation was critical. The company was shaken to the core and was about to go bankrupt. Managers realized that it is necessary to take radical measures in order to save the company, so downsizing was a logical solution. Management of the company had in mind that the measures have to be done in a systematic and planned way, and that this was the only way that this consulting company will survive. Before letting the employees go, management took the following five steps:

1.Frozen projects and drastically reduced costs, such as delivery of lunch for staff, travel and recreation etc.;

2.The wages of senior management were reduced (top managers by 50%, executive vice presidents by 20%, senior vice presidents by 10% and by 5% to vice presidents);

3.Employees were encouraged to use their time off and take unpaid leave for up to 20 days;

4.Management decided that some of the Fridays would count as willingly free days, unpaid, if employees do not have clients;

5.Only after all of this they let go 2,000 employees from 25,000 employed, with the following benefits: from 500 to 1,000 shares to every employee that was let go, payment in cash because of the increased health insurance costs and all services for re-employment and a voucher for a scholarship in the amount of 20,000 dollars.

After these measures, the remaining employees introduced an innovation in doing business: Internet trade system that charges for variable provisions depending on the usage of services. Company changed the name into CEO. The price of shares was increased ten times.

# *charles* SCHWAB

*Figure 1: Logo of the company „CHARLES SCHWAB“*

*Source: Google Images*

## Example 2: company „Compaq computers“

In the beginning of 90s of the last century this company, that produced computers, was faced with fierce competition that produced and sold cheaper products. After conducting thorough analyses, the company's management decided that it should implement downsizing in order for the company to become more competitive. Having that goal in mind, they thought and planned the way to let go 15% of employees. Before letting go of employees they did the following:

- Managers went through training whose goal was to make them capable and prepared to provide support for the let go and help remaining employees;
- The list of possible questions of employees was put together along with the instructions how to answer them;
- The let go were treated with maximum dignity;

After letting go of the employees, sales were tripled in relation to the period before the letting go of employees.



*Figure 2: Logo of the company „COMPAQ“*

*Source: Google Images*

Besides the mentioned, there are also other examples of proper implementation of downsizing, like the example of American company „Cisco“ that deals with the development of Internet technologies. While it was letting go the employees in the process of downsizing, this company paid one third of wages to the employees. Because of the human treatment of the employees „Cisco“, even though it let go 5,500 people, remained at the 15th place on the Fortune magazine list of 100 companies that are best to work for.

Famous multinational company „Procter and Gamble“, which deals with production of cosmetic products, beauty products, detergents etc., had a big crisis in 2001 when they had to close down 5.600 positions in the USA. The company's management took the following steps:

- 20,000 employees got offered a package of measures (severance package, specialization, health care);
- Employees had 20 days to decide and 7 more to eventually change their mind;
- There were meetings held daily with the best employees in order for the manager to convince them that they do have a future in „Procter and Gamble“.

Mutual termination of employment gave to the workers the sense of personal control. Although the direct expenses were higher and the program lasted for several months, organization remained stable, and the productivity did not fall.

Another positive example is a multinational company „Accenture” that deals with consulting, technology and outsourcing. The company was facing high expenses, so through the thorough analysis, management came to a conclusion that the best thing would be to decrease the number of employees. In June 2001 the company let go 600 employees. From that number, 100 highly educated employees got 20% of their wage in the following 6-12 months, they kept their benefits like business number, lap-top and e-mail. In this way they succeeded in reducing the costs and to keep the employees in which they have invested a lot of time, effort and money through various trainings and education.

The famous company „Motorola” was in a crisis in 2001, so it was forced to dismiss 30,000 employees out of 147,000, which it did in January that same year. Every employee that was let go got a minimal wage for eight months. The company actively sponsored the employment fairs. When the company got to its feet again and gained financial stability, it began hiring the same people that it had let go.

The mentioned examples show how a company should behave while realizing downsizing. By a humane relation to the employees that are let go, the company is being socially responsible, it protects its reputation and sends the message to the employees and the public that it is the company that is serious and responsible, despite the crisis. Also it prevents the leaving of the best experts in this way.

## ***CONCLUSION***

Based on the used methods of deduction and research of relevant literature in printed and electronic form, it can be concluded that the hypothesis: Downsizing represents an effective measure for increase in efficiency and flexibility of an enterprise is confirmed.

Managers are advised, in the case that their company gets into crisis, to consider the application of downsizing, but to approach it in a planned and systematic way and to make decisions based on the conducted relevant analyses. Otherwise, they will only deepen the crisis in the company.

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# **MARKET ORIENTATION AND BUSINESS PERFORMANCE**

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## **ABSTRACT**

*The global market environment is growing in complexity. The recent past has been characterised as technologically turbulent. The accelerated rate of technological innovations is affecting all business activities from the development of new product concepts to marketing communication and the rate of new product introductions has increased. The availability of large quantities of data has made it difficult for a business manager to conveniently convert the data into action-oriented information in order to make appropriate key marketing decisions. The level of corporate failures has increased, time for making decisions has become shorter, and the negative results of wrong business decisions have become more severe. The competition in some industries has become more intense and sophisticated.*

*In this market environment, that can be characterised as growing in uncertainty and risk, organizations that are unprepared to change in reaction to market dynamics will have little opportunity to survive.*

*The importance of market orientation is in its potential contribution in influencing the achievement of organizational objectives. The literature on market orientation reflects findings by many researchers that being market orientation, potentially, improves organizational long-term business performance. The market-orientation firms with concentration on the entire customer experience are better positioned to achieve a higher rate of business success.*

**Key words:** *Market Orientation, Business Performance, Competition, Organizational Objectives*

**JEL Classification:** *D24, L11, L25*

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## ***INTRODUCTION***

In a time characterized by increasingly rapid change in consumer preferences, even faster technological progress, and growing competitive rivalry, it becomes essential for companies to develop mechanisms within their organizations to generate market information, analyze it, and respond accordingly. The set of activities developed by companies permanently to monitor, analyze and respond to these market changes is referred to in the marketing literature as "market orientation".

Over the last decade there has been a growing interest in the construct of market orientation and its usefulness in increasing companies' economic performance. However, it is still not well understood why there is such an effect and – particularly – how it operates. More research is clearly needed in this area. Two streams of research have developed aimed at filling this gap. One stream of research has focused on the effects of market orientation on innovation. The other has investigated the links between market orientation and relationship marketing.

Marketing theorists such as Kohli, Jaworski (1990), Narver, Slater (1990), Carr and Lopez (2007) have argued that market orientation traces its origins from the market concept (also labeled marketing concept) and has noteworthy consequences to overall business strategy. The market concept is concerned with customer-orientation, innovation and profit as an inducement for creating satisfied customers (Narver, Slater, 1990, 1994; Kohli, Jaworski, 1990).

Theories on market orientation have been widely accepted by scholars and academics either as the implementation of the market(ing) concept, as an organizational culture, or as a mix of those two (Greenley, 1995). Through the years, numerous scholars have found that market oriented behavior in marketing new products or services leads to better performance, has positive effects on customer satisfaction and loyalty as well as innovation, employee satisfaction and cooperation (Deshpandé et al., 1993; Rapp et al., 2008).

Naturally, the many definitions given to the marketing concept have common trends such as the customer orientation, the implication of all functional areas of a firm, and being a means to achieve long term corporate goals and objectives. On these grounds, we can now deduce that the market orientation is an organizational culture that places the customer in the center of the strategies or even at the top of the company's considerations.

## ***HISTORICAL BACKGROUND AND DEFINITION OF MARKET ORIENTATION***

Market orientation is not a new concept in the marketing and management literature. Scholars argued that the postulation by Drucker (1954) that the customer

must be the focus of organization's operations and the subsequent support given to this idea by Levitt (1960) that the customer is the reason for the organization's existence were all pointing to the fact that market orientation behavior was necessary at that time. This idea was extended to become known as the marketing concept.

Following these developments, the subject market orientation has received a great deal of attention from marketing scholars who have developed, tested and refined market orientation scales for measuring the degree of market orientation that organizations exhibit (Kohli, Jaworski, 1990; Narver, Slater, 1990; Hooley et al., 2005).

Businesses aim to maximize their profit to shareholders by creating a sustainable competitive advantage over rivals on the market. But where competitive advantage was once based on structural characteristics such as market power, economies of scale, or a broad product line, the emphasis today has shifted to capabilities that enable a business to consistently deliver superior value to its customers. After all, this is the meaning of competitive advantage. Research shows that a market-oriented culture provides a solid foundation for these value-creating capabilities.

We can reason that market orientation builds on the same foundations as the market concept, as that concept is believed to have three facets that are customer focus, coordinated marketing focus and profit focus (Kohli, Jaworski, 1990; Wrenn, 1997). Customer focus implies that companies need to have intensive knowledge and understanding of customer needs, demands and expectations. In order to be able to fulfill those demands and expectations with goods and services those must be carefully charted. This is done with marketing planning, surveys, market intelligence dissemination and generation. Focus on integrated marketing means that all marketing efforts of the company are in sync and support each other. Profit focus is an important measurement in all strategy-making and management.

The marketing concept can be classified into two parts, being the "old" marketing concept and the "new" marketing concept. According to Gunay (2002) the "old" marketing concept is concerned with customer-orientation, innovation and profit as an inducement for creating satisfied customers. The "new" marketing concept is more a business culture than a philosophy. Philosophic questions cannot be answered empirically by observation or experiment, while it is possible to measure the level of culture, and then describe its characteristics.

Market orientation can be defined as a form of organizational culture where employees throughout the organization are systematically and entirely committed to the continuous creation of superior customer value (Narver, Slater, 1990; Kohli, Jaworski, 1990; Desphandé et al., 1993; Day, 1994).

Kohli and Jaworski (1990) argued that the market orientation of an organization is one of degree rather than one of presence or absence. Narver and Slater (1990) confirm the view that market orientation cannot be turned on or off. Being marketing orientated is more than just being customer-led. It requires the full support of the organization to be fully implemented in the long term and, in most cases, may need a complete change in an organization's culture.

Narver, Slater and Tietje (1998) state that market orientation is an organizational culture where culture, management and market orientation are

interwoven. For an organization to be market oriented, leaders within that company must have a clear vision that is continuously mediated to employees. Market oriented companies must communicate their mission, vision and values in such a way that every employee knows his/her role. Companies must be able to change and adapt to new market situations such as increased competition, needs and expectations of customers and new technologies.

Bisp (1999) defines market orientation as a series of actions to obtain, analyze and apply information about current and new customers, consumers and competitors. According to Bisp, the form and intensity of market oriented activity is a behavioral manifestation of elements of corporate culture and strategy. He emphasizes the importance of organizational learning and states that the ability to attract and develop staff with the needed knowledge and skills drives market orientation.

Farrell (2000) also emphasizes that organizational learning is of great importance when installing a market orientation. Other scholars prefer to view market orientation as proactive business actions that take place in a certain sequence.

Kotler (2001) points out that market oriented companies must balance between customer orientation and competitor orientation when installing a market oriented culture in the company. Logically, a company that only focuses on either the customer or the competition will end up performing poorly.

The last decade the field of marketing has grown tremendously and many books and articles about the subject have educated business people across the globe. Before market orientation became the general term for this a well-known concept within marketing, many scholars had described the concept in different ways.

Terms such as market-oriented, market-driven and customer-focused have become synonymous with proactive business strategy in organizations all over the world. The notion that the customer needs to be at the origin of business planning processes seems a very contemporary one, as is the idea of organizing the firm's activities around a thorough understanding of customer needs and demands (Desphandé, 1999).

The first books on marketing were printed in the years 1911 to 1915 and they were mainly based on basic economic theory. The first empirical research papers on marketing and connected issues were printed around 1920 (Converse, 1945 and 1951). The first academic journal about marketing was published in 1936 in the USA as "Journal of Marketing". In 1948, The American Marketing Association put forward the following definition of marketing: "The performance of business activities directed toward, and incident to, the flow of goods and services from producer to consumer."

Paul Converse was one of the first academics that created a comprehensive overview of the concepts of marketing in 1945. He made a list of text books and articles about marketing, reviewed the offer of marketing courses taught in American universities and lectures about the subject until the forties.

Many management theorists cite Peter Ducker's statement from 1954 that marketing is not a specialized functional activity but rather "the whole business seen from the point of view of its final result, that is, from the customer's point of view."

The market orientation concept builds on the marketing concept which is a relatively new academic. A definition of the marketing concept from the American Marketing Association website (AMA, 2008) is: "Marketing is the activity, set of institutions, and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large."

According to both the old and the new definition, marketing is considered a specialist function managing certain decision-making areas to create exchanges that satisfy the customers' and the firm's goals alike (Grönroos, 2006).

Several studies have found a consistent positive relationship between businesses' degree of market orientation and their economic performance (Greenley, 1995; Jaworski, Kohli, 1993; Narver, Slater, 1990; Selnes et al., 1996; Slater, Narver, 1994). As stated previously, many studies have been conducted to assess the market orientation and its relation to performance. Gounaris and Avlonitis (1997) compiled a summary of empirical studies done in this field and their relation to performance (Table 1). From this table, we can safely say that market orientation has a positive influence on performance.

*Table 1: Summary of empirical studies*

<b>Empirical study</b>	<b>Marketing orientation/ performance association</b>
Narver and Slater (1990)	Positive
Hooley, Lynch and Shepherd (1990)	Weak positive
Kohli and Jaworski (1990)	Positive
Kohli and Jaworski (1992)	Positive
Slater and Narver (1992)	Positive
Diamantopoulos and Hart (1993)	Weak positive
Wong and Saunders (1993)	Positive
Greenley (1995)	None

*Source: Avlonitis, Gounaris, 1997, p. 388*

In 1987, the Marketing Science Institute (MSI) in the USA organized a conference on the topic "Developing a Market Orientation". According to Desphandé (1999) the main purpose of this forum was both to showcase some early learning from market orientation implementation and, more importantly, to articulate the need for strong, scholarly research to better define, measure, and model the construct. This conference marks a major development in market orientation research. In 1990, a second conference was organized, this time it featured both academic speakers and practitioners that summarized their

companies' experiences with instilling a market orientation. In 1994, market orientation was anointed to be a capital research topic by MSI. After that, market orientation became a very popular area for research.

Two research papers, both published in 1990, have established the concept of market orientation firmly into the academic of business research. The first paper by Kohli and Jaworski (1990) put forward antecedents to and moderator effects of market orientation and the second one that came later in 1990 by Narver and Slater proposed a market orientation framework with three dimensions. Most studies on market orientation revolve around three components that were first defined by Kohli and Jaworski (1990) and later established by Narver and Slater (1990).

### ***KOHLI'S AND JAWORSKI'S VIEW ON MARKET ORIENTATION***

The scholars Ajay K. Kohli and Bernard J. Jaworski published their article "Market orientation: The construct, research propositions and managerial implications" in July 1990. They viewed market orientation as the implementation of the marketing concept. The model they propose emphasizes the collection of marketing data, dissemination of this data across functions within the organization and the action that is taken based on this intelligence. The model is built on the results of interviews with 62 managers in both marketing and nonmarketing positions in US companies. A main finding was that profitability is a consequence of market orientation, and not a component of it. Kohli and Jaworski did not suggest that market orientation is an aspect of organizational culture.

Their definition of market orientation: "Market orientation is the organization-wide generation of market intelligence pertaining to current and future customer needs, dissemination of the intelligence across departments, and organization-wide responsiveness to it."

In other words: Market orientation is the implementation of the market concept and a firm with a high degree of market orientation is one whose actions are consistent with this concept. Market intelligence is said to be the starting point of market orientation, and refers to the collection and assessment of data on customer's current and future needs plus competitor data and government regulations that could influence those needs.

Organizational learning plays a major role in the creation of a market orientation: managers/employees must continually gather, disseminate and communicate information around all departments of the company in both a formal and informal manner. It is important to acknowledge that this vital function is not the exclusive responsibility of the marketing or sales departments.

Kohli and Jaworski propose three sets of antecedents for market orientation and they are senior management factors, interdepartmental dynamics and organizational systems.

Senior management has an important role to foster market orientation. Kohli and Jaworski state explicitly that the commitment of top managers is an essential prerequisite to a market orientation. Their job is to facilitate communication and data flows between organizational levels. Important characteristics that senior managers should have are a positive attitude towards change and organizational learning.

Kohli and Jaworski define interdepartmental dynamics as the formal and informal interactions and relationships among an organization's departments. Their study findings suggested that departments that have conflicts are not likely to be willing to share information and as such endanger a high market orientation. Connected departments on the contrary cooperate and create an atmosphere leading to a higher degree of market orientation. As such, they are an important antecedent to market orientation.

The third set of antecedents to a market orientation relate to organization-wide characteristics. Expectedly, high formality and centralization levels create a barrier for market orientation because it obstructs information dissemination and knowledge sharing. Important customer messages or market knowledge that must travel a long way before they can be acted upon become irrelevant and obstruct market oriented behavior.

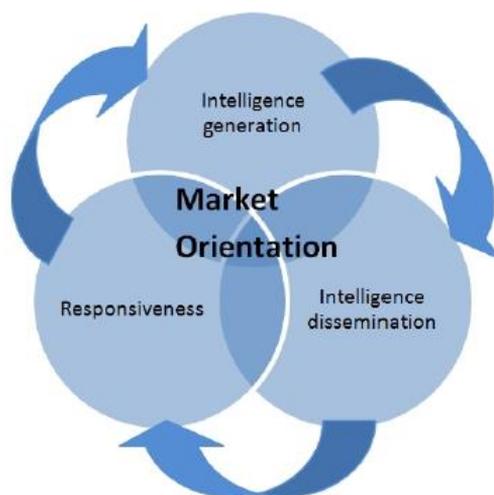
In terms of employee response, Kohli and Jaworski conclude that market orientation leads to a cohesive product focus, clear leadership, better coordination of sales activities, a much better job of reviewing products from a worldwide basis and better differentiation. A market orientation provides psychological and social benefits to employees. The greater the level of market orientation is, the greater the esprit de corps, job satisfaction, and organizational commitment of employees.

In terms of customer response Kohli and Jaworski find that a market orientation leads to more satisfied customers who spread the good word to other potential customers and keep coming back to the organization.

In terms of performance, the study suggests that though a market orientation is likely to be related to business performance in general, it may not be critical under certain conditions. A greater market orientation is likely to lead to increased demand and sales, better margins, more market share and increased profits.

In 1993, Kohli and Jaworski published yet another research paper "Market orientation: Antecedents and Consequences". The goal of this paper was to review and measure the antecedents that lead to market orientation and the consequences of it for the company. The hypotheses proposed in the 1990 construct were tested and results concluded that market orientation builds on three equally important pillars: Customer focus, coordinated marketing and profitability.

Figure 1 shows the interaction between intelligence generation, dissemination and responsiveness. Intelligence gathering is just what the name implies: Gathering intelligence about customers, competitors and the marketplace. Intelligence dissemination, however, is what a department, manager or employee chooses to do with the information after they have it.



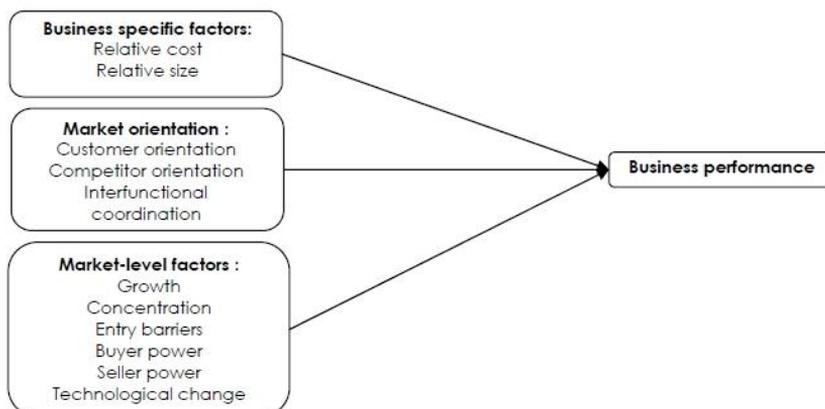
*Figure 1: Kohli and Jaworski's view on market orientation*

*Source: Kohli, Jaworski, 1990*

Responsiveness only happens if the formalized process for sharing business intelligence is not too burdensome. If management emphasized sharing, and if the organizational system's reward system provides an incentive to do so or there is no penalty for doing so. In other words, a department, manager or employee is only willing to share information if it implies no costs.

### ***NARVER'S AND SLATER'S VIEW ON MARKET ORIENTATION***

The renowned scholars John C. Narver and Stanley F. Slater published their now famous article about market orientation in October 1990, several months after their colleagues Kohli and Jaworski. Narver's and Slater's goal was to shed light on the components that build a market orientation and propose a useable definition of the concept. They interviewed managers in 113 strategic business units in one corporation. Narver and Slater (1990) were the first to highlight and prove the relationship between market orientation and performance. For the authors, market orientation is one way to achieve a greater performance. Figure 2 illustrates this relationship.



*Figure 2: Relationship between market orientation, business specific factors, market-level factors and performance*

*Source: Narver, Slater, 1990, p.29*

Narver and Slater viewed market orientation as an organization culture, just like Desphandé and Webster (1987). However, they took the definition further and argued that market-oriented firms focus not only on customers but equally much on competitors. Additionally, they placed emphasis on inter-functional coordination that is meant to create unison between all functions in the organization and become part of the organizational culture. So they developed this definition: "Market orientation consists of three behavioral components – customer orientation, competitor orientation, and inter-functional coordination- and two decision criteria – long-term focus and profitability."

Narver and Slater define three equally important behavioral dimensions of market orientation, them being customer orientation, competitor orientation and inter-functional coordination. They add two decision criteria that are long-term focus and profitability to their model.

Research shows that the consequence of market orientation materializes in all tasks performed by a firm. The degree of market orientation shows through employee- and customer satisfaction, as well as content shareholders. Customers of a company with a high degree of market orientation experience great value for money and excellent service that is gladly delivered by skilled and professional employees of that company.

Competitor orientation is the second component of market orientation and states that organizations should identify, analyze and use the strengths, weaknesses, opportunities and capabilities of both current and future competitors. This is very logical although not entirely new. Levitt (1960) said that parallel to customer

analysis, companies must do competitor analyses and contemplate possible solutions that might fulfill current and future customer needs and expectations.

Inter-functional coordination or integrated marketing means that all departments within the company play a critical role in satisfying customers.

According to Narver and Slater, competitor and customer orientation include all activities that involve generating market intelligence about customers and competitors, analyzing it and distributing that knowledge throughout the organization. This means that the market oriented company must provide adequate business processes and systems for data input and coordinate the communication of disseminated business info in order to create superior value for customers.

Market oriented organizations typically have a long term focus related to profits and to implementing a high degree of market orientation. A short-run focus on profits is not inconsistent with long-run profit performance. According to Levitt (1960), the relationship between them is as follows: At all times a business attempts to create superior value for buyers. As competitors respond and diminish business's buyer-value superiority, the business discovers and implements additional value for its customers (i.e. it augments its product). To grow and survive in a competitive environment they must focus on long term investment strategies that are important for building the market orientation. Market orientation is not a business mode that can be switched on or off, which also implies a long term focus.

As discussed earlier, the first rigorous study of the effect of a market orientation on business performance done by Narver and Slater (1990) found a significant relationship between market orientation and return on investment in a sample of business units belonging to one corporation operating in the forest products industry. However, another study did not show the same results. In two broad samples of businesses, Jaworski and Kohli (1993) found no significant relationship between their measure of market orientation and managers' assessments of either return on equity or market share. These finding of "no results" in a broad sample were found troubling, because it raised concerns about the generalizability of Narver and Slater's (1990) result. It is possible, based on the Narver and Slater study from 1990 that the market orientation – profitability relationship does not apply in all organizations or business sectors.

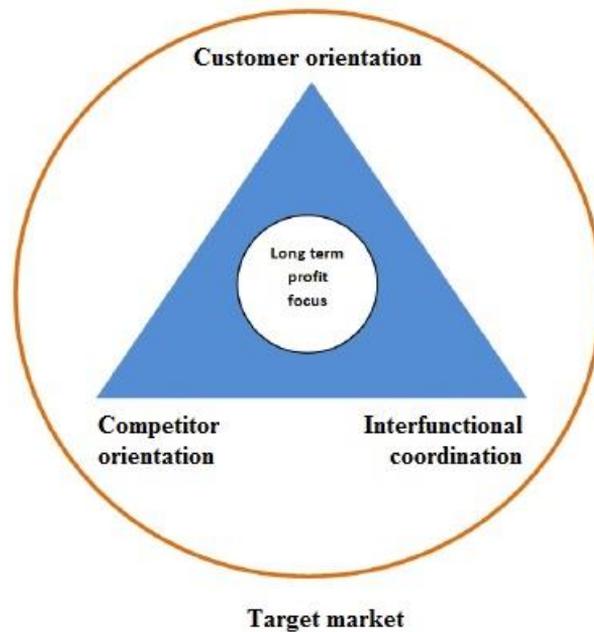
Therefore, in 2000 Narver and Slater decided to repeat their research from 1990 and retested the hypothesis "market orientation and business profitability are positively related". To address the limitations of the original study, this time they used a broad sample of businesses and different respondents' assessment of market orientation and business performance in a business unit. Again, they found a positive relation between market orientation measures and performance. Actually, the positive relationship was even stronger in 2000. However, market orientation is said to be influenced by the business environment and competition levels. Paul D. Ellis (2005) say that the strong relationship between market orientation and performance materializes in strong economies like the United States (Kohli,

Jaworski, 1993; Slater, Narver, 1994) but not at all in weaker economies with less knowledgeable consumers, less competition and less capitalism.

Figure 3 below shows the interaction between the three behavioral components customer orientation, competitor orientation and inter-functional coordination.

According to Narver and Slater, continuous innovation is implicit in each of these components. If there is no innovation and continuous data generation, employees will not have the right prerequisites to offer that extra service to the customer.

The two decision criteria shown in the figure are a long term profit focus and profitability. It is through the continuous creation of superior customer value that a business creates its long-run profit performance. A short period marketing campaign or sales action might boost sales, but the organizational image and generation of repeat-customers only evolves over time along with reputation and "good word of mouth".



*Figure 3: Narver and Slater's view on market orientation*

*Source: Narver, Slater, 1990*

## ***SIMILARITIES AND DIFFERENCES OF VIEWS***

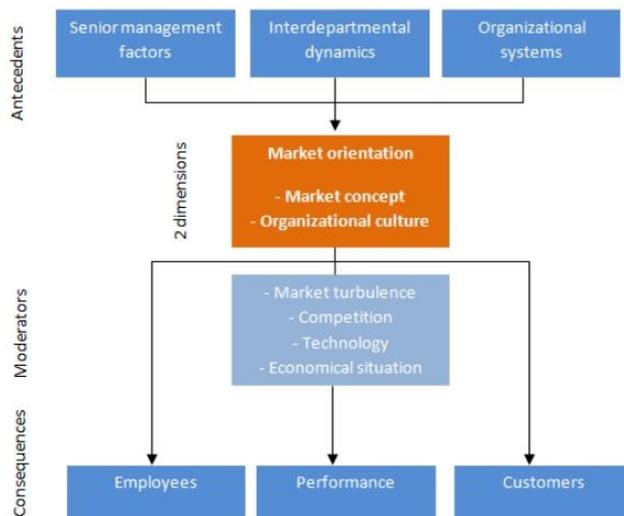
On the whole, the two views on market orientation are quite similar and complementary and very useful to anyone seeking to learn the meaning of the market orientation concept. Both research papers view market orientation as a concept that (if well implemented) leads to a greater competitive advantage for the company. Both duo's agree that business intelligence about customers and competitors is a key prerequisite to build market orientation; that all managers and staff must participate in creating and maintaining the market orientation; that market orientation is a construct with three equally important components.

However, the two views have important differences. Kohli and Jaworski do lay a bit more emphasize on customers than Narver and Slater do. They viewed market orientation more like the implementation of the market concept as discussed earlier. Narver and Slater emphasize the human role and explain market orientation as a corporate culture, which leads to certain custo-mer/competitor oriented behavior throughout the organization creating this specific atmosphere that leads to better performance.

It is not possible to prefer any of these theories above the other, but it is advisable to critically review both of them and use the best from both when building a market orientation. A mix of the theories might lead to the optimal degree of market orientation.

The enhanced model (Figure 4) is divided into four layers: 1) antecedents (as defined by Kohli and Jaworski, 1990), 2) moderators of market orientation (as defined by Narver, Slater, 1990; 3) Kohli, Jaworski, 1990) and 4) consequences (as defined by Narver, Slater, 1990; Kohli, Jaworski, 1990).

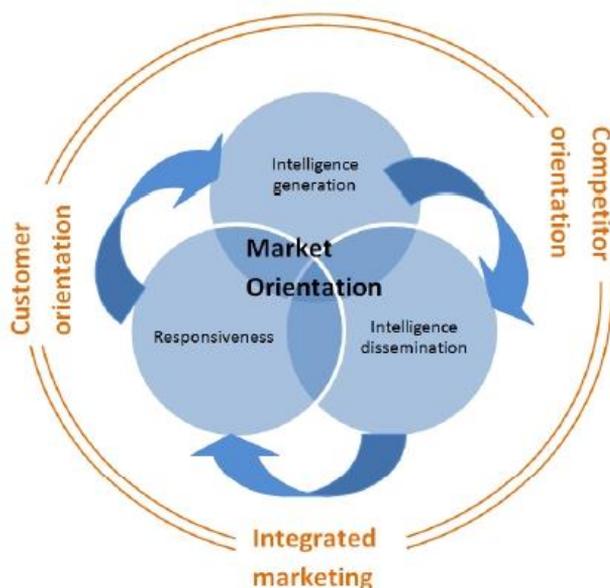
Until recently, scholars either followed Narver and Slater's view, or Kohli and Jaworski's view on market orientation leading to rather imperfect studies.



*Figure 4: The enhanced model of market orientation*

*Source: Kohli, Jaworski, 1990; Narver, Slater, 1990*

With the new millennium came a new awareness that the two concepts are not exclusive but rather complementary. Evidence shows that both the market concept view and culture view are equally important pillars when building a market orientation. Cervera, Molla and Sanchez (2002) agree to this and state that the two views are not mutually exclusive and in fact show different facets of the same concept. When combining the Kohli and Jaworski framework with that proposed by Narver and Slater, a two-dimensional model appears. Figure 5 visualizes this model.



*Figure 5: Two-dimensional approach to market orientation*

*Source: Kohli, Jaworski, 1990; Narver, Slater, 1990*

As shown in the outer circle of figure 5, customer orientation, competitor orientation and integrated marketing must exist in all company operations. To empower management and staff with business intelligence, companies must also have systems in place for intelligence generation, dissemination and distribution of this information. This is shown in the inner circle in figure 5. Obviously, management and staff must act upon the intelligence that they have access to. The task of top management is to install the market oriented culture through strategy making and implementation on all levels (Kohli, Jaworski, 1990; Narver, Slater, 1990). The integrated model showing two views suit the definition that a market orientation is the implementation of the marketing concept; a form of organizational culture.

Cultural differences and opinion forming might have effect on the link between market orientation and performance measures. A relevant question is whether the relationship between the two can be strengthened or weakened by changes in the geographic situation, economic situation and business environment of a firm. Research shows that market orientation is less likely to have impact on performance in some environmental conditions such as a very strong demand (Day, Wensley, 1988; Bisp, 1999). In such an environment, companies can get away with not being market oriented at all. In a market with scarcity where products are rationed to consumers, market orientation also does not matter at all. Kohli and Jaworski (1990) concluded that market turbulence and competition turbulence will

strengthen the relationship between market orientation and performance, while technology turbulence will weaken this relationship.

The effects of market orientation on business performance might be moderated by the turbulence in the environment (Kohli, Jaworski, 1990, Slater, Narver, 1994). In more turbulent environments, a high level of market orientation will be more beneficial as firms can better follow, sense, and use changes in the environment. Kumar, Subramania and Yauger (1998) found that in a high market turbulence companies need a higher level of market orientation in order to perform well. This relationship worked both ways and therefore we could say that in an easy market with little change the level of market orientation is not relevant. Slater and Narver (1994) found limited support that the competitive environment influenced the relationship between market orientation and performance in any way. They found that market turbulence does have impact on the rate of return on assets, whilst technological change has impact on the success of newly marketed products. Hence they conclude that companies should not adjust their level of market orientation to match environmental conditions. Being market oriented is never harmful in their opinion.

## ***CONSEQUENCES OF MARKET ORIENTATION***

Having read different definitions and opinions about the market orientation concept we have a good idea of what it means to be market oriented. We have learned that it is both a business culture and an implementation of the market concept. That being clear, we can now move on and discuss what the consequences of market orientation can be, and how they can be influenced. Main consequences of market orientation derived from literature are great esprit de corps (team spirit), greater organizational commitment, greater competitive advantage and better performance. Other (indirect) consequences include clarity of focus, more innovation and increased organizational learning.

Kohli and Jaworski (1990) discussed the organizational consequences of market orientation. They stated that greater market orientation should lead directly to one consequence in particular, more esprit de corps (later supported by Jaworski, Kohli, 1993; Rose, Shoham, 2005), and to another consequence, greater organizational commitment. They suggested that marketing orientation's positive impact on performance might be greater than previously assumed because of its indirect impact on performance through organizational commitment and esprit de corps. The word "through" suggests that organizational commitment and esprit de corps could both be causal antecedent variables and consequences of a market orientation. The management literature has a rich collection of research suggesting that organizational commitment develops from many other aspects of the firm's environment and culture other than market orientation. Kohli's and Jaworski's (1990) supposition was that marketing orientation fosters company spirit and employee commitment, when, in fact, the exact reverse may be the case.

Many scholars that have researched market orientation and its consequences as well as its effects on performance and have concluded that it leads to a competitive advantage, if well implemented (Narver, Slater, 1990; Slater, Narver, 1993; Kohli, Jaworski, 1990, Martín-Consuegra, Esteban, 2007). Respected economics and business authors also state that market oriented companies perform better and gain competitive advantage that is sustainable (Desphandé, 1999; Webster, 1988). The positive link between the degree of market orientation and organizational performance has been found in many countries and business sectors disregarding company size, culture or product/service (Kohli, Jaworski, 1990; Narver, Slater, 1990; Ruekert, 1992; Jaworski, Kohli, 1993, 2000; Slater, Narver, 1994; Desphandé, Farley, 1999, Slater, Narver, 2000).

Market oriented business culture facilitates clarity of focus. This focus becomes evident through the mission statement, the common vision of management and staff and the overall attitude of the company towards the customer. This creates a high degree of employee satisfaction, better morale, and greater commitment to the job and loyalty to the organization.

The relationship between market orientation and performance is a cornerstone in the market orientation literature. A positive relationship between the level of market orientation and diverse performance measures was found by Narver, Slater (1990), Kohli, Jaworski (1990), Ruekert (1992), Deshpandé, Farley (1999); Rose, Shoham, (2005); Martín-Consuegra, Esteban, 2007; Skerlavaj, et al., (2007). A few empirical studies do not measure this positive relationship, which raises concerns about whether or not the most market-oriented firms are the best performers (Diamantopoulos and Hart (1993), Greenley (1995), Appiah-Adu (1998). Greenley (1995) developed an empirical study of 240 firms in the United Kingdom to test the relationship between level of market orientation and performance. His findings showed no significant effects on return on investment, sales growth or new product success.

Scholars have mixed opinions on the relationship between market orientation and business performance. Is it moderated by other environmental factors such as economic situation, market turbulence, technology and competition, or does geographical situation matter the most?

The consequences of market orientation seem not to be sector specific. A high extend of market orientation not only benefits companies that sell to consumers, but also to service companies that exclusively sell business-to-business and even not for profit organizations and the public sector.

The most common measure for performance is business profitability. Slater and Narver (2000) found that market orientation is indeed positively related to business profitability, measured by return on investment. Other measures include sales growth and new product success and those were used in Narver's and Slater's research of 1994 and also showed a positive relationship. Castro et al., (2005) found that market orientation links with customer- and employee satisfaction.

Market orientation has several indirect effects on performance. Research provides evidence that a high level of market orientation will lead to increased

innovation and organizational learning that in turn lead to better performance, as the company obtains more knowledgeable employees that make better products and provide better service (Rapp et al.,2008; Shepstone, Currie, 2008; Laforet, 2008). Jaworski and Kohli (1993) connected innovation with market orientation because they believed that the concept was driven by creating change and introducing new ways of doing business in order to differentiate and build a competitive advantage. Skerlavaj et al (2007) propose that organizational learning culture might be the missing link between business process change and organizational performance. Results from Laforet (2008) show that medium-sized and small companies are more innovative and market-oriented than larger companies.

The majority of research on market orientation is conducted in the United States of America. In general, American researchers conclude a positive link between market orientation and performance. When the same studies are replicated in non-US countries however, they yield mixed results. Often a weak or non-significant relationship between market orientation and business performance is found (Diamantopoulos and Hart, 1993; Greenley, 1995; Appiah-Adu, 1998). In their study of the effects of market orientation in the United States of America, Denmark, Sweden and Norway, Selnes, Kohli and Jaworski (1996) say that the findings indicate that (1) organizational antecedents are affected by national context; (2) the effects of the antecedents of market orientation are similar in U.S. and Scandinavia; (3) market orientation affects overall performance in both the U.S. and Scandinavia; and (4) strong effects of market orientation on esprit de corps are evident in both cultures.

## ***SCOPE AND STATUS OF MARKET ORIENTATION***

The marketing concept can be classified into an "old" marketing concept and a "new" one (Gunay, 2002). The shift in focus becomes clear with the new millennium. Before 2000, scholars mainly focused on the direct effects of market orientation that were found to be diverse business performance measures, while after 2000, the focus shifted to the numerous indirect effects of it such as the effect on learning, employees satisfaction, and innovation. For example, Farell (2000) was one of the first to come with new evidence that the level of marketing orientation goes hand in hand with organizational learning. The "old" marketing concept emphasized customer-orientation, product innovation and profit as drivers to creating happy customers while the "new" one emphasizes culture, innovation and the importance of organizational learning. Today's marketing concept comprises customer orientation, distinctive advantages, market intelligence, value or quality delivery, continuous improvement in goods and services, customer-oriented business culture, and coordinated and integrated business activities in the whole organization creating a competitive advantage.

In order to get this job done, organizations must gather and analyze market knowledge and empower their people with it. Market orientation involves an outward-

looking perspective from a firm, meaning that it should not only focus on customers but also on competitors, the development of their business sector and the work environment as a whole (Narver, Slater, 1990). As the definitions of market orientation suggests, there is quite a strong market-related information aspect to market orientation. Hence, its fit within an organization is related to the ability of that organization to effectively manage its business information systems and make sure that all data is analyzed and developed into useable knowledge. Desphandé (1990) poses that the fit of market orientation within a firm is threefold: as part the development of strategic competence as a learning organization; as part of a market knowledge management system and as a foundation for corporate strategy.

It has become clear that the traditional perspective of market orientation sees the concept as a business philosophy. However, contemporary approaches to market orientation see it as a dimension of a firm's culture; a guiding representation to a firm's tendencies; a differentiating capability; and an array of business behaviors (Varela, Rio, 2003). Market orientation has, also, been seen as both a behavioral and cultural business philosophy (Gounaris, Avlonitis, 2001). Figure 6 visualizes the nature and scope of the marketing over time.

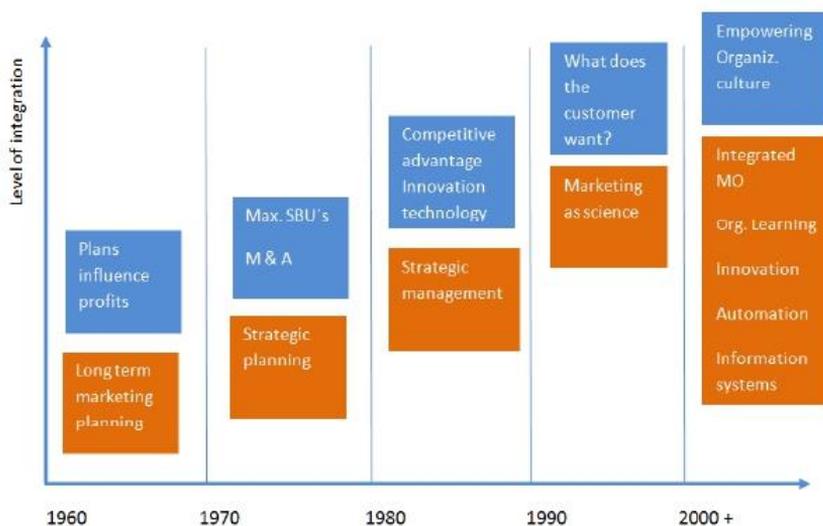


Figure 6: Scope of marketing and its focus over time

Source: Hunt, 1995

From literature we learn that market orientation is not an operating mode that can be turned on or off but rather a state of being that evolves over time (Narver, Slater, 1990). It will manifest itself through the organizational culture where employees strive to continuously provide outstanding service to internal and external customers. The higher the degree of market orientation, the more skilled employees become to integrate all processes in order to maximize performance for the company as a whole (Laforet, 2008).

There are a number of steps that must be taken in order to install a market orientation. What follows is a rough road-map that is grounded in theory. To install the market orientation process, one should start with thorough analysis of the company and its environment, the markets on which it operates, competition, customer demands and expectation and the satisfaction level of customers and employees to name a few. Kohli and Jaworski (1990) write about the antecedents in this context.

Marketing theorist have provided a number of simple tools such as SWOT (analysis of strengths, weaknesses, opportunities and threats), PESTEL (analysis of political, economical, social, technological, environmental, legal issues) to do this analysis. The next step is to systematically and continuously mediate the obtained knowledge and information to all employees (Kotler et al, 2001). This organizational learning process will mix with the corporate culture and as such create market oriented behavior that will have a positive effect on employees and customers and lead to better overall performance. The third step is continuous learning and adapting.

## ***MARKET ORIENTATION AND ORGANIZATIONAL CULTURE***

Having reviewed relevant literature about market orientation, its ins and outs, models and effects, we now discuss how organizational culture and market orientation interact. To begin with, literature concerning organizational culture is reviewed. Next, the cultural model by Denison is explained in more detail and linked to the theories of Narver and Slater and Kohli and Jaworski. Furthermore, this chapter explains why organizational culture can be an effective way to measure market orientation.

Organizational culture is a concept that is hard to describe distinctly. One could say that organizational culture is the personality of the organization (Schein, 2004). In that perspective, culture is viewed as a set of shared beliefs and values that are reflected in habits and traditions as well as in more tangible manifestations-stories, symbols, or even buildings, brands and products. It is an organization's self-identity: What members really think about what the company is and where it is going. Another perspective poses that companies are comparable to ethnical societies with respect to culture, where different people have different opinions of what norms and values are perceived prudent.

Deal and Kennedy (2000) introduced the concept of organizational culture. They say that organizational culture, broadly defined, is a collective understanding, a shared and integrated set of perceptions, memories, values, attitudes and definitions that have been learned over time and that determine expectations (implicit and explicit) of behavior that are taught to new members in their socialization into the organization. Culture is comprised of the assumptions, values, norms and tangible signs or artifacts of organization members and their behaviors (Mobely et al., 2005).

Culture is particularly important when attempting to manage organization-wide change, which is often necessary when implementing a market orientation. Practitioners realize that, despite the best-laid plans, organizational change must include not only changing structures and processes, but changing the corporate culture as well. Desphandé, Farley and Webster (1993) recognized this fact and were the first scholars to connect market orientation with company culture. O' Regan et al. (2006) propose that innovation is driven by a company's culture, leadership and strategic planning. They conclude that high performing firms have stronger and more defined leadership and culture styles compared with low performing firms. This is in line with the findings of Narver and Slater (1990) that suggest a strong relationship between organizational culture and market orientation. So, an empowerment culture where all employees encourage and assist each other associates with successful innovation, leading to a stronger market orientation and better performance.

There has been a great deal of literature generated over the past decade about organizational culture, particularly in regard to learning how to change organizational culture. Organizational change efforts are rumored to fail the vast majority of the time. Usually, this failure is due to lack of understanding about the strong role of culture and the role it plays in organizations (Laforet, 2008). That is one of the reasons that many strategic planners that want to install a market orientation now place as much emphasis on identifying strategic values as they do mission and vision. A market orientation can only build upon a strong organizational culture, and has to become a part of that culture (Desphandé et al,1993).

There is much evidence that links organizational culture with market orientation (Denison, 1990; Denison et al., 2004; Gainer, Pandanyi, 2005; Skerlavaj et al., 2007; Laforet, 2008). The first scholars that connected market orientation with organizational culture were Desphandé, Farley and Webster (1993). Their study found that corporate culture is positively related to business performance through the market culture, which is the organizational culture that includes a high goal achievement orientation stressing competitive advantage. In such a culture, managers and staff are aware of the fact that the company exists to continuously produce great service and therefore they behave in a customer oriented way. A strong organizational culture that empowers employees is one of the most valuable resources to be found within a company (Denison, 1984).

Organizational culture plays a critical role in creating a work environment where employees are committed and contribute to the success of the organization (Shepstone, Currie, 2008). So this is where the implementation of a market orientation should start.

One of the most frequently cited studies of culture and performance is Denison's research (1990). It showed that organizations with a participative culture experience better performance than organizations that have a more formal culture with less room for employee participation in decision- and strategy making. Denison suggests that studying organizational culture provides a way to capture the

impact that culture has on organizational performance. In other words, Denison's study provides hard evidence that the cultural and behavioral aspects of organizations are closely linked to both short-term and long-term survival. In further research, Denison and his colleagues (Denison, 1990; Denison et al., 2004) developed and empirically supported a theory of organizational culture and effectiveness that identifies four cultural traits that are positively related to organizational performance.

Denison (1984) proposed a model to evaluate the shape of organizational culture and an instrument to measure it that he called DOCS (Denison Organizational Culture Survey). The methodology originates from research by Denison (1982, 1984, 1990). Initially, Denison studied 34 companies and found that results were significantly different depending on behavioral issues. Denison and Mishra (1995) expanded the database to 756 companies and now this database includes results of over 1500 companies of different sizes (Mobley, Wang and Fang, 2005). The main focus of this method is to connect several different cultural/behavioral dimensions to company performance. Those dimensions are involvement, consistency, adaptability, mission and cultural traits. Figure 7 shows the Denison model and its dimensions graphically.



Figure 7: The Denison model to measure organizational culture

Source: Denison 1984, 1990

The model scales the four dimensions on a horizontal axis showing internal vs. external focus and a vertical axis that depicts flexible vs. stable focus. The dimensions "adaptability" and "mission" belong to the external environment and "involvement" and "consistency" to the internal environment of the organization. The dimensions "mission" and "consistency" also belong to the stability side of the axis while "adaptability" and "involvement" belong to the flexibility side of the axis.

The Denison culture model is a tool which helps organizations, divisions, and teams, and the individuals within each attain a baseline assessment of current cultural strengths and weaknesses. A high score on any of the 12 dimensions is regarded to be positive, a strength, for the organizational culture, while the opposite is true for a low score. The center of the model (Figure 7) shows the underlying beliefs and assumptions that are the foundation for the human behavior and the actions taken by the organization. A run with the Denison model will provide managers with an understanding of bottom-line related performance such as profitability, sales/revenue growth, market share, quality, innovation, and employee satisfaction, with direct links to cultural elements which may be supporting or hindering these performance areas.

The outcome of a measurement with DOCS defines the shape of the organizational culture. At the same time, the outcome of the adaptability dimension shows the level of market orientation of that organization. Knowing that the right research instrument has been chosen for the purpose of this study, we can now proceed to the research questions connected to the main research question: what are the effects of the bank's level of market orientation on its business performance?

## ***SITUATION IN SERBIAN COMPANIES***

In almost all previous studies in this field, the primary emphasis has focused on the market orientation of manufacturing firms in developed economies. Despite the importance of market orientation in the modern business world, the need for market orientation investigations in the developing countries is still ignored by researchers.

In mature economies characterized by prevalence of buyer's markets, stable growth and intense competition, firms that are more oriented towards customers' needs and competitors action will do better as per the claims of market orientation scholars. In contrast, in developing economies characterized by ill-defined market boundaries and strong or burgeoning demand, firms may be able to "get away with" a minimal amount of market orientation. Until recently; however, there has been relatively little research into the applicability of the market orientation construct in developing economies.

Although various conceptualizations of market orientation appear in literature, researchers in general agree that market orientation encompasses three key dimensions, i.e. customer orientation, competitor orientation and interfunctional

coordination (which means a coordinated utilization of resources for creating superior value for customers). A market oriented firm is supposed to be one which successfully applies the marketing concept. What is not so clear is whether the market orientation concept is appreciated by small firms. According to some authors, small business owners have a problem with marketing and often see it as a peripheral to small firms' requirements.

The reason why market orientation has received a great deal of attention from many researchers is because it is believed that a high level of market orientation can provide a solid basis for a sustainable competitive advantage. In this paper, we hypothesize that market orientation has a positive effect on performance.

Over 95% of companies in Serbia are small and medium-sized companies and represent important part of our society and economy. From the perspective of the researchers small and medium-sized companies are big (and unexplored) field of potential clients – users of researcher's services. Theory, research and everyday experience suggests that small and medium-sized companies have problems with marketing and that they don't consider it particularly useful.

Therefore the objectives of this paper were: a) to examine the degree of market orientation exhibited by small firms, and b) to investigate the impact of market orientation on business performance of small firms.

Market orientation implies usage of marketing concept as a business philosophy. In the center of most definitions is the customer – importance of reacting to customer, but also to the other participants (competition, employees in the company). Behavioral conception (Narver & Slater, 1990) defines market orientation as business culture or behavior that reflects in the activities of the company in three aspects: 1) orientation to customers, 2) orientation to competition, and 3) inter-functional coordination. MKTOR scale is created for measuring market orientation, with claims of situation in company in every of given aspects.

#### Orientation to customers

Orientation to customers reflects orientation of company on satisfying the needs of customers and creating added value. MKTOR scale has *six* claims for measuring this aspect of market orientation.

#### Orientation to competition

Orientation to competition reflects monitoring and understanding short-term strengths and weaknesses as well as long-term abilities and competition strategies. It represents reacting to competition activities and orientation to creating competitive advantage. MKTOR scale contains *four* claims for measuring this aspect of market orientation.

#### Interfunctional coordination

Aspect that reflects the degree of information exchanging and knowledge inside the company, as well as the common action of all departments and employees in achieving companies goals. MKTOR scale has *five* claims for measuring interfunctional coordination.

## ***ANALYSIS OF THE EXAMINATION***

Analyzing the examination of 200 top managers of small and medium-sized companies throughout Serbia (Brakus, Aleksić, 2008), we have tried to check our market orientation assumptions. In examination was using CATI (Computer Aided Telephone Interviewing) method, and sample was random, with quotas for size of the company, sector and region. MKTOR scale is used for measuring market orientation. Claims are presented using the Likert 5 degree scale (1 – strongly disagree, 5 – strongly agree). In table 2 presents the data relating to the size of companies, sectors in which they work, and regional distribution.

*Table 2: Sizes, sectors and regional distribution of companies*

<b>Size</b>	<b>Number</b>	<b>%</b>
1-5 employees	57	28,5
6-15	40	20,0
16-50	41	20,5
51-250	62	31,0
<b>Sector</b>	<b>Number</b>	<b>%</b>
Trade	72	36,0
Services	55	27,5
Production	73	36,5
<b>Region</b>	<b>Number</b>	<b>%</b>
Belgrade	56	28,0
Vojvodina	55	27,5
Central/West Serbia	45	22,5
South/East Serbia	44	22,0
<b>Total</b>	<b>200</b>	<b>100</b>

*Source: Author's view, 2014*

In table 3 presents MKTOR scores according three aspects.

Table 3: MKTOR scores

<b>Orientation to customers</b>	<b>Mean</b>
We are carefully measuring the degree of our employees dedication in satisfying the needs of the customers	4,60
We are very dedicated to our customers	4,75
Satisfaction of our customers is the main goal of our business	4,79
We are regularly monitoring satisfaction of our customers	4,71
We are always trying to find a way to create added value for our customers	4,66
We are dedicating a lot of attention to the services after the sale	4,49
<b>Orientation to competition</b>	
Our dedicated staff regularly monitors and exchanges information about strategy of the competitors	4,22
We are quickly reacting to the competition activities	4,30
Management of our company is regularly considering the strategy, strengths and weaknesses of our competitors	4,18
We are creating our offer so that we can achieve competitive advantage	4,41
<b>Interfunctional coordination</b>	
Top management regularly visits our key customers	4,04
Information about the customers is freely distributed throughout the whole firm	4,40
All of our employees and departments understand the needs of the customers	4,52
All of our departments are taking part in the preparation of business plans and strategies	4,10
Activities of our departments are well integrated	4,36
<b>TOTAL MKTOR SCORE</b>	<b>4,42</b>

*Source: Authors, 2014*

Using the K-Means cluster analysis, SMEs are grouped by the way of evaluation MKTOR claims. Companies differ little in orientation to customers – the biggest differentiation is in claims about competition and coordination. Four different segments have singled themselves out:

Competitive ("ideal") market orientation includes companies that have significantly higher score on claims about competition. And scores for every other aspect are very high. This is the biggest segment, with 54% companies.

Balanced market orientation represents companies that gave relatively high scores for all claims and on less extreme – well-balanced way. This is the second segment in size, with 27% companies.

Non-competitive oriented are companies that have significantly lower score on claims about orientation to competition. They represent 12% of entire sample.

Non-coordinated companies that have scored the lowest in claims about coordination inside of the company. This is the smallest segment, with 8% of the companies.

Figure 8 shows relevant data relating to the first segment.

Orientation to customers and competition is almost ideal in this segment, while the interfunctional coordination is little less. These companies often have more than 50 employees, and work in trading industry. Some departments that they have, or better, do not have, cast doubt on their "ideal" market orientation.

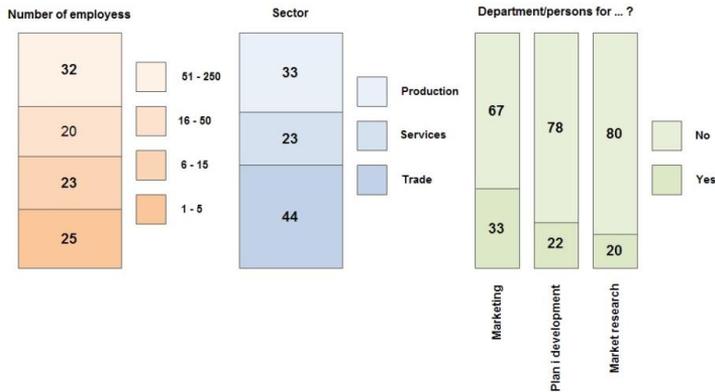


Figure 8: Competitive ("ideal") profile

Source: Author's view, 2014

Figure 9 shows relevant data relating to the second segment.

Companies in this segment dedicate equally a lot of attention to every market orientation segment. They also have bigger number of employees, but mostly in the production sector. In comparison to companies in the previous segment, difference in the structural level is especially significant – it is more probable to have departments for marketing, planning, research and development.

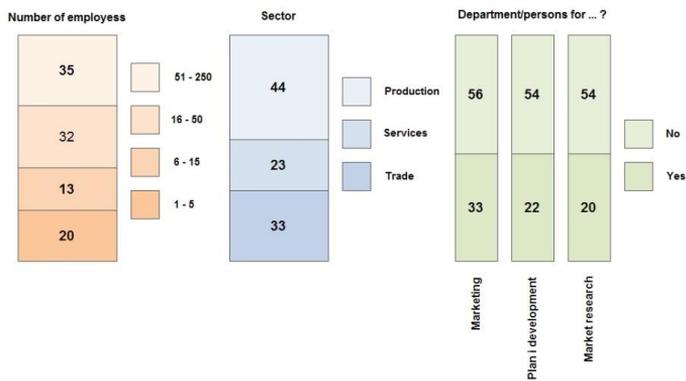


Figure 9: Balanced market orientation

Source: Author's view, 2014

Figure 10 shows relevant data relating to the third segment.

In this segment are mostly micro companies, with up to 5 employees, that work in area of services. Their strongest focus is on customers, while the competition is less important. They rarely have the departments or persons that are in charge for marketing, planning, research and development.

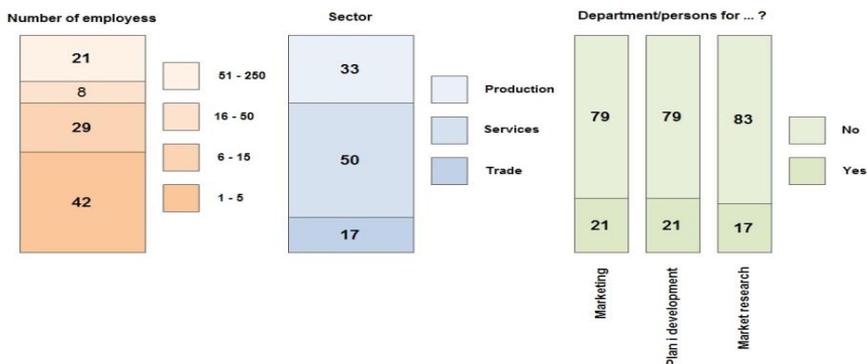


Figure 10: Non-competitive oriented profile

Source: Author's view, 2014

Figure 11 shows relevant data relating to the fourth segment.

These are mostly micro companies, in sector of services and production – rarely in trade. Unlike the previous segment, they dedicate equal attention to competition and customers. Having in mind the number of employees, it's a surprisingly little coordination – so one can assume that "keeping the information" is a reflection of influence of the personal characteristics.

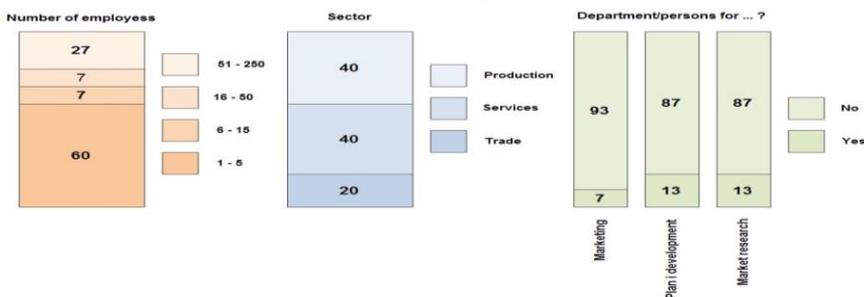


Figure 11: Non-coordinated profile

Source: Author's view, 2014

## ***FINDINGS***

As opposed to expectation, MKTOR score suggests that most of the small and medium-sized companies in Serbia are market orientated. Yet, behind the total score, there are different types of orientation – especially in their relation to competition and coordination inside company. Second segment (Balanced Market Orientation) is theoretically closest to market orientation, while the last two segments represent companies that are the least market orientated.

The biggest part of SMEs has strong focus on competition and customers, and a bit weaker on internal coordination. This kind of external focus could reflect specific organizational culture, and maybe internal problems. Structure of "ideally" oriented companies suggests that there really exists a difference between theory and practice – claims and realization.

Most of the small and medium sized companies in Serbia are strongly orientated to customers and competition. Market orientated companies are more open to research, because of their integration in their business philosophy – they take in consideration both the customers and the competition, and also imply intensive exchange of information.

## ***CONCLUSIONS***

The emerging consensus is the concept of a market orientation constitutes a fundamental strategic approach to understanding markets. This orientation can be described as an organisational culture focused on understanding the market which helps firms to develop customer value strategies that take advantage of opportunities and repel threats. Through the years, numerous scholars have found that market oriented behavior in marketing new products or services leads to better performance, has positive effects on customer satisfaction and loyalty as well as innovation, employee satisfaction and cooperation.

One important fact to consider is that a firm's entrepreneurial orientation is positively related to the firm's performance. This suggests that the firm and its managers may benefit from implementing strategy to encourage and increase the firm's level of entrepreneurial orientation, which has been shown to be the propensity of the firm to be innovative, proactive to marketplace opportunities, and be willing to take risks. Porter (1996) posits that an entrepreneurial orientation may be the mechanism for firm survival and success.

Market orientation which is, broadly speaking, understood as the implementation of the marketing concept as a business philosophy has received a strong attention in the marketing literature. However, there has been little research on market orientation within the small business sector. The same can be stated for

Serbia, despite the fact that Serbian firms are prevailingly considered to be small and medium businesses.

Serbia is, as is well known, a country in transition and based on analyses of situation in SMEs can be concluded that most of SMEs are strongly oriented to customers and competition. Thus, managers should acknowledge that the primary function of market orientation might be to act as an impetus that fuels the development of market-based capabilities.

For better understanding of situation in Serbian small and medium-sized companies it is necessary to conduct more thorough research. As it is already said, this is still unexplored field with great challenges, so it is expected that, use of scientific methods and knowledge, provide a more realistic view of the state. Orientation to market reflects on position, development and growth of these companies, and better performance is expected with changes in organization, orientation to learning, exchange of information and introducing the innovations.

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# ***BUSINESS IMPROVING WITH CLOUD COMPUTING TECHNOLOGY***

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## ***ABSTRACT***

*More and more small and medium business managers are thinking seriously about their data protection and storage strategy. They know their businesses are dependent upon the computers and storage that handle customer orders. Sharing and protecting that information is vital. At the same time, the increasing pace of business and the need to speed operations makes sharing information among teams critical to customer satisfaction and efficiency of business. Cloud Computing offers reliable service to its customers at flexible prices. However, as creative and innovative Cloud Computing may be, it doesn't necessarily mean that Cloud Computing is good for all businesses. In most situations, small businesses reap the most benefits of cloud computing. Finally, looking to the future of cloud computing, we will see how Cloud Computing can be used in business in the future. Analyzed parameters and conclusions in the paper were given and based upon the conducted desk research.*

***Key words:*** *Cloud Computing, Small and Medium Business, Protection, Sharing, Efficiency*

***JEL Classification:*** *M15*

***UDK:*** *005.5:004.72*

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## INTRODUCTION

Whenever we think of clouds, one of the association that comes to mind is that they are a phenomenon that is always present and which always follows. Using this association, software companies recently launched the concept of cloud computing, Figure 1.

In its most simple description, Cloud Computing is taking services ("cloud services") and moving them outside of the organization's firewall on shared systems. Applications and services are accessed via the Web, instead of via the hard drive. In cloud computing, the services are delivered and used over the Internet and are paid for by cloud customer (business) - typical "as-needed, pay-per-use" business model. The cloud infrastructure is maintained by the cloud provider, not the individual cloud customer.

Cloud Computing networks are large groups of servers and cloud service providers that usually take advantage of low-cost computing technology, with specialized connections to spread data-processing chores across them. This shared IT infrastructure contains large pools of systems that are linked together. Virtualization techniques are often used to maximize the power of cloud computing.

Currently, the standards for connecting the computer systems and the software needed to make Cloud Computing work are not fully defined at present time, leaving many companies to define their own Cloud Computing technologies.

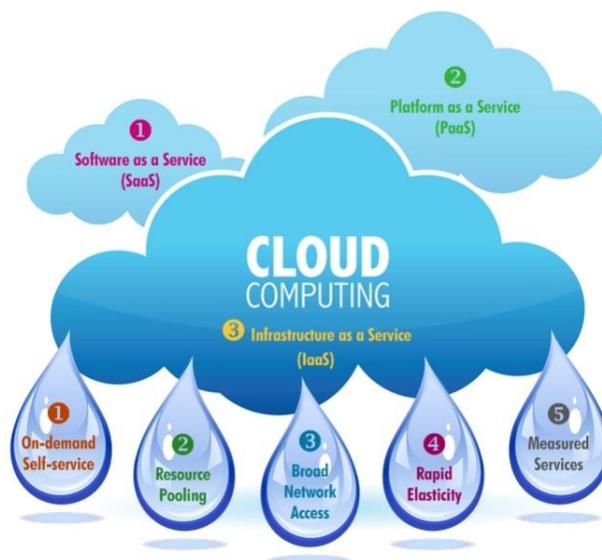


Figure 1: Illustration of Cloud Computing

Source: <http://bodhost.com/blog/cloud-computing-principles-and-paradigms/>  
(11.4.2014)

They connect users in a virtual world, enabling access to email, creating profiles on social networking sites, uploading photos or performing everyday tasks in banking, electronic commerce, shopping or reading a newspaper.

## WHAT IS CLOUD COMPUTING

Cloud Computing is a Web-based computing. Computer has been simply defined as any electronic gadget that enables the input of data for processing into a predetermined format that can be dispensed through an output media.

Cloud Computing is a term that describes the use of the internet to perform functions that could have been done in the past by a PC. Information, data, files, videos, photographs etc. can be stored in the cloud for processing instead of the regular movement of a computer system before gaining access to such information. The main requirement is access to the internet and understanding how it works.

Many people have heard about the advantages of doing business in the cloud, but they are not sufficiently informed about the system usage. It is true that business in the cloud has the potential for development of small and medium-sized enterprises. The advantages are: *low cost, savings, increased productivity and efficiency.*

Simply put, clouds allow business to rent IT and hosting services instead of investing in new infrastructure, training new personnel or licensing new software. It differs from traditional hosting in three key things: the cloud service is rented on request, allows the user to take as much space of a service as they want at any time and provides full service provider. Business in the cloud offers easy operating cost that doesn't burden the budget so much. Companies using this service, pay monthly rent, so there is no longer need for current and large capital investment in own hardware and software that will be amortized in the future. Because of this, more companies from the world are deciding (instead of the traditional IT) using cloud computing, Figure 2.

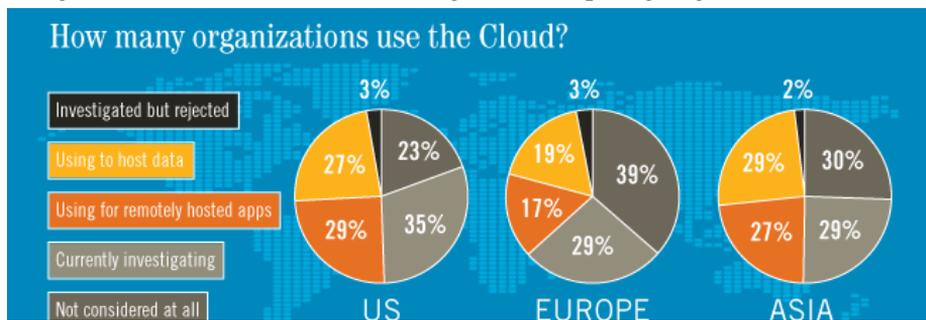


Figure 2: Example of use cloud computing in the world

Source: <http://community.amd.com/community/amd-blogs/amd-business/blog/2011/06/01/amd-2011-global-cloud-computing-adoption-attitudes-and-approaches-study-infographics/> (11.4.2014)

Although some commentators categorize Cloud Computing services somewhat differently, the most common approach segregates services into three-part taxonomy (Mell, Grance, 2009). Software as a service (SaaS), probably the most popular category, offers software for conventional operating functions such as e-mail (Microsoft Exchange mail) and desktop applications (Microsoft Word and Excel). It is also suitable for specialized functions such as accounting, payroll and customer relationship management (CRM). Infrastructure as a service (IaaS) is offering remote access to IT resources such as servers, processors, storage devices and other devices and networking equipment. Business owner and IT team are exempt from the management and maintenance of hardware. Platform as a Service (PaaS) provides shared resources (including hardware and software) which are available on request. In combination with the advantages of IaaS, this category of services allows subscribers to download and management software of your choice and can be used for design applications, development, testing and deployment.

In traditional model of software delivery, software is purchased in advance under permanent license agreement. They usually pay an annual maintenance fee to remove any bugs or bring some improvements. Software is the data center of the company. Implementation services must engage the partner companies that have the expertise in the application software. This model is still prevalent with large application vendors, making these applications available to SMB (Small and Medium Business) sector, due to the high cost and scope of the implementation.

Today we recognize a different approach when using a licensed software. Before, the license of the software vendor and the buying additional service provider (ASP) was required. ASP is a peak in the late nineties and the early years of the 21st century, but hosting fees, costs of licenses and ongoing support made the total cost of ownership extremely high. Software provider quickly identifies a better method of delivery of software from the data center and this is the way wa SaaS was born. The SaaS approach is a software solution whose delivery is made via the Internet using a common web browser. SaaS applications are typically hosted in discrete data centers that are owned or leased by the seller. SaaS model uses a complex architecture, which means that SaaS users share common parts of the application and their data and configuration of business processes are specially kept. In SaaS model, customer paid subscription price includes the use of software, support and access to all updates and service packs. From the user perspective, it is less important whether the application of a dedicated data center or cloud, although the cloud offers increased reliability and reduced downtime due to possible falls. Nowadays, the concept of SaaS includes applications which are delivered as a service via the web browser, either from the data center manufacturers, public or even from a private cloud.

## CLOUD COMPUTING SERVICES

Cloud Computing providers offer their services according to several fundamental models, Figure 3:

- infrastructure as a service (IaaS),
- platform as a service (PaaS), and
- software as a service (SaaS).

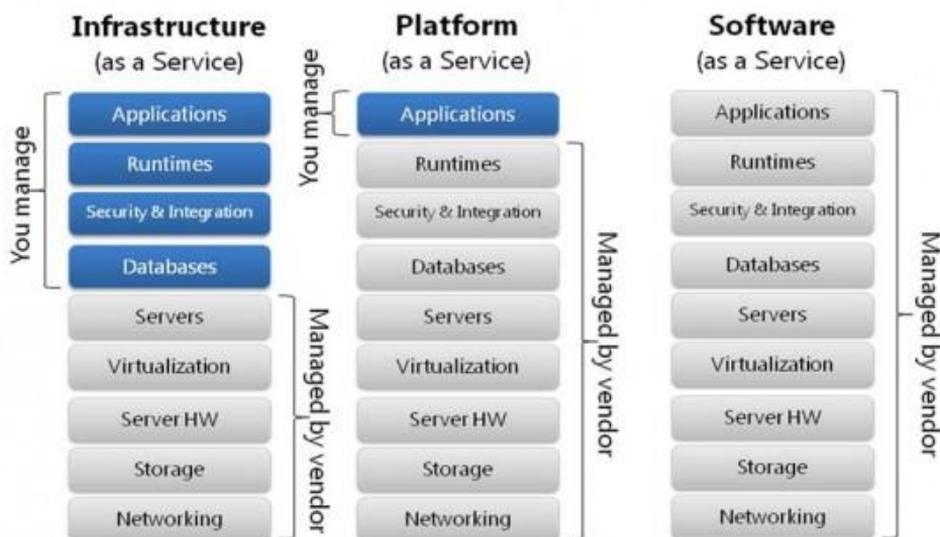


Figure 3: Structure of Cloud Computing

Source: <http://deletemalware.blogspot.com/2011/07/paas-cloud-computing.html> (11.4.2014)

Other key components in anything as a service (XaaS) are described in a comprehensive taxonomy model published in 2009, such as Strategy-as-a-Service, Collaboration-as-a-Service, Business Process-as-a-Service, Database-as-a-Service, etc. In 2012, network as a service (NaaS) and communication as a service (CaaS) were officially included by ITU (International Telecommunication Union) as part of the basic Cloud Computing models, recognized service categories of a telecommunication-centric cloud ecosystem (WikiPedia).

## ***CHARACTERISTICS OF SAAS***

### ***THE OBVIOUS ADVANTAGE***

This is a small model of the evolution of software delivery and an attractive option specifically for the SMBs sector. The main advantage is that SaaS allows SMBs to gain access to features that was previously available only to large companies with high capital. Hence, when they eliminate capital expenditures and expenses to be paid in advance, any organization can pay a fee and obtain an application as a service. Besides these obvious advantages, SaaS provides numerous additional benefits. For example, every company in Benchmarks portfolio uses Amazons cloud infrastructure in one way or another (Ha, 2009).

### ***LOW FINANCIAL RISK***

Many traditional applications include initial fees and periodic fees for support and maintenance. SaaS is different. There is not only initial investment in IT infrastructure and technological development. There are predictable and recurring costs. There are no hidden costs for upgrades and maintenance. Everything is included in the subscription. This results in a lower total cost of ownership and avoiding large capital expenditures for the benefit of lower operating costs. Upon termination or completion of the contract, the user is free to choose whether to extend them or not. The US federal Chief Information Officer Vivek Kundra has argued that Cloud Computing is economical. They are flexible, can be rapidly implemented, can improve consistency in service, can be more energy efficient, and can increase an organization's ability to focus on its mission since it can spend less time and fewer resources on information technology (Kundra, 2010).

### ***EASY APPLICATION***

It is assumed that the implementation can be expensive and a time-consuming task. In addition to investments in technology infrastructure to run the application, they must earmark funds for the installation and customization of the application. Fee for advice may further increase costs. However, today's organizations who want to be competitors cannot afford a long and complex projects in which there is an interruption or disturbance of the basic work processes. The advantage of SaaS in the fact is – in the most SaaS instances, it can be provided in a few minutes.

## ***COMPREHENSIVE SUPPORT***

Many SaaS vendors establish rates for different levels of support and service. In this way, they can choose the best package without paying for more or receive less service than you need. Unlike traditional software license, SaaS model includes subscription for comprehensive support and product maintenance and upgrades. So, there are no hidden costs or additional costs, they do not have the need to take care of the maintenance of the hardware or loss.

## ***RELIEF FOR STAFF***

In most organizations, IT staff is already overburdened. It is very important that SaaS doesn't set new demands on the IT team in the company, because there is a technological infrastructure and application environment to support it. For small and medium companies, which often lack dedicated IT resources, SaaS applications are an attractive solution. If you need additional assistance, SaaS vendors will often offer their services directly.

## ***HIGH SECURITY***

When you relocate important data to a service provider, there is a firm belief that the system is safe. SaaS vendors place their applications in world-class data centers with the most reliable power supply system and security. They also use the latest security protocols for ensuring the security and protection of data integrity. This also goes for the cloud vendors, whose servers are located in the same data center. Sellers who use public cloud application delivery also incorporate security features to protect data in transit. Crucial point for the eventual acceptance of Cloud technology in business industries will be the safety of critical data, both in transfer as in storage. Large enterprises will not be willing to support the Cloud concept as long as there is not more transparency available at which geographical location the data is stored and protected (Henschen, 2008). Reasons for that are foreign laws, which would possibly allow foreign governments to access these data, or domestic insurance contracts, demanding the data to be stored only in certain regions. But providing this required transparency would in some ways contradict the whole idea of Cloud Computing itself, and it remains to be seen how the large Cloud vendors will tackle this concern.

## ***CROSSING AND ACCESS TO SAAS***

Virtually, every type of application can be delivered as a SaaS. Customer relationship management, document management, accounting and finance, human resources - all of these critical applications are available from the SaaS provider. But the question is how many of them are willing to do this transition. SaaS application allows you to gain access to data and documents from any place that has Internet connection. People who work in the field or travel, can effectively collaborate with colleagues and share information using any mobile device. In some case, offline workers cannot use this technology, because it is solely offered online (Miller, 2009).

## ***SMART INVESTMENT***

If a company has to elicit only a recommendation and group them in one place as unique tips to help someone recognize their need to move to SaaS and decide easier to take this step, the following questions may help:

If the business has grown, are the applications geared towards small and medium sized enterprises?

Is more power and more functionality needed to assist in the growth of the company?

Is there a growing number of workers in the field and those who are mobile and who have trouble connecting via VPN (Virtual Private Network) and is there a concern about safety in these connections?

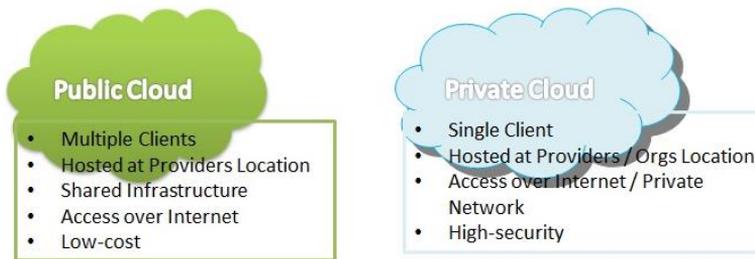
Is the technology infrastructure up to the task to run today's applications and is there the ability to invest in updating equipment?

If IT staff is overwhelmed by tasks of providing support or resources that might not have been intended and who in that case pays for the job?

Those who answer yes to more than two of these questions need to think about the basic SaaS applications as a possible solution for their organization. A further recommendation is to start with one application, such as for example stacking documents and trying how it works. Many providers offer a SaaS trial period of thirty or sixty days, so that a small team can assess the application. And if they are satisfied with reliability, security and ease of use of the application, they can include other applications that are integrated with other front and back - office systems. For sure, SaaS has many strengths and very few weaknesses. For small businesses looking to grow and remain competitive, SaaS is a smart investment.

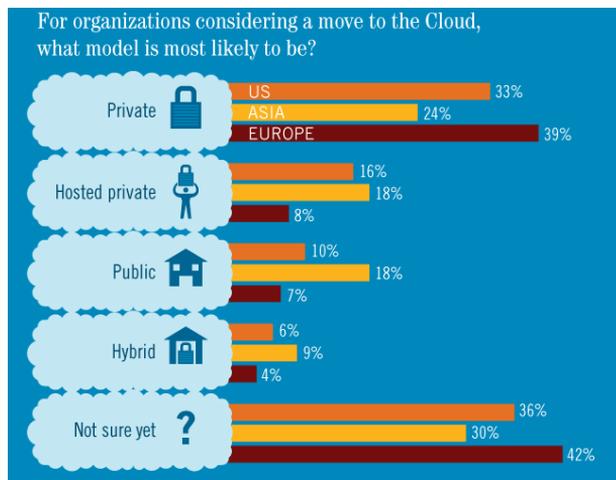
## ***PUBLIC OR PRIVATE CLOUD***

Company management often faces the dilemma of whether to take advantage of the public or a private cloud, Figure 4. The decision to create a private cloud, or use a public or hybrid cloud is based on various factors. It is important to define the differences between private and public clouds. However, these businesses should be mindful of the uses of Cloud Computing, as well as of the fact which services provide suitable public or private clouds (Staten, 2008). In Figure 5, the percentage of used Cloud Computing types around the world is given.



*Figure 4: Private and Public Cloud*

*Source: <http://blogs.msdn.com/b/aronrakwal/archive/2012/08/16/what-is-cloud-computing-public-cloud-v-private-cloud.aspx> (25.5.2014)*



*Figure 5: Representation of Cloud Computing in the world*

*Source: <http://community.amd.com/community/amd-blogs/amd-business/blog/2011/06/01/amd-2011-global-cloud-computing-adoption-attitudes-and-approaches-study-infographics> (25.5.2014)*

## ***PUBLIC CLOUD***

The public cloud is provided as a service over the Internet. In the virtual premises of Cloud provider, the customer does not have the visibility and control to cloud services. The core infrastructure is shared between many organizations, but data and usage are logically separated so that only authorized users can access them. Public Cloud reduces the complexity and time testing, as well as the implementation of new applications. It allows companies small or virtually no capital expenditures. Public Clouds have their advantages over the private cloud services.

### ***PUBLIC CLOUD - ADVANTAGES***

The simplicity and efficiency are the overall benefits of a Public Cloud service. Public Cloud offering their services is usually over an Internet connection. This type of technology provides a higher capacity of memory storage, so the users do not have to worry about their PC memory storage (Miller, 2009). Host is to manage the system and the users are to connect to the system via the web. Public Clouds charge month or annual subscription. By keeping the public cloud, organizations can reduce their IT budgets, because they don't have to buy hardware. The organization doesn't have to spend money on employees who keep track of the system, because they are taken care of by the host. If the hardware or software configuration needs to be changed or if there is a server crash and the process needs to be restarted, that would take several hours or days depending on the situation. In Public Clouds, all the virtual reconfiguration takes a minute. If one server fails, another can immediately be activated by reducing the time of arrival. Due to the fact that the Cloud serving is the host, employees are responsible for maintaining the system. The design allows users to update or introduce the tools into the system more quickly. There are no contracts and no long-term commitments. In general, the ease of use and price of Public Clouds usually wins private ones.

### ***PUBLIC CLOUD - DISADVANTAGES***

Companies need to have in mind the lack of public clouds before making a decision. Due to the fact that a third party is responsible for maintenance of data, many organizations feel they have little control over their personal data. Public Cloud services are based on the Internet connection, which means slower data transfer. If the organization keeps or carries a large amount of data, public cloud may not be the best solution. For example, many users will not tolerate slow

loading. Poor security is seen as a major drawback. Google addresses this by storing government data only within the US, but it doesn't guarantee for Public Cloud customers like small businesses (Krishnan, 2010). This doesn't mean that public cloud has no security. Most of them have great actions, but for customers with sensitive personal information, such as financial, it is difficult to trust a third party. As with any technology, such benefits are partly offset by the existence of risks, and in particular for cloud computing, security tops the list of concerns for most organizations (Gens, 2008).

## ***PRIVATE CLOUD***

A Private Cloud can also be called an internal cloud. This means that accounting and other infrastructure hosted on a private platform are not shared with other organizations. The key is that technological innovation helps organizations in the Private Cloud virtualization. Virtualization helps organizations achieve cost savings by using the existing hardware infrastructure. Virtualized systems run multiple virtual machines on a single physical host and as such, virtualized servers will be more vulnerable than physical servers for the next few years until organizations learn more about securing their systems (Gartner, 2010). It is important to note that private cloud offers the opportunity to the customer to quickly add new applications.

## ***PRIVATE CLOUD - ADVANTAGES***

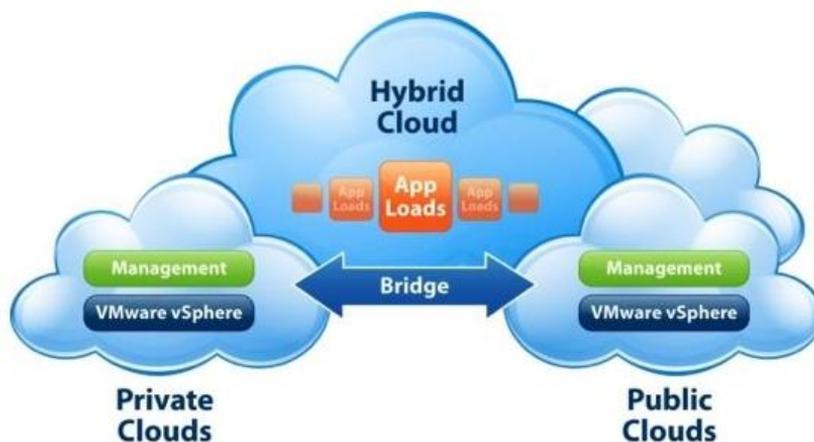
Due to the fact that the hardware is owned by them, organizations have more control over their data. The organization is responsible for monitoring and maintaining the data taking in the full control over the data. A Private Cloud is dedicated to one organization and the network can be designed to ensure a high level of security. It is deployed inside the firewall on the network organization, which means that the transmission rate is increased in relation to the use of the Internet. Hardware performance and storage can be customized to Private Cloud, because it is owned by the company.

## ***PRIVATE CLOUD - DISADVANTAGES***

Private Clouds are generally more expensive than the public ones, because they both require hardware and maintenance. In order to build a Private Cloud service, organizations must invest in hardware or use existing systems. They require system administrators, which leads to higher costs of administration. If a company has multiple data centers, maintenance costs also increase significantly. Due to the limitations of the hardware in the data center of the organization, there are limitations in the capacity of data, which is considered their biggest flaw.

## ***HYBRID CLOUD SERVICE***

A hybrid Cloud service, Figure 6, is the combination of a Private and a Public Cloud. It refers to an organization that keeps some of its operations in house (Private Cloud) and also utilizing a cloud service from an outside provider for its other operations (Public Cloud).



*Figure 6: Hybrid Cloud*

Source: [http://www.nirix.com/cloud-solutions/\(11.4.2014\)](http://www.nirix.com/cloud-solutions/(11.4.2014))

For example, if an organization has both sensitive and non - sensitive applications, it can use a hybrid cloud to get the best of both worlds. The Hybrid approach can allow business to take advantage of the cost effectiveness that a Public Cloud service offers while keeping mission-critical applications within a Private Cloud. A company can keep each aspect of its business in the most efficient environment possible. The downside is that you have to keep track of multiple different security platforms and ensure that all aspects of your business can communicate with each other.

## ***RETURN ON INVESTMENT BY USING CLOUD COMPUTING***

The cost of Public Cloud is dropping fast, so how can they make sure that the value is in accordance with the money spent? It is not a secret that the cost of cloud services is dropping as more choices become available and the providers battle for the customers, but it is not always easy to ensure them. Although it may seem clever to go for the cheapest option in terms of balancing the books, it is more important to go for an option that will give you the highest return and this can sometimes mean paying that little extra in the beginning, to make it the best value for money offering in the future. In the SMB segment, the fastest adoption of Cloud services is in the UK and Europe and that is because many of the SMB firms are growing fast and looking to use cloud for cost saving. SMBs also want agility and the ability to reach new markets that other, larger, companies are not able to do because they already have investment in non-cloud-based real estate.

The first important step in identifying which service provider to go for and whether to go for a Public, Private or Hybrid Cloud is to approach a local trusted provider for help and identifying what should be moved into the cloud and for advice on whether everything should be moved to a Public, Private or Hybrid service.

Although the Public Cloud is cheaper, it may be more appropriate to focus more on creating a Hybrid Cloud and understanding what workloads are best deployed where and not automatically thinking everything is the best concerning the Public Cloud. It may be that they only need to use a service part-time and in that case, there is no need to pay for server space full time. The world is getting more dynamic in the sense that volumes of transactions are not predictable from a business point of view. The world is automated. Everything depends on IT and infrastructure. They must run and implement business processes.

Already at present, many consumers use Cloud services for private purposes – although possibly without knowing that they are doing so – for example through the usage of certain e-mail providers or social networks. Apart from data management advantages, consumers can be motivated to use cloud services by means of financial and ecological benefits, for example if they learned that cloud usage could reduce their energy bill and help them protect the environment (Jaeger et al. 2009). The IT devices of private households in Germany consumed 60 % of the total energy consumption of IT in 2007, and the ratio is expected to further rise until 2020 (Stobbe et al. 2009). Thus, even small energy savings in each household may lead to a significant overall impact (Kumar, Lu, 2010). However, these favorable prospects again rely on customer knowledge and acceptance of the new IT infrastructure.

## ***EXAMPLES OF CLOUD COMPUTING***

Before the advent of the various developments in the parlance of Cloud Computing, the majority of internet users were used to the email, which could be stored in the cloud and remain if deleted ( in case the person has an account like Yahoo mail, Hot mail, Gmail etc). But the idea of massive storage of data, synchronization of such data, word processing, gaming and a bulk of what the computer could hitherto perform physically in the past, is now done in the cloud. There are typical examples of Cloud Computing.

- Microsoft SkyDrive (Microsoft Cloud Computing) is a cloud based storage device for personal and corporate files, data, information etc. which is accessible from anywhere through an internet connection. Microsoft Word, Power Point, Excel and a great deal of other products of Microsoft can be accessed for free. SkyDrive application can be downloaded and installed in a PC if the system supports it. Otherwise, it has to be accessed directly in the clouds. In order to access SkyDrive, you need a SkyDrive.com account, through which the cloud is accessed. Microsoft provides up to 7GB free storage for documents, photos, files, data etc. Users of Windows 8 are at advantage as SkyDrive application is integrated into the operating system and by implication, it can be accessed easily when the system is online. This is one of the advantages of Windows 8.
- Google Drive (Google Cloud Computing): This was known as Google Docs until recently, when it was changed to Google Drive. Google Drive is an example of Cloud Computing where videos, photographs, files, documents and data can be stored and organized whether for an individual or a corporate organisation. Google offers up to 15GB free storage for users. There is a periodic payment plan for additional storage as the demand grows for clients. Google account is required to access this facility. For easy access, Google Drive can be downloaded into a PC or into a similar form.
- Dropbox (Dropbox Cloud computing): This one is the Cloud Computing giant and a front line outfit in the industry. Since its inception in the year 2007, it has made some remarkable landmark achievements worth emulation by others in the same competition with respect to quality of service. By implication, Dropbox offers Cloud storage for its clients for files, documents, Videos, data synchronisation and much more. Apart from the free storage offer, more storage as referral bonus is available. For additional storage demand, a competitive payment plan is available.
- iCloud (Apple Cloud computing): iCloud is cloud based and owned by Apple incorporated for the storage and sharing of files, music, documents, applications, videos, photographs, data etc, built into every compatible Apple and other form. The iCloud application can be downloaded from Apple store and installed into your form if compatible. This can be accessed anywhere, as long as the device is compatible via an internet connection.

## ***WORKING IN A VIRTUAL OFFICE***

However, Google's online suite of office applications is probably the best known, but by no means the only solution or offer. Rather than having a system and space hogging suite of applications like a word processor, a spreadsheet creator and a presentation or publishing platform sitting on computer, they could opt to work online instead. Accessibility, potential for collaboration and perhaps even online storage are just some of the benefits of satisfying your office suite needs by working online. Examples of online suite offer include: Ajax 13, Think Free and Microsoft's Office Live. When somebody needs to meet with a customer, sending him a meeting request in Outlook that includes a link to an online meeting hosted in Lync Online, that is very impressive. Online meetings are much easier to arrange and enterprises use them extensively. In addition, online conferences can host up to 50 people at a time (O'Reilly, 2012).

## ***ACCOUNTING IN THE CLOUD***

Painless bookkeeping: brings all your finances together into one place, tax payment and invoice dates to calendar, free support and regular software upgrades, bank-level security and data protection. They build professional estimates and proposals which can be tracked through to approval and converted to invoices. Charts of invoice payments show month-by-month when payments are due, overdue or have been paid. Electronic bank statements and building monthly balanced charts are obvious advantages, as well as tracking what the company owes to the user, by adding out-of-pocket expenses, including scanned expense receipts.

## ***FLEXIBLE ENTERING***

If you need complete visibility on how your time is being spent, FreeAgent lets you easily log timeslips for work done on active projects. Switch between weeks and months and see at a glance where your time is going. When the project is complete, generate an invoice from all unbilled time and send this to the client in minutes.

## ***TIMESHEET REPORTING AT YOUR FINGERTIPS CLOCK ICON***

At any stage in a project, they can generate flexible and professional time tracking reports, broken down by contact, project, user and tasks. If necessary, these can be printed off as high quality PDFs and submitted to the client. This is something especially useful for contractors.

## ***INVOICING SOFTWARE THAT HELPS GET PAID FASTER***

The FreeAgent traffic system instantly shows the status of invoices, allowing quick determination what has been paid, what payments are outstanding or what still needs to be sent. Also, it is possible to filter invoices by status or invoice date, including tax years. Once the invoice has been paid by clients, FreeAgent will reconcile the invoice and payment into bank account. This provides a more accurate picture of money used in business. Integration with PayPal means that PayPal links could be included in emails so clients can settle the invoice online immediately. It's all about getting paid faster. Invoicing with FreeAgent means getting paid faster and with less effort. They can create invoices with a company logo or even create their own design.

## ***EXPENSE TRACKING***

For expenses such as magazine subscriptions or web hosting, it is possible to set them to automatically recur. A comprehensive list of expense categories helps building accurate accounts which are priceless at tax time. For complete accountability, FreeAgent allows uploading of scanned expense receipts as attachments to expense records. These can be viewed as individual expenses or be downloaded as the original files again, at any time.

## ***ACCOUNTANT FRIENDLY***

By giving access to account, the clouds are able to give you instant, better and more relevant advice, Figure 7. It's a completely new way of working with your advisor that benefits both parties.

Income	Expenses	Operating Profit ?	Less
\$34,977	− \$17,651	= \$17,326	\$1,300 Drawings
Retained Profit ?	Carried Forward/Distributable ?		
Current year so far \$16,026	+ From 2011/11 \$10,358	=	\$26,384

Figure 7: Year and Month Profit and Loss

Source: <http://www.freeagent.com/tour/accounting> (25.5.2014)

Track income and outgoings to get a true picture of business over time. FreeAgent also builds month and year Profit and Loss statements. FreeAgent builds a fully balanced sheet for business with a comprehensive list of your company's assets and liabilities. Year-end accounts can be handled as soon as the books are up to date. Some Cloud-based systems allow accepting many forms of payment and have the funds deposited directly into business bank account, to help firms in maintaining a healthy cash flow (Bates, 2011).

### ***SIMPLE SALES TAX***

Everybody can set the appropriate sales tax for any country and FreeAgent applies this to all required sales and purchases. Additional sales taxes can also be added for regions where multiple sales taxes are needed and can mark these sales taxes as compound, as is required in certain places. Quick, easy and configurable reports show all the sales tax charged on invoices.

### ***CLOUD ACCOUNTING***

FreeAgent's cloud accounting software is completely web-based - there's nothing to download, update, or install and you can access it from your regular browser. Everybody can use it anytime, from any computer - no more sharing spreadsheets or lugging around your laptop. It is not needed that the user worries about computer crashing and losing all of your business's books - with FreeAgent's cloud accounting, all of data is securely transferred at backup servers several times an hour.

### ***SECURE CONNECTIONS***

The security of data is of biggest concern. FreeAgent uses 256-bit SSL technology to encrypt all transactions between firms and servers of vendor. It is the same technology that banks use to protect data. Redundancy and resilience is built into hosting infrastructure. They operate out of two geographically isolated data centres (DCs), so they can offer full DC-level failover in the unlikely event that an entire DC becomes unavailable. As well as maintaining real-time copies of vendor database across two separate data centers, they additionally run a full database backup every four hours with additional incremental backups several times an hour. These backups are encrypted and transferred to a secure offsite location. They also allow downloading all data from within FreeAgent account at any time.

## ***MOBILE PHONE***

Whether on iPhone, an Android handset or Windows Phone, FreeAgent will just work on browser. It's free and there's no application to be installed.

## ***DISCUSSION***

Cloud Computing is a challenge to many analysts. Most people think that solutions must be created within the organization as well as its own product, based on its needs and capabilities. Management companies do not need to waste valuable time on managing and maintaining servers, database or application infrastructure, they should be more devoted to their primary business. Opponents of Cloud Computing mainly deal with security issues and legislation.

In the transition to Cloud, it is necessary to check the performance that the vendor offers. Applications that use large data base or require a fast processor and capacity of RAM may not be the best choice for the Cloud, since it would run them and the use itself would be too expensive. It is the best to check the details with the Cloud provider. Caution is needed with providers that have a minimum price for a monthly service fee, because it can directly affect the level of support that the provider offers.

It is necessary to determine precisely which security issues are the responsibility of the organization, and which security issues are the vendor's responsibility. It is necessary to estimate the time and cost of transferring large amounts of data on the Cloud, as well as to inform on the business continuity and the training of employees. Along with that, it is needed to pay special attention to internal business issues, especially to those related to human resources, because a large number of organizations is faced with the discontent of employees who may feel threatened.

Cloud computing is definitely a new age in the era of computing that tags along a number of benefits. They can be classified into several different categories, namely:

- virtualization,
- democratization of computing (small and medium enterprises operating in the infrastructure that has already been available only to large companies),
- scalability,
- commodification of infrastructure (IT department is able to deal with the strategic aspects of the business).

## **CONCLUSION**

Cloud Computing has numerous advantages, but also some disadvantages. It can be seen that the benefits of cloud accounting outweigh its negative aspects. When firms use cloud correctly and efficiently in a business, they cannot only increase profits for a company by allowing fewer employees to work remotely, they can also increase the productivity of a company. As more and more companies turn to Cloud Computing to save money and to increase business value, the future of Cloud Computing becomes more uncertain. The popularity of these services will only continue to increase, especially while companies are continually forced to adjust to decreased budgets.

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# APPLICATION OF BUSINESS INTELLIGENCE AND OLAP TECHNOLOGY IN BUSINESS DECISION-MAKING

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## ABSTRACT

Basic goal of this paper is application of business intelligence and OLAP(On-Line Analytical Processing) technology in development of decision-making process in a way that it should facilitate, as much as possible, decision-making based on the knowledge which is hidden in the transaction systems. Managerial decisions that are made in business systems, determine their competitive advantage, so obvious is the need for decision-making to be free of subjective impressions, and to be based upon knowledge more. Having in mind the area and the goal of the research, the methods that will be used in researches are: inductive and deductive method, as primary logical method, which during research enables drawing of certain conclusions on the research subject and methodology of objectively oriented development of business intelligence system, which includes: defining the demands, analysis, design and implementation of business processes. Analytic processing of data can be done directly over relational data base (ROLAP) or over the prepared data base (MOLAP). OLAP gives the opportunities to users to individually pose questions, which significantly increases the possibilities to do analysis necessary for decision-making. In this paper the authors used exam results as indicators of efficiency of educational process, by analysing them according to the examination period. This paper uses the exam results as indicators of efficiency of educational processes, analysing them according to the exam periods, terms, subjects, grades... The application of instruments of business intelligence and OLAP technologies enables the users to individually set demands, which significantly increases the possibility for executing the necessary analyses in decision-making, providing the conditions for better and faster reactions to spotted problems. The contribution of this paper can be seen in application of business intelligence and OLAP technology, to the following and advancing the teaching processes, improving their standards, developing the scientific and research work, more quality decision-making and management of educational processes. Also, the significance of this paper can be seen in application of very efficient standardized tools like Microsoft programs, MS EXCEL and MS Query for quality and successful business analysis; it makes the decision-making processes shorter and decisions better and more rational.

**Key words:** Business Intelligence, Data Base, Multi-Dimensional Analysis

**JEL Classification:** D80, I21

**UDK:** 005.94:004.9 005.311.6:004.65

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## ***INTRODUCTION***

Complete and precise information at the right time represents one of the basic resources of business and the key for best business decision-making. During data processing one finds hidden relations, sees new business possibilities which contribute to making quality managerial decisions.

Quality management of a business system and its processes represents a critical factor of business success. Making the right decision directly and indirectly depends upon the quality and the right time of information that the decision-maker has. For obtaining such information it is necessary to have appropriate data in every moment. The gathering of raw data does not represent the solution of the problem of decision-making process, nor the quality management. Great amount of unstructured and unprocessed data can represent the difficult circumstance during decision-making, because it can easily blur the essence of a problem and „getting lost in the sea of data that do not have a purpose“ (Balaban, 2006).

Operational information systems are mostly oriented towards executing business and transactions and less towards the issue of decision-making. Information of one enterprise is mostly inconsistent and unavailable. The problem is finding the necessary information as well as uncertainty of the information's accuracy, which results in poor business decisions. Additional problem in managing large systems is the inability of the managers to individually and in a simple way access the necessary data and shape them into necessary information. Even in the cases when wanted information exists, it is often hidden in the huge mass of data and cannot be used. Obtaining the necessary data from such a complex systems is very expensive and sometimes impossible. That is the reason why the larger and larger number of companies develops and uses the systems for business intelligence, in order to use the existing data better and faster in creating information needed for the decision-making process.

The application of business intelligence process enables using only that information that is necessary, at that moment, to make the managerial decisions. The advantage of this concept is the increase in information quality, to show it in a simple way as the reduction of large number of information that the employees are usually exposed to.

The main purpose of business intelligence is generating the quality information that will enable making the best possible business decisions.

## ***DEFINITIONS***

Business intelligence is an area within the information technologies, whose goal is to put all the information potentials of an enterprise into function of making the top quality decisions, with the ultimate goal to realize the determined strategic goals of an enterprise.

Intelligence: intelligence is inborn ability to understand properly the things and notions in life and everything else, reason, mind, the ability to understand, as a collective noun, all people that have this trait, classier and better world in general, educated people (Vujaklija, 1980).

The notion of „business intelligence“ that signifies the systems for support in decision-making process, in the respect of a separate part of information technologies comes from English language. (Business Intelligence, BI). "Business Intelligence" as a notion was suggested by Howard Dresdner (A Brief History, 2014.), in order to categorize the concept and methods that help in easier business decision-making by using the facts based systems.

Business intelligence represents the data analysis, reporting and tools for setting demands that can help business users to make their way through multitude of data and to synthesize the right information. Those tools are today called business intelligence (Gartner Group report, 1996).

There are many definitions of the notion of business intelligence that are different according to the author, and the point of view that is used to approach this subject. Even though there is no unique definition, what is in common to all the definitions is that the business intelligence is seen as a group of methodologies, i.e. the concept that brings the qualitative progress of decision-making process. A positive effect of the decisions made by using this concept is greater because it implies obtaining the quality information on time, systematization of information, clearer identification of the right information and easier access to information.

When one uses data to make quality information on time, i.e. knowledge, the probability that the decision made based on them will be right and on time and largely free from subjective impressions (in the sense of assumption on missing information) and uncertainty with making decisions ( decision-making needs decisiveness).

Business intelligence represents the group of new application formed in such a way that they can organize and structure data on business transactions in a way that enables the analysis useful for the support to the decision making and operational activities of an enterprise. Or simply said, business intelligence represents the process of gathering of available internal and significant external data and their turning into useful information that help business users with decision making (Kalakota, 2001. p. 349).

According to Larisse T. Moss's and Shaku Atrea's (The Origins of Business Intelligence 2014) definition, business intelligence represents an architecture and the collection of integrated operational applications, then the applications for support to making decisions and data bases that enable the business systems easy access to information.

From the technical point of view, i.e. from the point of view of information technologies, business intelligence is a process of multiple levels, where a large amount of information is stored in information systems of an organization and the application systems, turns into useful information. Business intelligence system consists of three wholes, the first one is made of data sources, central point is the data base where data from the source systems are collected and adjusted and the third component is the analytic tools (Rajković et al., 2012).

## ***RESEARCH METHODS***

The setting and developing, as well as the general researches, are based on certain scientific and research methods:

- modelling method as a systematic research action which is used to build simulation model that is capable of substituting the subject of the research,
- observation method which enables gathering, from the real system, sufficient amount of data which will be used as entry data for researches the simulation models in order to draw the conclusions on the system that the model represents,
- methodology of objectively –oriented system development of business intelligence which includes: demand defining, objectively –oriented analysis, objectively –oriented design and implementation,
- inductive and deductive method, as basic logical methods, that enable the drawing some of the conclusions on the research subject.
- With the goal of comparative analysis and forming the personal attitudes and conclusions we used comparative method is the process of comparison of obtaining information by a classic process and process by using the business intelligence and OLAP technologies.

## ***KEY FINDINGS***

"Business intelligence is some kind of business radar. It warns for threats, points to the business opportunities, foresees that something is going to happen, adequately prepares for the inevitable, expands the manoeuvre space for decision making, to sum it up, it increases the controllability of success that you want to achieve by doing business" (Kukrika, 2011).

Business intelligence is a necessity and an imperative of every successful business, managerial idea with clearly defined tools, without which the quality management is an illusion. The conditions of doing business are constantly changing and becoming more complex, and the changes demand faster reactions. In order to manage the right way, management needs quality information, directed

towards managing, that encourage activity. Such information are delivered by business intelligence.

Considering the spectrum of activities of business intelligence which implies: analyses of the set goals of an organization, constant comparison of planned and realized, coordination of activities of different organizational units in the business system, assessing the current state, making decisions, information transfer etc. it can be concluded that the business intelligence represents the means of efficient realization of business results.

Frequent question is: Can we predict what the future holds? If our business system has a modern information system, well-developed management control and uses the elements of business intelligence, we will surely have quality information based on which we will no longer feel insecurity in making decisions and we will have a better vision of future business (Medić, 2013).

When an organization gathers the data and organizes them into databases, data warehouses and local data warehouses, then it can use them for further analysis (Figure 1).

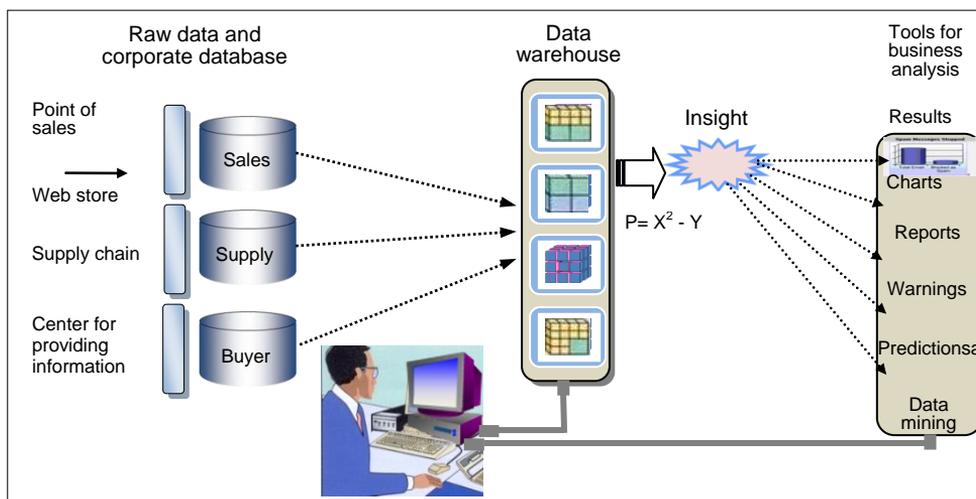


Figure 1: Principles of business intelligence operations

Source: Authors

Business intelligence implies applications and technologies for consulting, analysis and securing the access to a vast amount of data that help users to make better strategic and business decisions. Business intelligence system unifies the methodologies, technologies and platforms for data warehousing, OLAP data processing (Online Analytical Processing) and data mining, enabling the companies to create useful managerial information from the data on the business found in various transaction systems and come from different internal and external sources.

## ***DATA WAREHOUSE***

Base of the support system to decision making is analytic data base Data Warehouse (DW), whose one of the primary functions is to maintain the processes and regulations of business of an organization as a whole. As an effective and efficient support to management, DW cleans and aggregates the data from the operational systems and places them into so-called dimensional data bases, which represent the repository of consistent historical data, easily accessible and subject to effective manipulation. Data organized like this are used for assessing the state of business situations, trends, projections and alternatives with the purpose of support to decision-making process (Balaban, 2006.).

DW contains a large amount of data which are organized in smaller logical wholes that are called Data Marts. Data Warehouse systems use denormalized data, which enables faster execution of the demands over such data. According to the definition set by William H. Inmon (Inmon, 1995), data warehouse represents subject-oriented, integrated, time-variant and non-volatile group of data, and the ultimate goal is support given to the managers in decision-making processes:

- subject-oriented – directed towards specific organizational activities or decision processes instead on the current operations.
- Integration – centralized database which contains data from different sources internal, external and personal.
- Invariability - DW does not change permanently, but it only periodically adds new data depending on the business needs.
- We can say that the key characterises of DW are time dimension and ability to transform business, operational and other data into data warehouse, in a quality way.

Data in data warehouses are time-variant, which means that every data that is in the warehouse is connected to some moment. In the end, data in warehouses are invariable i.e. when a data is written in the warehouse he can only be accessed. Ralph Kimball defines the data warehouse as a copy of transactional data structured in such a way that it enables setting the demands and data analysis (Kimball, 1996.).

These demands and data analyses are almost impossible to execute in OLTP systems because in such systems data are constantly changing. Information from a specific time frame is often called data recordings. For example, if an analytic database contains data recordings on sales that are taken every evening, it will be clear during data analysis tomorrow that those data are a day old. Then daily, weekly and yearly comparisons make sense because we will always have consistent values which we can compare.

Data Warehouse is formed to enable the users of different levels the solving of various analytic tasks. It enables:

- reporting and monitoring of business processes,
- analysis and setting the diagnose, finding information in an interactive way by setting the demands and analysing the obtained results,

- planning and simulation, making and executing models of plan and simulation,
- access to a large amount of data for the end user,
- creating and demanding different trend reports,
- extraction, transformation and placing the large amount of data.

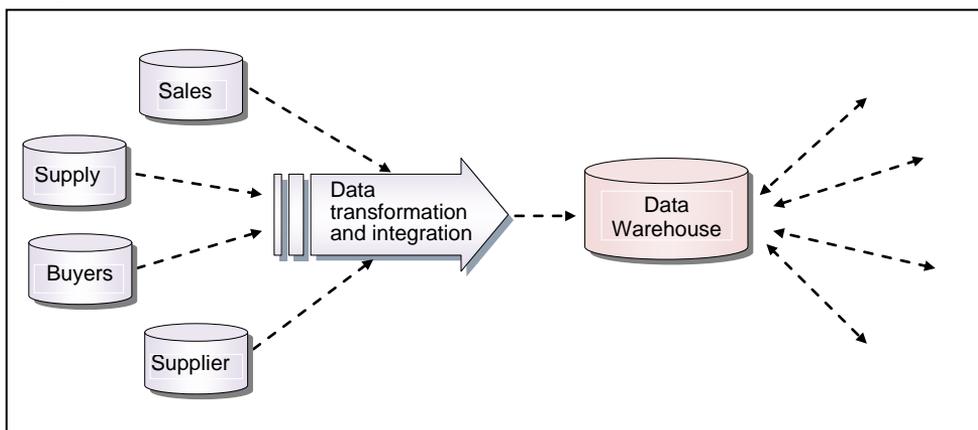
## ***DATA WAREHOUSE ARCHITECTURE***

Data from the source systems are integrated and transformed before they load to the data warehouse considering that the data are taken over from various sources and platforms, they have to be integrated and transformed before they are placed into data warehouse.

Some of the advantages of data warehousing are:

- simplicity,
- better data quality,
- faster data access,
- separate support processes for decision-making and production processes,
- providing competitive advantage,
- distributed data base,
- possibility of parallel processing,
- platform independence,
- security.

Basic architecture of data warehouse is given in the figure no 2. Basic component of data warehouse is database



*Figure 2: Basic architecture of data warehouse*

*Source: Authors*

Data warehouse architecture has the following characteristics:

Data are extracted from various source systems, databases and folders – systems found in companies are basic data sources for data warehousing. Data which are necessary for support system to making decisions are taken from these systems where their number can be large. Sometimes it is necessary to extract all the data that are found in these systems. It is most often the case that the data are taken from different data bases, from different platforms and different formats and data types.

## ***ON-LINE ANALYTICAL PROCESSING (OLAP) SYSTEMS***

Basic role of OLAP (on-line analytical processing) tools is to find and answer to the users questions as quickly as possible, their usage is for n-line analysing of data and reporting. In the beginning the users' questions were relatively simple. However, in time they have become complex so that the relational tools (OLTP tools - On-Line Transaction Processing), (by definition OLTP systems represent the transactional systems for updating of databases and transactions' processing), were not able to provide answers in an acceptable timeframe. This is exactly the purpose of OLAP tools. They enable a simple synthesis, analysis and consolidation of data. They are being used for intuitive, fast and flexible manipulation of transactional data. OLAP systems support complex analyses that are done by analytics and enable data analysis from different perspectives (business dimensions).

When we say OLAP we think of the program tools that are being used for manipulation of multidimensional data that come from different sources. In order to use fully the OLAP's potential it is necessary to have as large amount of data as possible. This is why along with OLAP we talk about data warehousing. In order for an OLAP product to be considered an application, it has to have three key characteristics:

- multidimensional view of data,
- possibility of using complex computer operations,
- possibility of time data analysis.

Analytic systems are the systems that provide information which are used for problem analysis and are primarily done by using comparison or analysis of patterns and trends. For example, analytic system could show how a certain type of product is being sold in different areas of the country. It could also show how one type of product is being sold now in relation to the period when the product appeared at the market for the first time. Analytic databases are developing for analytic systems.

The question of what the end user needs?

- He must be able to pose any business question,

- Able to use any data from the business system for analysis,
- Able to get indefinite number of reports.

Business decision-makers need answers to the questions that directly influence their ability to be competent at the fast changing modern market. They need clear answer no matter how difficult the question is, as soon as possible. This is why we use OLAP analytic systems that provide information that are being used for problem or situation analysis. Analytic processing is primarily done by using the comparisons or pattern and trend analysis.

Figure 3. shows the place of OLAP systems in decision-making process.

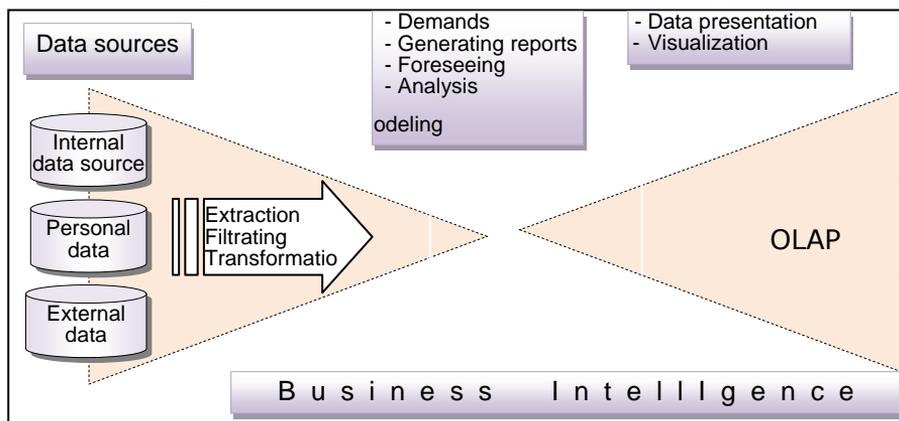


Figure 3: Place of OLAP system in decision-making process

Source: Authors

Analysing the data patterns and trends demands the existence of large number of historical data. That is why the analytic data bases do not contain newest data, but they keep information from a specific moment. For example, it is possible to determine if the sales in one month has significantly fallen only if the system has the data on sales in the previous months, so that the data can be compared.

OLAP systems use characteristics of multidimension and denormalization of data and it can be said that they represent the upgrade of data warehouse.

Interface of OLAP system should enable the user to work comfortably, to individually perform the analytic operations and getting the overview and business graphics, without the skills of programming and knowledge of database structure.

OLAP tools very efficiently enable moving from the tables to multidimensional charts by using the dynamic screens. This defined OLAP or hyper cube contains tens of thousands of possible reports that are easily changed, quickly defined and executed even faster.

Demands that OLAP system has to fulfil are:

- Possibility of working with a large group of data and users,
- Short response time,
- Integrated data that connect OLAP server and relational database,
- Possibility of working with data with various levels of details,
- Ability to calculate the complex mathematical functions,
- Support for what-if analysis modelling and planning,
- Simplicity of introducing and maintaining the system,
- Data protection,
- Possibility of working with a large number of tools with which one can access the data, do analyses and show data.

## ***ARCHITECTURE OF OLAP SYSTEM***

Under OLAP system architecture we imply the way in which OLAP system works with the data from data source.

- Some of OLAP tools physically transfer all connected transactional data from the relational database and other sources into multidimensional database, using meta level, and fill data warehouse over night (batch approach), i.e. they do complete renewal of data in certain time intervals.
- Another approach, the so-called *on-line*, transfers every individual change of relational into multidimensional database i.e. it updates the warehouse only with the data which have changed between two intervals of updating. However, middle solution is often used, where batch method is the basic one while only some changes at the old data are transferred individually.

Previously defined approaches provoked the appearance of two basic architectures:

- multidimensional OLAP (MOLAP) and
- relational OLAP (ROLAP).

MOLAP is a solution when multidimensional databases are being used, and ROLAP emerges as the upgrade of relational databases. MOLAP and ROLAP are different in the way they physically store data. With MOLAP systems data are kept in multidimensional structure and in the case of ROLAP system data are kept in relational databases.

Based on what we have just said, we can conclude that the cubes in OLAP tools store in three different models:

- relational storing model is called relational *on-line* analytic process or ROLAP, and
- multidimensional on-line analytic process is called MOLAP.
- When the dimensions are kept as a combination of these two variants, then such a model is known as hybrid on-line analytic process or HOLAP.

## RELATIONAL OLAP (ROLAP)

ROLAP or relational OLAP systems are done based on the data that are in the relational database, where the databases and dimensions charts are kept as relational charts.

This model allows the multidimensional data analysis considering that it enables the users to use traditional OLAP functions of cutting and turning. This is achieved by using any of the tools of SQL system for reporting the system to separate directly over the data warehouse.

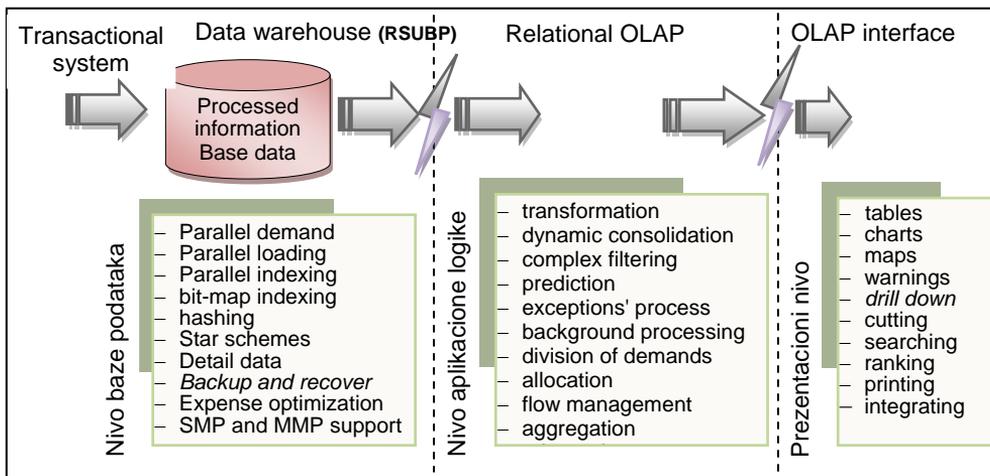


Figure 4: Architecture of ROLAP system

Source: Authors

The advantage of ROLAP model of OLAP analytic tools is that it is more stable when managing a huge amount of data. Another advantage of ROLAP tools is that they are efficient in managing the numeric and textual data. It also enables the users to get the details of data that are found at the lower level of hierarchical structure (drill down). The picture 4 shows the architecture of ROLAP system.

Lack of ROLAP applications is slower performance in relation to other styles of OLAP tools because the calculations are done inside the server. Another lack of ROLAP tools is that it is dependent on using the SQL for data manipulation.

ROLAP systems are optimized for data access, while MOLAP systems are optimized for data gathering. Advantage of the ROLAP systems is that the summary tables are created directly in relational system for database management (RSUBP), which provides short response time, and the tables are very clear.

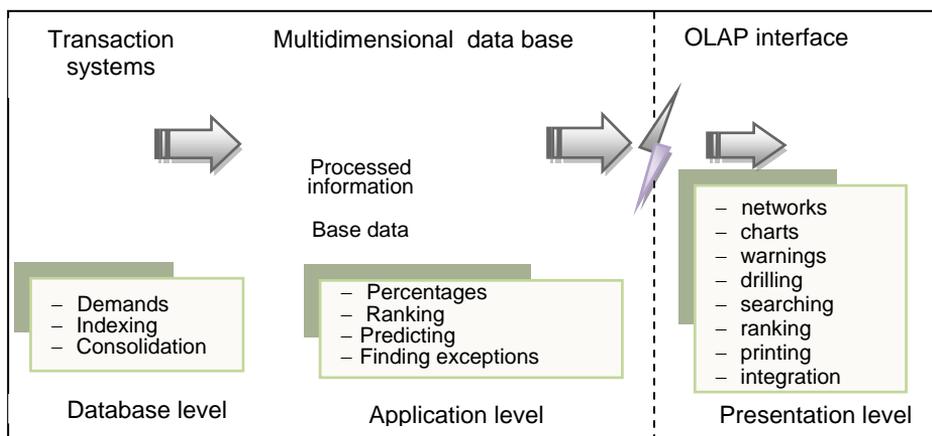
Basic reasons for using the ROLAP system is that there are already developed and checked tools for them for data storage. Also ROLAP systems are created because they provide a direct approach to data from tables so there is no need to duplicate the data like MOLAP systems do.

## ***MULTIDIMENSIONAL OLAP (MOLAP)***

Multidimensional OLAP – MOLAP is considered a classic form of OLAP. One of the main differences between MOLAP and OLAP tools are the data, With MOLAP they are summed and kept in an optimized form of multidimensional cube, instead of in relational database.

Main advantage of this model is that it provides excellent performances of the demands because the cubes are designed for a fast data access. While using this model, data are structures in such formats in accordance with the clients' demands for reports with already calculated data in cubes.

MOLAP model is considered to be the best OLAP tool for creating reports considering that it enables the users to reorganize easily or rotate the structure of the cube in order to see different data aspects. MOLAP analytic tools are in condition to do complex calculations. Considering that the calculations are previously defined during the creation of the cube, it results in faster access to calculated data in relation to ROLAP. MOLAP systems also enable users to quickly forward the data into a group of data. Also, in relation to ROLAP, MOLAP is significantly less demanding when it comes to hardware because of the data compression technique. In short, MOLAP is optimized for demands and access to summary data.



*Figure 5: Architecture of MOLAP system*

*Source: Authors*

There are certain limitations in MOLAP system's application. Basic weakness of MOLAP tools is that they are less scalable in relation to ROLAP tools. MOLAP approach also introduces data redundancy. In the end, MOLAP demands additional investing because cube technology has to be specially built in an organization which demands investments in people and resources. Picture 5. shows the architecture of MOLAP system.

MOLAP databases have a limitation of physical size of data groups with which they can operate. In order to do any kind of analysis, it is necessary to load the data first into multidimensional structures. Various calculations are done in order to create the aggregations and complete the data, which can last for a long period of time. After the process is completed, the user can start the analysis.

Lack of MOLAP systems is the difficulty to add new dimensions. According to that MOLAP systems are good to use in cases when it is impossible to divide a large group of data into smaller groups of data (Tot, 2009).

We can see in picture 4 that the data from different transactional systems are loaded into multidimensional database with the help of batch routines. When data loading is done, creation of aggregations begins, after which database is ready to work. Users make their demands for OLAP reports via interface.

### ***CONNECTION DATA WAREHOUSE - OLAP- DATA MINING***

Creating Data Warehouse and using OLAP tools enables the aggregation of historical data and data manipulation through interactive approach to multidimensional information. Through previous models and methods one can get the answer to the questions like what the last month's income was, what the fluctuation was in the observed period, what region the highest growth was achieved in. Identifying the observed fact (e.g. income) in relation to certain previously defined factors (place, time, buyer, product, price etc.), conditions for further analyses is created based on which the decision will be made.

Analysis should give answers to why the situation is like that and in which way business actions should be directed in the future in order to improve the business result. Data Mining is a process of automatic finding of hidden relations and patterns in behaviour among data, which implies using various statistical techniques, artificial intelligence and creating the predictive models based on discovering the relations among the data. Data Mining gives the possibility of receiving an answer to the question without setting of any assumption in the influence of a certain factor.

As a data source that is processed through Data Mining one uses databases and data warehouse. Data warehouse is not necessary for data mining, because data mining technology can be applied to the operational and transactional databases.

Data Mining and OLAP are complementary systems because before the relations among the data are determined (data mining), the certain assumptions based on which the relations are made have to be set (OLAP):

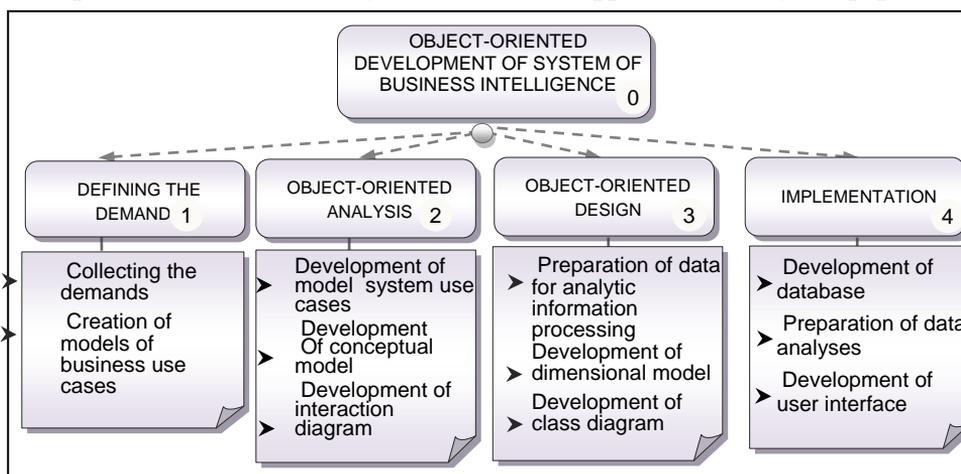
- OLAP is a part of system tools for decision-making process support and it gives answers to the questions if some assumptions that are taken from the database are true. OLAP analysis is basically a deductive process.
- Data Mining access tries to find some relation between data. Data Mining is an inductive process.

## ***EXAMPLE OF APPLICATION OF BUSINESS INTELLIGENCE IN EDUCATION***

There are several approaches or methodologies for designing and development of business intelligence concept. However, there is no consensus over which technology is best, but it depends on the characteristics of and actual system.

Methodology of object-oriented development of business intelligence system was born form the analysis of standards IDEF0 (*Integration Definition Function Modelling*), IDEF1X (*Integration Definition Information Modelling*), UML (*Unified Modelling Language*) and methods for creating data warehouses. This is a contributing to the development of methodology of object-oriented development of business intelligence system, because it integrates the known classic methods of functioning (IDEF0) and informatics (IDEF1X) modelling with object approach (UML), (Stanojević, 2008).

Figure 6. shows the structure of the built methodology of object-oriented development of business intelligence, which was applied in writing this paper.



*Figure 6: Structure of methodology of object-oriented development of business intelligence system*

*Source: Authors*

Object-oriented methodology consists of the following steps:

- Defining the demands,
- Object-oriented analysis,
- Object-oriented design,
- Implementation.

## DEFINING JOBS' TREE

Based on the defined limits of the system, we go over to the activity of defining the jobs' tree where it is necessary to determine the vertical (hierarchical) connections among jobs. Jobs' tree is defined by application of the method of solving problems top-down, when a complex job is separated into many sub jobs, and then one should solve simple sub jobs.

Defining of the diagram of decomposition jobs – Faculty of Business Economics and Entrepreneurship from Belgrade.

Figure 7. shows the decomposition diagram of jobs in the school.

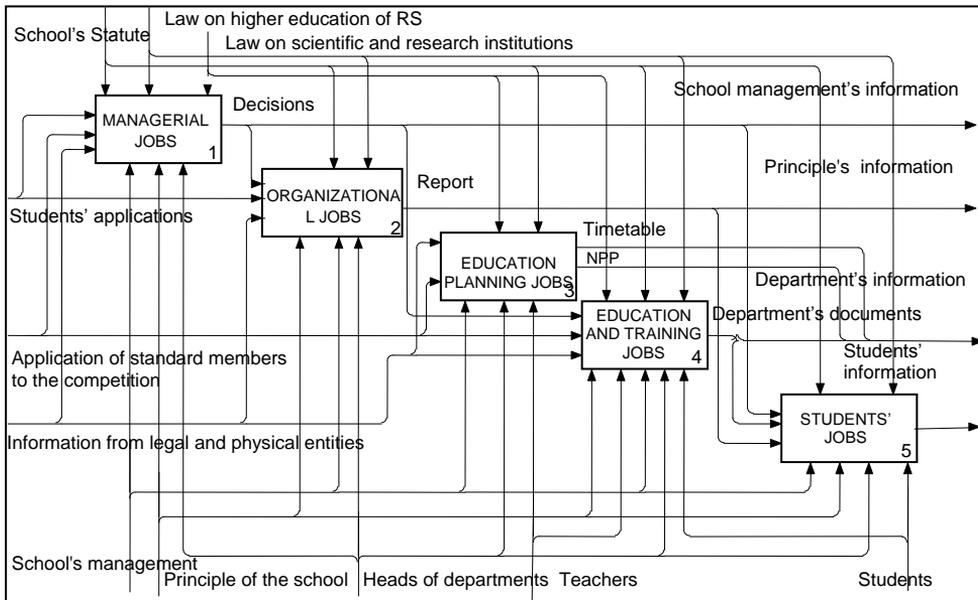


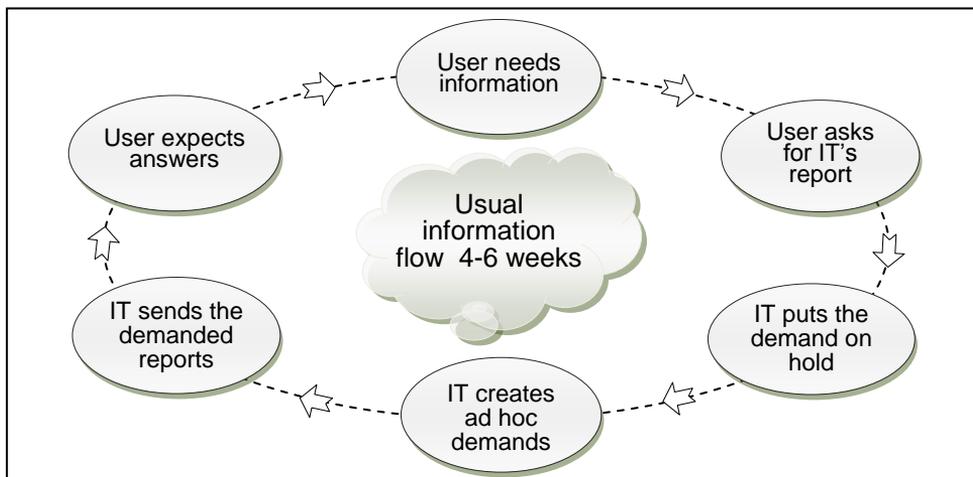
Figure 7: Decomposition diagram of jobs in school

Source: Authors

Following IDEF0 standard, appropriate arrows show the sets of documents that are defined as information. All information at every next level is divided up to the level of activities, where they are defined through arrows as actual documents.

## ***PROBLEMS WITH TRANSACTION SYSTEMS***

Basic source of data for the Faculty of Business Economics and Entrepreneurship are transaction systems. Their basic purpose is to enable everyday collection of the data on business transactions, with as low time delay as possible, in order not to slow down the business processes.



*Figure 8: Inadequate attempts of IT sector to provide information*

*Source: Authors*

Transaction systems are practically developed to perfection and have enabled current evidencing of business transactions and storing vast amounts of data. However, because of high complexity of the structure of these systems, obtaining the analytic reports is very hard and demands involving information technologies experts. Besides this, this kind of structure demands great time delay while receiving the analytic reports, and they are often unable to respond to information demands of the strategic nature (Figure 8).

OLAP cube solves the problems of complexity of reporting from transaction systems by introducing the new so-called dimensional data structure, which is intuitively clear to business users (decision-makers) as well and not only to information technologies experts. Dimensional data structure consists from *dimensions* and *measures*. Dimensions represent the structure of the cube's heading of report, while measures represent the aggregated data according to dimensions and dimension members.

Besides the problem of complexity of reporting OLAP cube solves the problems of time delay while obtaining reports, by keeping in its structure previously aggregated data according to dimensions and dimension members. OLAP takes up larger data warehouse space in relation to transactional systems but it significantly speeds up the process of creating complex reports which often cannot be obtained from the relational structure.

## ***OLAP SYSTEM FOR STUDENTS' SUCCESS ANALYSIS***

OLAP or multidimensional analysis signifies the analytic data processing that is done in real time, interactively. OLAP is the only business intelligence technology. It enables to analysts and control managers to have an insight in business indicators by a fast, consistent and interactive approach to analyses. Through analyses, information got via data transformation from operational sources, is seen from various angles of business context.

OLAP as one of the technologies of business intelligence, through consistent and interactive approach, enables the following and analysis of students' success. The purpose of this system is following the number of students that:

- have the right to apply for exam,
- apply for exam,
- sit an exam,
- pass the exam,
- fail an exam,

As well as the percentage reports of all parameters like for example. Sat / passed, at the level of:

- exam period,
- term,
- year (or more years),
- every subject, or
- cumulative, per department and at the level of the entire school,
- for Bachelor and Master studies.

These reports are being analysed at the end of every exam period, term and year. Without OLAP system for obtaining these reports it would be necessary to create dozens of complex demands, which are usually inflexible, so even the slightest change in the demand would cause creating new demands.

Additional problem is that the data needed for creating of new demands are physically kept at different places. That is why a data warehouse is created, which unifies all extracted data and automates the flows for transfer and integration of data into the warehouse.

We will show the way in which the demanded reports are being got, with the help of OLAP cube. As a software tool for reading the data from the cube we used *Microsoft Excel*. If there are only three dimensions according to which the data are analysed, OLAP structure can be represented graphically as a three-dimensional cube (Figure 9).

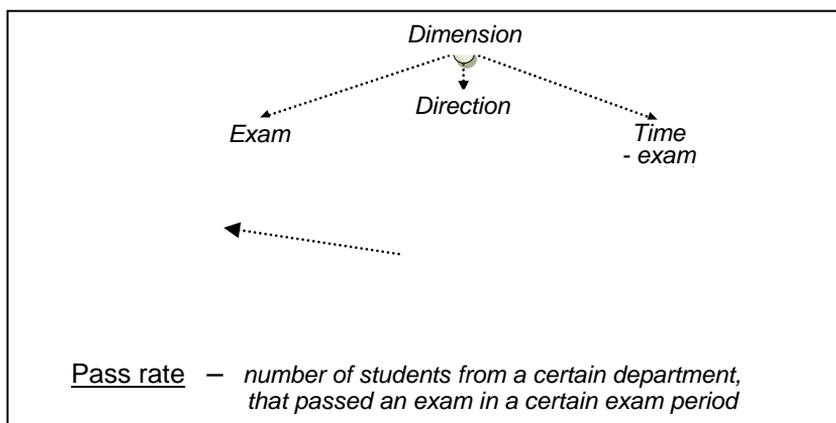


Figure 9: Three-dimensional OLAP cube for monitoring the pass rate

Source: Authors

In the case shown in the picture 9, every cube represents the number of students from a certain department that have passed the exam in a certain exam period.

In the picture 10, we showed the report on basic parameters of students that passed exams according to subjects in one term in 2013. These reports can be very important to decision-makers in analyses of results, number that sat an exam and number that passed it, number of students applied, comparing results among the subjects, terms etc. We wanted to be concise so the rest of the subjects per term have not been shown, but such results are got by just one click to the wanted term. In this case the parameters refer to all the students that took exams and all exam periods that are noted in OLAP system.

Row Labels	Sum of ImaloPravo	Sum of Izasao	Sum of Pao	Sum of Polozio	Sum of Prijavilo
0	516	306	89	261	366
1	532	584	218	366	850
2	913	555	198	261	554
* Makro ekonomija	143	78	12	66	90
* Poslovna informatika	115	79	20	59	89
* Poslovna ekonomija	151	80	48	32	123
* Menadzment	17	12	4	8	15
* Matematika za ekonomiste	156	80	43	194	194
* Monetarna ekonomija	150	120	34	128	128
* Sociologija	17	11	10	11	11
* Ekonomska statistika	164	95	30	55	139
3	663	497	228	269	954
Grand Total	954	243	135	918	991

Figure 10: Report on the number of students that took exams per terms and subjects at the yearly level

Source: Authors

However it is often necessary to analyse the number of the students who passed or failed an exam, but only of those who enrolled at that year of studies for the first time. This is achieved by dragging the dimension Student in the field for data filtering. If it is necessary to get a report only for certain exam periods the dimension Exam Period is dragged in the field for filtering and one can choose a specific exam period.

By introducing the dimension Group in the columns of the report, one would get a report that shows the number of students that passed and failed an exam per every department for every subject, while choosing different parameters of dimensions Year and Exam Period one can get different reports (for one of more years and exam periods). It is generally possible to create a large number of reports that are structurally different, as well as the values of parameters, without information technologies expert knowledge.

The advantages of Microsoft Excel as a tool for report creation from OLAP cube is that it shows the desired reports in the format favourable for presentation, and further formatting of data showed is possible as well as calculation of derived values based on data got in the report.

Further, we showed a pivot chart connected to the exam analysis, which was created for the needs of this paper.

The figure 11 shows pivot chart which shows the average grade at the exam per year of studies (2010, 2011, 2012 i 2013) for subjects, Business informatics (BI), Management of information systems (MIS) and Electronic business (EB).

*Table 1: Pivot chart which shows the average grade of selected subjects,*

Year	(All)				
Exam period	(All)				
Student	(All)				
Subjects and average grade per year of study		2010	2011	2012	2013
Business informatics (BI)		7.63	7.86	7.92	8.12
Management of information systems (MIS)		7.22	7.18	7.33	7.33
Electronic business (EB)		6.78	7.34	7.89	7.95

*Source: Authors*

Figure 11. Gives a graphic overview of data from pivot chart, Table 1.

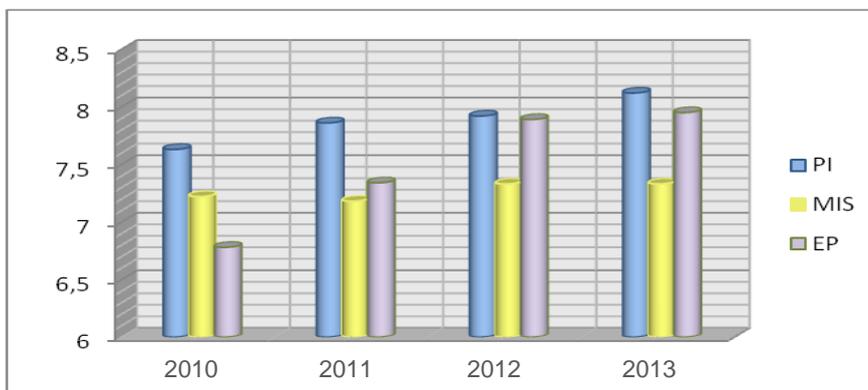


Figure 11: Average grade of selected subjects - graphic overview

Source: Authors

Pivot tables and charts enable insight into some value's movement trend like it is shown in table 1. And figure 11., which enables predicting the results for the following period. We can notice the growth trend of the average number of passed exams of Business informatics, Management of information systems and Electronic business, so we can predict that in the following year this average number will be even better. This can be a signal to decision-makers to specially monitor the process of realization of lectures from subjects with this trend, so that it can serve as a positive experience. It is more important for the decision-makers to spot a trend of fall in the exams passed, in order to fix the educational processes by appropriate measures.

In general it is possible to create a great number of reports that are different in structure and values of parameters, without information technologies expert knowledge. The result of this paper is a developed business intelligence system that contains data warehouse, OLAP cubes and appropriate pivot tables for data analysis which decision-makers need. OLAP cubes and pivot tables enables the exam analysis to be done using many dimensions, different levels of details, depending on the current need.

## **CONCLUSION**

Economic globalization, constant and radical changes in business environment, imposes the need to change the current management style. New technologies and tools that enable fast and efficient approach to data become inevitable in such circumstances. Business intelligence transforms data into information and information into knowledge, which leads to decisions based on information and actions that follow them, and that is the value that it brings to the business world in fighting the competition.

Business intelligence tools enable the process of gathering internal and external data and their turning into useful information which help business users with making-decisions. Data based on using these tools of business intelligence provide the possibility to see not only the advantages but also the problems, so the causes can be analysed on time, instead of just solving the consequences. Business intelligence systems are focused on improving the possibilities for access and distribution of information, to those who make them as well as to those who use them.

Efficient process analysis in educational institutions is essential for control and improvement in their operations. Modern education systems at all levels should have a function of satisfying the students' needs for knowledge. At the same time, educational institution must develop, adjust to the circumstances and thus improve educational processes in the conditions of global competition.

This paper describes the advantages of application of OLAP systems for analysis of students' success at a higher education institution (picture 6 and 7). We shortly presented the procedure of implementation of one of OLAP systems by using the object-oriented methodology of development of information system on the example of analysis of the students' exams. As a base for building OLAP system, we used OLTP information system which is implemented in the School, we defined OLAP cube (picture 9) and completed the creation of user application in pivot tables and charts (table 1 and picture 11). Pivot tables enable analysis and comparison of data according to various criteria. It is also possible to create large number of reports that are different by their structure and the value of the parameters.

Created user interface provided, through OLAP system, a detailed analysis of students' success per selected subject, measures and comparisons of success per term and year of studies, which enables an adequate analysis of all educational processes and comparison of success with all the educational systems in the environment. Information got by the process analysis of the School is a base for an efficient work of the management of the School.

For successful management of educational processes of high education institutions in the conditions of fast development of advanced information and communication technologies, we suggest using business intelligence tools. In this way by application of OLAP system technologies, through business intelligence one can provide taking the corrective measures in case of deviation from set goals, which enables the decision-makers to have an optimal control of all educational processes in all scientific areas and it is applicable in all educational institutions.

Combining of various business intelligence techniques, OLAP cube, development of Data Mining methods, and usage of data from the external and internal sources as well as expert knowledge contributed to improvement of performances of all components of business intelligence system showed in this paper, which had as an ultimate goal to increase the efficiency and effectiveness of educational processes as a whole.

The applied models of business intelligence and OLAP technologies provided faster, more precise and flexible reporting, which enables fast and quality decision-making of all interested decision-makers. Optimized ILTP systems, applied for business analysis of operations of higher education institution, enabled the decision-making process to be shorter, better and more rational. Application of business intelligence, OLAP technology contributed to understanding the necessity of using knowledge, as the most important resource for fast and efficient decision-making in the process of successful business systems' management. We believe that, very soon, business intelligence and OLAP technologies will find their wider application in our region.

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# **LEAN LEADERSHIP AS A PRECONDITION FOR SUCCESSFUL BUSINESS OPERATIONS OF ENTERPRISES**

Saveta Vukadinovic, MA<sup>13</sup>

Jovanka Popovic, PhD<sup>14</sup>

## **ABSTRACT**

*Lean is a process-focused management concept that seeks to increase customer's value by reducing waste and continuously improving processes. Majority of enterprises, when implementing Lean concept, puts emphasis on tools and methods, although a full commitment of employees to continuous process improvement is crucial for the successful operation of Lean enterprises. This is accomplished through a special management style - Lean leadership, so we can say that leadership is a key success factor for accelerating the adoption of Lean concept and the missing link between theoretical solutions and its application in practice.*

*This paper suggests that enterprises implementing Lean should focus on the leadership behaviors that are crucial for Lean to progress beyond the standard limitations, and have a significant impact on business of enterprises and the whole industry. The paper is based on a systematic literature review that examines how the application of Lean leadership contributes to the creation of value in the organizational processes and achieving operational excellence. The starting point is defining concepts and key features of Lean and Lean leadership, given by the prominent authors. The next step is clarifying the basic principles of Lean leadership, the main objectives of its application and possibilities for further improvement. Further, we have discussed the relationship between traditional and Lean leadership, as well as the process of knowledge management in Lean enterprises. Finally, the aim of the paper is to attempt to offer some original consideration to what Lean leadership is and why it is important for management and business. By doing so, the authors hope to bring more clarity to the subject of Lean leadership, which will be beneficial for people studying Lean, as well as for Lean practitioners and the body of academic knowledge.*

**Key words:** *Lean Concept, Lean Leadership, Continuous Improvement, Employees*

**JEL Classification:** *L21, L23*

**UDK:** *005.346 005.336.1*

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## ***INTRODUCTION***

Lean is a philosophy derived mostly from the Toyota Production System (TPS), and has two fundamental elements - process improvement by removing waste in order to maximize value for customers, and a commitment to respecting and developing people in order to create a culture of continuous improvement. The main purpose of Lean manufacturing is to increase productivity, improve product quality and manufacturing cycle time, reduce inventory, reduce lead-time and eliminate manufacturing waste.

Today, there are already many organizations trying to implement Lean philosophy in everyday business. This paper suggests that the enterprises implementing Lean should not be overwhelmed with the toolbox of Lean tools and techniques, but should focus on the leadership behaviors that are crucial for Lean to progress beyond the standard limitations, and have a significant impact on company business and the whole industry. Lean is much more than just techniques; it is a way of thinking which involves everyone in a culture of continuous improvement. It is a human system, customer focused and customer driven approach, where the employee are the customers of their upstream colleagues (Liker, 2004, pp. xi).

The most contemporary organizations are managed and led by thoughtful, hardworking people who want success of their enterprises, but problem lies in finding leadership system that will make this possible. Leadership, nowadays, is the well-known and often discussed process of influence exerted by one person, accepted and followed by all, over the other factors (human resource) that he works with, in order to reach the organizational goals (Văcar, Miricescu, 2013, pp. 430). Leadership is the critical success factor for accelerating the adoption of Lean in the organizations. Bearing in mind a growing interest in the importance of Lean leadership, this paper attempts to offer some original consideration to what Lean leadership is and why it is so important in management and business.

## ***LEADERSHIP - THE CONCEPT AND FEATURES***

Any group of people, that wants to work together and achieve a shared objective, need to march in the same direction. People need to know where the enterprise is going and what they are supposed to do to contribute in reaching enterprise goals. Leadership is the process by which leader sets goals or direction for that group of people and motivate them to act with competence and commitment in achieving goals. Leadership is one of the defining elements of successful enterprises and it is linked to the leader's personality, his ability to influence, to generate interest, expectations and emotions, and his ability to arouse the interest of employees. This involves creating the vision, setting goals, determining the values and principles of action.

Leadership is actually an observable set of skills and abilities that are accessible to any person, at any level, in any organization. With this in mind, the term leader is used to describe anyone with the ability to influence the work of others (Kouzes, Posner, 2007). Burns (1978) saw the leadership in relationships and developed the concepts of the transactional and transformational leadership. He described the transactional leadership as a relationship between leader and follower where they exchange values, and the transformational leadership as an engagement between leader and follower based on an increased level of motivation and morality. Glynn, DeJordy (2010, pp. 122-125) have summarized different theories of the leadership. They began with the trait or great-man theories, which claim that leaders were born, not made. These are followed by behavioral theories, in which leaders have certain properties and features. In contingency theories, leadership is treated as a change process, and leaders are adjusting to different situations becoming a catalyst of change. The most current leadership theories are based on behavioral and contingency theories.

The definitions of the leadership can also be organized into five approaches. Yukl (2010) defines them as a trait, behavior, power-influence, situation and integrative. The each approach has its merits and contributes to the application and practice of leadership. The trait approach assumes that great leaders are born, not made and determines which personality traits were important for effective leadership. Traits that are common for most of leaders are intelligence, self-confidence, determination, integrity, and sociability (Northouse, 2013). In behavior approach, the focus is on behaviors that individuals demonstrate, not on innate characteristics of the individual (Yukl, 2010). This approach attempts to map leader's behaviors to their effect on subordinate satisfaction and performance (Bass, 2008). The power-influence approach examines the influence process between a leader and the group members. The essence of leadership is the realm of power, the capacity to influence (Bass, 2008), and sources of power are reward, coercive, legitimate (position-based), and expert and referent (person-based). In the situation approach, the leader's effectiveness is dependent on the situation, in particular of competency and commitment of subordinate workers (Yukl, 2010). At the end, integrative approach involves more than one of the above approaches (Yukl, 2010). Despite the difference in perspectives, Northouse (2013) identified some common elements of leadership, which all approaches share: 1. it is a process; 2. it occurs in a group; 3. it involves influencing; and 4. it is concerned with goal attainment.

The role of the leader is to articulate a common vision and then marshal management and organizational resources to build the necessary systems and structures to insure the smooth accomplishment of the mission (Shim, Steers, 2012). A good leader must be a good communicator who cares about his employees and an expert in his field, a good strategist who thinks ahead and a promoter of change, because change is vital for future success. By the continuous adaptation to market changes, a leader helps his organization to continue to grow and thus become more competitive, by employees whom they have available. He must encourage employees to come up with new ideas to involve them in planning and

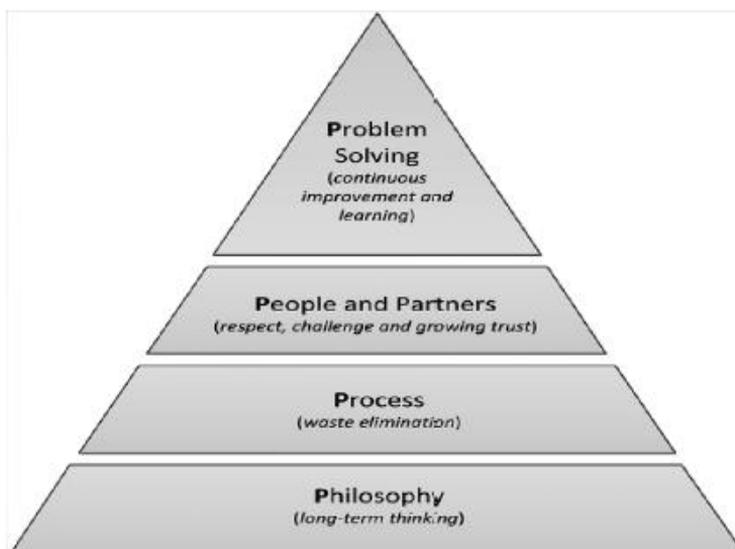
implementing change and such change will not be only accepted, but also implemented by the team (Văcar, Miricescu, 2013, pp. 431). For this reason, some theorists suggest that the essence of leadership is the leadership of change (Yukl, 2010). The leadership of change is important for Lean philosophy because the adoption of Lean practices is fundamentally about managing an organization-wide change.

### ***NEED FOR A LEAN LEADERSHIP***

Lean leadership is the missing link between theoretical solutions and application in practice. It can also be considered as the missing link between the toolbox Lean and continuously improving organizations (Mann, 2009, pp. 16). Developed as a production system, eliminating wastes in the Toyota's plants in the 1960's, Lean is evolving into a management approach that improves all the processes at each level of an organization. Many eminent authors have studied this phenomenon, but a unique and generally accepted definition of Lean leadership has not been adopted yet.

The crucial element in transforming an organization from traditional to Lean is leadership. The contemporary researchers argue that the lack of understanding which leadership style is preferred is a problem for management in implementation of Lean practices. In Lean management, the people bring the system to life: working, communicating, resolving issues, and growing together. Lean leadership goes well beyond by encouraging, supporting and demanding employee involvement. Lean leadership requires committed management, proper training, and culture of continuous improvement in the enterprise. Continuous improvement literally means making things better every day, sometimes by taking big steps and more often by taking small steps.

The key factor for the success of Lean enterprises are employees (Liker, Meier, 2007, xvii), and their biggest challenge the change in behavior and mindset of employees and leaders (Mann, 2009, pp. 17). The essence of Lean can be described with Liker's 4P model: philosophy, process, people and partner problem solving (Liker, 2004, pp. 6).



*Figure 1: 4P model of the Toyota Way*

*Source: Liker, 2004, pp. 6 (adapted)*

According to the 4P model, Lean philosophy and long-term thinking are an inextricable part of Lean leadership, indicating a need for constant and sustainable development of employees and leaders. Lean leadership is a precondition to continuous process improvement, so its task is to create an environment in which waste will be eliminated, and the great value for consumers will be made. Respect for people, that is encouraging participation and improving knowledge of employees, is one of the main foundations for Lean leadership. Finally, Lean leaders should have the expertise in learning and coaching problem solving.

Most enterprises have focused on the process and elimination of waste by using Lean methods and techniques, completely ignoring the other three elements of Lean. Their goal was to improve constantly every process, every day, in order to achieve continuous process improvement, which is impossible without motivated and dedicated employees. For the Lean, the core of empowerment is workers participation in Kaizen – the ability to participate in decision-making and problem solving. In the past, management instructed the workers in their improvement actions. Now, operative employees have to point out improvement possibilities, too. Therefore, leadership needs more employee participation and employees need basic knowledge about the Lean production systems (Dombrowski, Mielke, 2013, pp. 570).

For a Lean initiative to succeed in an entire enterprise, leaders at three organizational levels must play complementary roles and be closely related. Effective Lean leadership comes from both, the top and lower in organization, but

senior leaders play a central role in Lean management. Their contributions are essential in (Mann, 2009, pp. 16):

- Developing and implementing structures and processes that anticipate and respond to the difficulties of a Lean initiative that crosses internal boundaries;
- Transforming commitments to change into actual change, supporting and sustaining new behaviors and practices;
- Increasing the odds that process improvements survive the transition from project mode to the ongoing process;
- Establishing and maintaining new, process-focused measures alongside conventional measures of results;
- Creating conditions in which a sustainable Lean culture of continuous improvement can develop.

Successful sustained Lean conversions often involve changes in culture. Proper use of Lean is to create a Lean management system to fit the environment and culture, rather than forcing the environment and culture to fit a Lean management system. Therefore, it follows that success in Lean implies a change in what leaders reinforce - a change in leadership behaviors and practices. The failure of most Lean initiatives can be pinned on a failure to change leadership practices (Mann, 2009, pp. 17). Lean success requires a change in mindset and behavior among leadership, and then gradually throughout the organization. Throughout the continual effort to decrease inefficiency, the Lean leader strives to create a more efficient organization.

## ***PRINCIPLES OF LEAN LEADERSHIP***

Lean leadership is a methodical system for the sustainable implementation and continuous improvement. It describes the cooperation of employees and leaders in their mutual striving for perfection. This includes the customer focus of all processes, as well as the long-term development of employees and leaders (Dombrowski, Mielke, 2013, pp. 570). Although there is no consistency among authors about defining Lean leadership, the majority agrees about five of basic principles inherent to this concept.



Figure 2: The five principles of Lean leadership

Source: Dombrowski, Mielke, 2013, pp. 570.

Improvement culture contains all the attitudes and behaviors that result in continuous striving for perfection in the enterprise. Perfection is most often described as a state with zero waste, zero inventory, zero defects and losses of any kind. A distinct feature of improvement culture is observing current problems as a chance for learning and future advancement. The goal is to discover the root cause of failure and make an effort it does not happen again, not to find the culprit for the failure. Operational workers have the best insight into the weaknesses and shortcomings of the process, but they need management support in order to implement improvements in all processes and at all levels. Continuous improvements essentially do not function without formal rules and regulations and the active role of leaders in improvement activities. Lean leaders need to hear the ideas of employees and help them to carry out those ideas in practice.

The self-development is an important principle of Lean leadership, since some attributes depend on the leader's personality, but others have to be learned and developed (Liker, Convis, 2012, pp. 47). Transformation into Lean leadership requires new knowledge and leadership skills, and both leaders and workers are guided by a sensei, who is a kind of teacher or mentor. Sensei uses short learning cycles based on Deming cycle (Plan-Do-Check-Act) to achieve self-development.

Qualification of employees is a crucial task of Lean leaders, because in this way workers can actively participate in the continuous improvement. As Liker, Convis (2012, pp. 228) impose, continuous development of processes must go along with a continuous development of people. Developing skills and qualifications of employees does not imply only conventional education using courses and trainings, but also the everyday training through the problem solving in a specific workplace. That is the famous Toyota kata method, presenting particular behavior routines, habits or patterns of thinking and conducting oneself, that are practiced over and over every day (Rother, 2010, pp. xvi). Toyota Kata is a structured way to create a culture of continuous learning and improvement at all levels.

Gemba is a Japanese word that signifies an actual place, ie workshop or a place where value is added. It is also known as go-to-Gemba or genchi genbutsu. According to the Gemba principle, Lean leaders should go to the workshop frequently, in order to truly understand the processes and to make the right decisions. They need to spend a couple hours observing processes, until they realize, from the first hand, critical points and opportunities for improvement. With this approach, the Lean leaders can identify the root cause of a failure without being misled by inaccurate data collection or interpretation (Liker, Convis, 2012, pp. 35). They should even get their hands dirty by working on process improvement. Doing so, Lean leaders will have an insight into the importance of operational workers and appreciate more their contribution to the enterprise success.

In order to implement these behaviors in their daily practice, Lean leaders should follow the five golden Gemba rules:

- Go to Gemba first. Lean leaders should go to the place where the problem occurs.
- Check. Lean leaders should urgently analyze everything - products, processes, people etc. until they find out the cause of the problem.
- Take temporary countermeasures. Find some countermeasures that will satisfy the customer immediately and provide extra time for the next rule.
- Find the root cause. It is very important to identify the root cause of the problem. Otherwise, the solution will not have long-term effectiveness.
- Standardize. After finding the root cause, the permanent countermeasures can be taken. The current process is being revised and new standard must be found.

Hoshin Kanri or target management is the fifth principle of Lean leadership and it implies that is necessary to have a superior system, which directs individual activities on the path to continuous improvement. It seeks to improvement activities do not have opposite directions and to contribute the big-picture strategic goal. Hoshin Kanri is the process of setting goals and targets and, most important, the concrete plans for reaching those targets. It's another example of personal leadership being guided by institutional leadership (Liker, Convis, 2012, pp. 148). Hoshin Kanri is a leadership development tool, not just a tool for achieving business objectives. As leaders develop and follow good problem-solving processes, achieving the business objectives will come more naturally (Liker, Convis, 2012, pp. 249).

The above principles are developed into practical behaviors that can be demonstrated, understood and replicated using rapid learning techniques, with particular focus on team leadership.

## CHARACTERISTICS OF LEAN LEADERS

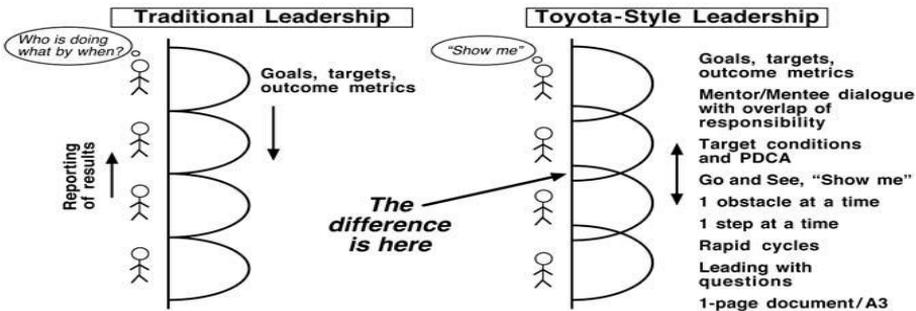
Lean management is surprisingly different from the conventional leadership practices. The next table shows some essential differences between the traditional and Lean leadership.

Traditional Leadership	Lean Leadership
Short-term financial results focus	Long-term philosophy
Get the product out (push)	Customer Driven (flow & pull)
Local optimization	Overall system optimization (by reducing waste)
Standards limit creativity	Standards enable continuous improvement
Hide the problem	Make the problem visible
We can't afford to stop the process	Stop and fix the problem
Leader is a boss	Leader is a teacher
Go to the charts and graphs (count the number of mistakes)	Go see at the workplace
Who?	Why?
Quick to plan, slow to act	Slow to plan, quick to act
Experts & specialists solve problems	Everybody solves problems at the right level
Position establishes (or seems to) authority to make decisions	Position establishes responsibility to get decisions made

*Figure 3: Traditional leadership - Lean leadership comparison*

*Source: <http://www.leanvs.com/lean-coaching.htm>*

In addition, we can say that traditional leader is proud and quickly achieves objectives through the people. Unlike him, the Lean leader is humble and patiently develops people throughout the process improvement. Furthermore, as Figure 4 underlines, the main difference lies at the interface, the interaction, between manager and subordinate (Rother, 2010, pp. 225). Some authors talk about the empowering leader, which is a leader, that actually does not lead, but supports and helps teams and people to learn and lead themselves. The traditional leader gives clear orders, well-defined tasks and seemingly tight control from top to bottom. Quite the opposite, the empowering leader is a developer of people, teams and the organizational structures that support them.



*Figure 4: Lean leadership*

*Source: Rother, 2010, pp. 225.*

It takes a deep commitment and usually about 10 years of time to become a true Lean Leader. Key factors for achieving this are patience, a focus on long-term rather than short-term results, reinvestment in people, product, and plant, and an unforgiving commitment to quality.

We know that Lean leaders must possess the general characteristics and skills of effective leaders, such as creating a vision, knowing what drives the people they lead, active listening, empathetic questioning, helping people to satisfy their needs, etc. Apart from that, Liker and Convis (2012, pp. 35) indicate five core values of a Lean leadership. These values are having the spirit of challenge, having a continuous improvement mind, going to where the work happens, embracing teamwork, and having respect for the people. Lean leader takes responsibility for other people reaching their objectives. He encourages engaging people through their contribution to team performances and strongly believes in developing individuals through team problem solving. Lean leader has exceptional relationship-building skills and he focuses on building the trust. Lean leaders are also advocates of change.

Lean leaders, like all other leaders anywhere, want to see measurable results. However, they know that the financial result is a result of quality of processes and people. Jon Miller suggests using the PROFITS acronym, to describe some of the essential qualities of Lean leader that result in profits (Seven Essential Qualities of a Lean Leader, retrieved from:

[http://www.Gembapantarei.com/2009/10/seven\\_essential\\_qualities\\_of\\_a\\_lean\\_leader.html](http://www.Gembapantarei.com/2009/10/seven_essential_qualities_of_a_lean_leader.html), June 18th, 2014).

P is for Perspective. The Lean leaders should hold a long-term perspective and guide their organization to make the best decisions over the long period. The depth of perspective requires the leader to be curious enough to go see, listen, connect with people and learn about the work in details. A lean leader sees beyond own horizon, is aware of the larger impact of actions, and thinks in terms of total costs.

R is for Responsibility. Many leaders have exhibited a high degree of personal responsibility to gain their position. The further an organization moves from interacting directly with customers, the weaker the sense of responsibility is (eg government bureaucracy, internal customer relationships, and financial service organizations). Therefore, Lean leaders need the quality of strong responsibility in order to earn lasting results and respect.

O is for Openness. Leaders must be open to change, especially to new ideas. Lean leader needs to constantly challenge ideas and assumptions, particularly his own. Taiichi Ohno said that even sages are wrong half of the time, but leaders are no sages, and need to be open to being wrong so they can mend their ways. With proper perspective and responsibility, openness should gain a sense of urgency.

F is for Flexibility. A Lean leader must be a skilled two-way communicator, able to adjust quickly to differences in styles. At best, communication style to accommodate the leader is only as effective as leader's style. Flexibility for a Lean leader is the ability to accommodate differences in style, communication, and circumstance without reverting to type and defining the problem as it fits their favored personal solution.

I is for Inertia. Inertia usually means "a tendency to remain inactive", but that is not the Lean leader's definition. Technically, inertia is the tendency of a body to maintain its state, speed and direction, unless acted upon by an external force. The essential quality of a Lean leader is steadiness, confidence, persistence, constancy, sticking to the principles and process, unless a sufficient external learning influences him to change his ways. Leader should have more of inertia.

T is for Teamwork. An effective Lean leader must be willing to identify, influence and be influenced by the needs of his team. A Lean leader effectively links one's own goals with the goals of the group, removes barriers to enable teamwork, and identifies strongly with the team. It is all about the people, since that is what leaders lead. A combination of flexibility, a strong sense of purpose and the ability to work through people will enable the leader's vision.

S is for Self-knowledge. Self-knowledge is an important category of learning. Before leader takes control of the organization and leads the team effectively, he needs to get knowledge. Knowledge by itself will not transform or lead to anything, unless it is properly directed and focused by the prism of effective leadership. The ability to learn constantly and to accept challenges is the mark of a true Lean leader.

A leader who possesses these seven essential qualities will guide his organization and his employees towards profits. Of the hundreds of leadership development models that exist, the Five Practices of Exemplary Leadership stands out as a proven approach to shaping organizational cultures aligned with the guiding principles of Lean management. This model is used by over three million people in thousands of organizations around the globe for developing individual leadership abilities and building effective teams (Integrus Performance Advisors, 2013, pp. 7):

- Model the way. Leaders live their values and lead with respect by establishing principles concerning the way people should be treated.. They create standards of excellence and set an example for others to follow. They unravel bureaucracy when it impedes action, and they create opportunities for victory.
- Inspire a shared vision. Leaders believe they can make a difference. They envision the future, creating an ideal and unique image of what the organization can become. Leaders enlist others in their dreams. They breathe life into their visions and get people to see exciting possibilities for the future.
- Challenge the process. Leaders search for opportunities to change the status quo. They use Lean thinking to look for innovative ways to improve the organization. They experiment, take risks, and accept mistakes as learning opportunities.
- Enable others to act. Leaders foster collaboration. They actively involve others, and strive to create an atmosphere of trust and respect. They strengthen others, making each person feel capable and powerful.
- Encourage the heart. Accomplishing extraordinary things in is hard work. To keep hope and determination alive, leaders recognize contributions that individuals make. In every winning team, the members need to share in the rewards of their efforts, so leaders celebrate accomplishments. They make people feel like heroes.

## ***LEAN LEADERSHIP IMPLEMENTATION***

Lean is more than just a kit of tools to improve the flow and quality; it is a business philosophy, which mainly refers to the appropriate leadership style and commitment of all management levels. The only way that Lean becomes a philosophy, rather than a tools-based improvement program, is for Lean leaders at all levels to encourage commitment throughout the whole organization to achieve the goals. By creating a philosophy of Lean leadership, more and more organizations are able to identify problems quicker, design solutions accurately and implement them at a rapid pace.

Successful Lean implementations require Lean leaders. Although many leadership teams know what Lean is, most do not know how to coach, guide, and sustain it. To transform into a Lean organization, an enterprise needs three types of leaders (Womack, Jones, 1996):

- someone who is committed to the business in a long run and can be the anchor who will provide stability and continuity - an experienced worker with long history in the company
- someone with deep knowledge about Lean techniques - Lean specialist
- someone who can be the champion/leader and fight against the organizational barriers arose as a result of the dramatic change in the organizational operations.

While the basic principles of Lean are the same in any organization, each implementation is unique. Different organizational factors such as human resource practices, management style, organizational strategic vision, organizational culture, external partnerships have importance in the Lean implementation process. Among numerous variables, management support plays an important role. Top management should not only demonstrate commitment and leadership, but it must also work to create interest in the implementation and communicate the change to everyone within the organization. Lean initiatives are likely to fail, without committing leadership who understands Lean principles, and believes it will deliver benefits to an enterprise. Lacking an implementation plan is also an important reason for Lean implementation failures. Therefore, an imperative task of leaders is to come up with a Lean implementation plan with clarity and purpose.

Lean leaders must understand the work in detail and know how to involve employees. If the top of the organization is not driving the Lean transformation, it will not happen. Therefore, enterprises struggling with implementing Lean, should analyze their leadership styles. They need to search for transformational leaders or to train their leaders to become transformational, because transformational leaders are most successful in implementing Lean practices. The dramatic transformation from traditional to Lean requires transformational leadership at all levels, from office to shop floor, to the executive suite, if the metamorphosis is to survive in the market.

Lean leadership helps in reducing costs and increasing the level of trust based on relationships with customers and employees. Employee involvement is one of the essential elements of a Lean implementation effort. When employees feel involved, they are more susceptible to changing their behavior. Leaders must realize their importance and agree that employee empowerment and involvement in Lean implantation is a crucial factor for business success. Seeing employees as capable and valuable for the organization is required if leaders want them actively participating in Lean implementation. Employees will only contribute to the Lean goals if believing these goals are aligned with their own individual interests. If some people have unfulfilled needs for self-expression and personal achievement, they would not be motivated to participate in Lean implementation programs. Obviously, personal needs can have a large impact over the attitude and behavior of employees towards Lean improvement activities.

It is often considered that an effective Lean leadership style involves coaching and leadership behavior that fosters participation and employee empowerment within certain boundaries. These are the responsibilities of the leaders and managers in Lean organizations. Study (Tracey, Flinchbaugh, 2006, pp. 50) surveying 226 managers and employees, indicated that five key variables that predict successful Lean transformation are:

- development of teams as a supporting structure of Lean
- calculation and communication of metrics
- communication among organization members, particularly across organizational barriers
- communication to employees regarding their specific role in Lean transformations
- acknowledgement and celebration of successes toward Lean transformation.

A successful Lean implementation requires dramatic changes at all organizational levels and departments involving work organization and culture. If the company wants to change the culture, it must develop true Lean leaders who can reinforce and lead the cultural change. The best way to do this, is through actions to improve the company's core value streams, supported by committed leaders who reinforce culture change (Liker, 2004, pp. 305). Culture is both a result and enabler for sustainable and successful Lean operations. It is a role model, which guides the employees through the organizational change towards the values of Lean thinking. Changes of mindset give people an aim in their working life, and have the potential to change attitudes, so that the employees begin to think differently, and are more willing to contribute to company's improvement initiatives. Motivation and creating a working environment that allows employees to develop their abilities, is the key for achieving the best condition for implementing Lean. The transition from decision making to being a coach for the employees is the lesson that enterprises need to master in their attempt to adopt the Lean approach.

For many leaders is surprisingly difficult to implement a Lean system. The leader's focus should be on teamwork in sharing values of Lean principles. The

core values of Lean enterprise should be known and lived with both, employees and leaders, in order to improvement culture be successful. In this regard, Lean leaders should be a role model for their team members. Leaders also need to praise team members for a job well done, and show appreciation for people's contributions. They should listen to diverse points of view, empower people to act, and support the decisions others make. Besides developing their team members, Lean leaders need to communicate their targets. Communication of Lean results involves the people and keeps them motivated. Leaders talk about the big picture which company wants to accomplish, and inspire others to share that vision. In essence, Lean leaders influence their followers by words or actions.

As stated above, one of the key challenges faced by enterprises in Lean implementation appeared to be the communication of the vision and values of Lean thinking to all employees. Lean leaders recognize that communication is a two-way process, encourage a diversity of opinions and see errors as opportunities for learning. When investigating problems, Lean leaders tackle the process, not the people. They lead effective root cause analysis and foster a deep understanding of the problems. Lean leaders deem that it is acceptable to make mistakes as long as employees learn from those mistakes. They recognize individual and team efforts and achievements and use integrity, knowledge, openness and honesty as guide in leadership practice. Finally, the primary task of managers and leaders in implementation of Lean leadership is increasing the improvement capability of people. That has to be made in way that enterprises develop people's knowledge and qualifications.

## ***LEAN LEADERSHIP I KNOWLEDGE MANAGEMENT***

Davenport and Prusak define knowledge as a fluid mixture of framed experience, values, contextual information, and expert insight that provides a framework for evaluating and incorporating new experiences and information. It originates and is applied in the minds of knowers (1998, pp. 5). Communication is the main method for sharing knowledge and making people understand, which is included as one of the essential factors of Lean. For structuring and organizing the knowledge of employees, it is important to implement knowledge management. Knowledge management is all about continuously creating new knowledge, disseminating it widely through the enterprise, and embodying it quickly in new products, services, technologies and systems. Therefore, knowledge management is a process that creates, disseminates and embodies knowledge.

The role of leaders in success of knowledge management implementation is very important, if not crucial. Lean leadership acts together with knowledge management initiatives to ensure that employees' knowledge can be transmitted to others. Lean leaders think horizontally, in the direction that value flows through the organization, and create strong horizontal focus by assigning a responsible person to manage product flows. At the same time, they create strong functions that focus

on knowledge capture and career paths. Knowledge management raises the level of operation with the help of Lean philosophy. While Lean emphasizes teamwork, eliminates waste, optimizes values and minimizes the time flow, knowledge management suggests all this through the organization and presentation of knowledge in a way that recognizes that it is possible to learn without repeating mistakes from the past. Knowledge management helps the organization to understand what intellectual potential it possesses, and Lean leadership to use this potential most effectively. The main advantage of applying knowledge management in Lean is the reduction of time, reduction of losses, increase in output and initiating innovations based on the experience and knowledge.

Lean advocates the importance of leader, but claims that a leaders' most important duty is to teach others. Training, teaching and educating are essential for every organization that wants to become Lean. In a Lean environment, training is pivotal in order to develop a workforce, which is capable of shouldering the increased responsibilities, to develop multi-skilled workers, and to create an environment in which workers have the skills and ability to push for continuous improvement (Puvanasvaran et al., 2009, pp. 132). Being an effective leader requires a willingness to learn. The goal of learning is to provide positive impact and outcomes, as a result of effective adaptation to environmental changes and improved efficiency in the learning process. Adaptation includes appropriate actions in response to technological changes and learning from other organizations achieved the best practices in the industry. Organizational culture facilitates the integration of individual learning by influencing the organizations' ability to learn, share information and make decisions. In a traditional hierarchical organization, position establishes authority to make decisions, but in a Lean organization, position only establishes responsibility to get decisions made. The leaders need to be fully committed to Lean implementation, to view the problems that enterprise faces as opportunities, and to turn every challenge into a learning experience.

Leaders within the organization must know and understand how to work and live the Lean philosophy and teach it to others. Lean leaders do not bring solutions to organizational problems, just the opposite; leaders give employees a challenge and an opportunity to learn by making small-scale mistakes along the way. Experienced and knowledgeable leaders lead and mentor, but also empower employees to solve problems by themselves. Lean leadership provides the templates and practices that enable leaders to learn, and then look for, ask about, and reinforce the leadership behaviors that sustain the gains. Lean leaders thoroughly understand the everyday operative work, live the enterprise philosophy, and teach it to employees. Leader's willingness to seek input, listen carefully and learn continuously creates an environment where employees feel respected and motivated.

Lean leadership has evolved as a concept over time. The interest in continuous improvement led on to the occurrence of a learning organization. A learning organization is one that actively seeks to acquire knowledge and changes behavior because of the newly acquired knowledge. Likewise, organizational learning is a process of improving actions through better knowledge and understanding, where

experimenting, learning new things and reflecting on new knowledge are the norms. A learning organization is involving the opportunity of developing knowledge about employees, suppliers, customers, and competitors. To convert an organization into a Lean learning organization, the right combination of a long-term philosophy, processes, people, and problem solving is needed (Liker, 2004, pp. 3).

The organization must develop a learning culture, which should never stop (Liker, Meirer, 2007, pp. 288). The culture of continuous learning is a great benefit for Lean enterprises that opens a new potential for future improvements and, in this way, achieving sustainability in a long run. It is obviously that leaders must create a learning culture and be well connected to the external environment, in order to learn continuously. In learning organization, people continually expand their capacity to create results they truly desire. The new and expansive patterns of thinking are nurtured, the collective aspiration is set free, and people are continually learning how to work together. Enterprises need to build improvement experts and group leaders who believe in Lean philosophy and have the desire to spread it throughout the organization over time, to transform into a real Lean learning organization. This involves allowing leaders to observe the work directly, so they can learn from the processes themselves. Once a leader understands the work, it becomes easier for him to teach it to others. Thus, the organization has the opportunity to learn more about itself and continually improve. Essentially, the true Lean leadership is about fostering a continuous learning environment for their team members.

## ***CONCLUSION***

Lean is a process-focused management concept that seeks to increase customer's value by reducing waste and continuously improving processes. This is accomplished through a Lean leadership, as the key success factor for the Lean implementation and the missing link between theoretical solutions and its application in practice. In this regard, this paper suggested that enterprises implementing Lean should focus their efforts and resources on finding the appropriate leadership style and behaviors, as a precondition for successful business operations and achieving operational excellence.

Lean leaders must possess the general characteristics and skills of effective leaders, such as creating a vision, knowing what drives the people they lead, active listening, empathetic questioning, helping people to satisfy their needs, etc. Besides, seven essential qualities of a Lean leader can be described using the PROFITS acronym as Perspective, Responsibility, Openness, Flexibility, Inertia, Teamwork and Self-knowledge. Lean leader's role is to create the long-term goals and shape an organizational culture, to learn and teach continuously on a road to continuous improvement. Lean leaders must learn and practice the power of understanding the human aspect of Lean and the significance of employees' engagement. Lean leadership is actually encouraging, supporting and demanding employee involvement. The true Lean leaders nurture the growth of their employees, bring out their best and inspire support for the organizational goals. Motivation and creating a working environment that allows employees to develop their abilities, is the key for business success of Lean enterprises.

The five principles of Lean leadership, namely improvement culture, self-development, qualification of employees, Gemba and Hoshin Kanri, describe the cooperation of employees and leaders in their mutual striving for perfection. Instead of direct leadership, the Lean leader supports and helps employees to learn and lead themselves. He is a developer of people and teams and has the exceptional relationship-building skills, focusing on building the trust.

Finally, Lean advocates the importance of leader, but claims that a leaders' most important duty is to teach others. Lean leadership acts together with knowledge management initiatives to ensure that employees' knowledge can be transmitted to others. The true Lean leadership is about fostering a continuous learning environment for their employees. Thus, the great Lean leaders are at the same time the great Lean educators.

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## **THE RESEARCH OF THE ECONOMIC EFFECTS OF STANDARDIZATION**

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### **ABSTRACT**

*Standardization usually represents the way of finding the middle between similar or opposing ideas and their merging into one overall idea. It is a specific instrument for the techno-economic self-regulation of business entities. It applies equally to all participants in the national, regional or global economy, and as such serves the creation of a "public good", embodied in documents called standards. Standards are specific "technical language" that meets a number of important functions, such as: enabling interoperability and compatibility; providing a minimum level of product quality; reduction of diversity; impetus to innovation development and technology exchange; providing information, as well as overcoming cultural and language barriers. Standardization and standards from an economic point of view can produce externalities, or unexpected external (positive or negative) economic effects to a third party. From the standpoint of positive effects, it is of interest to explore the assessment of the economic effects and the impact which standardization and standards have on the microeconomic level (the business system level), as well as the macroeconomic level (the national, regional and global level). Therefore, in this paper we focus on a methodology for assessing the economic effects of standards on a micro level which is based on an analytical approach of the value chain as well as at the macro level which is based on the production and economic function. In conclusion, it is stated how the policies in the development of standardization and standards adoption can contribute to the prosperity at the national level.*

**Key words:** *Standardization, Economy, Externalities, Methodology, Impact*

**JEL Classification:** *A12*

**UDK:** *006:33*

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## ***INTRODUCTION***

Standardization usually represents the way of finding the middle between similar or opposing ideas and their merging into one overall idea.

Standardization can be defined as “an activity for establishing terms for a general and repeated use in regards to real or potential problems, in the aim of achieving an optimal level of planning within a given context” (Popović, Živković, 2011).

Standardization is the process of establishing and applying certain regulations in the aim of coordinating and regulating activities in a given area, to the benefit and with the participation of all interested parties, and especially in the aim of realizing overall optimal savings, taking into consideration the functional aim and the technical security demands (the definition of ISO).

Standardization aims, as a rule, are one of the components of state politics and include improvement and development in the area of product and service quality, as well as rationalization of production and consumption.

Standardization can be understood as a specific instrument for techno-economic self-regulation of business activities of companies, and it relates to all the participants in the national, regional, that is, global economy, and as such serves to create a “public good”, embodied in documents called standards.

A standard is a “publicly accessible document, established by consensus and brought by an acknowledged body, which, for a general and repeated use, determines the regulations, demands, features, directions, recommendations or guidelines for activities or their results, in the purpose of achieving an optimal level of organization in a certain area in regards to the existing or likely problems” (ZOS, 2009).

Standards mainly have a positive impact on most aspects of our lives, as they secure the required characteristics of products and services. When products and services are in accordance with our needs and expectations, this is something that is implied and we are unaware of the significance and role of standards. However, if standards ceased to exist, very quickly we would become aware of the deficiencies. From the aspect of the contemporary consumer, products and services would be of a bad quality, inadequate for our needs, and incompatible with the equipment we already possess, or merely unreliable and hazardous.

Standards occur and develop as a result of accomplishments in science and technology, as well as based on experience and good business practice in all areas. By using standards in production and services, the efficiency and effectiveness of all processes are increased, as well as the quality of services, and thus at the same time the needs of the users of products and services are met and this in turn contributes to the raising of the general level of satisfaction.

Standardization as a rule starts and ends on the market, and the process takes place in two different ways: market exclusion (where only one technology survives in the market) and joint modification (where multiple technologies survive).

The diffusion of the current technologies, as well as the rapid emergence of new ones, create a space for profit increase but also raises the degree of technological uncertainty. Their combining reinforces market forces in the founding of the standardization process, which also increases the benefits of standardization (Cowan, 1991).

Thus, it is without doubt that standards and product standardizing produces have positive external effects, as the beneficiaries of their being introducing are, along with directly interested parties (such as proposers of standards, policy creators and other interested users), other factors of the economy as well. Such effects in economy are known as externalities.

Externalities (or overflowing effects) according to Samuelson and Nordhaus (Samuelson, Nordhaus, 2000) appear when companies or individuals impose benefits or expenses on other factors outside the market.

In the aim of a closer determining of externalities ensuing from a direct or indirect impact of standards on the economy, numerous research has been conducted which endeavoured to identify externalities – positive or negative influences of standards on economic effects. Here you can emphasize scientific papers (Swann, 2007, 2009, 2010).

## ***METHODOLOGY FOR ESTABLISHING THE ECONOMIC EFFECTS OF STANDARDIZATION***

### ***METHODOLOGY FOR ESTABLISHING THE ECONOMIC EFFECTS OF THE IMPACT OF STANDARDS ON THE MICRO LEVEL***

In the aim of determining the economic effects on the micro level, that is, on the level of an individual company which have ensued as a result of standard effect, a methodology under the following name was developed: ISO Methodology to assess the economic benefits of standards.

ISO Methodology secures a consistent framework of criteria, guidelines and instruments for assessing economic benefits (externalities) of standards from the perspective of individual organizations which are mainly companies (for example, profit organizations), but it can also be applied on the analysis of externalities in other types of organizations as well (for example, those the public sector).

The further text gives a short review of the key elements of methodology and concepts on the steps which are applied in the process of assessing and the methods for calculating externalities – the benefits from standards.

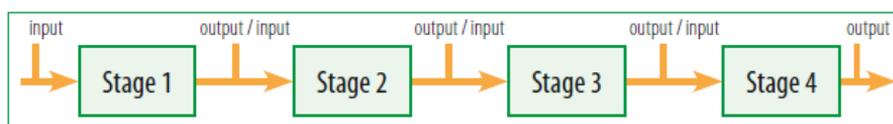
ISO methodology helps to systematically assess the economic benefits from standards, that is:

- to enable the participants from the private and public sectors to successfully assess the economic and social impact of standards which are based on voluntariness and consensus,
- to promote the awareness of the policy creators and business leaders of the significance of standards and standardization.

The methodology focuses the issue of economic contribution in creating corporative values due to bringing and applying standards. It includes international standards, regional and national standards, as well as standards developed by other organizations for developing standards, as well as the standards brought by consortia if they are open for the participation of interested parties, while internal (closed) standards of the company are excluded from this assessment.

The basic analytic approach of the methodology for determining the economic benefit of standards on a micro level makes up a value chain.

A value chain consists of stages (stages 1, 2, 3...), which represent a series of activities and which relate to creating a certain output in the form of products or services (Figure 1). In each stage, the output from appropriate activities adds a certain value. Stages can be organized within a company (then it is called “a company value chain”) or they can be spread across different companies which cooperate with each other, in a network supply chain (called a “supply chain” or an “industry value chain”).

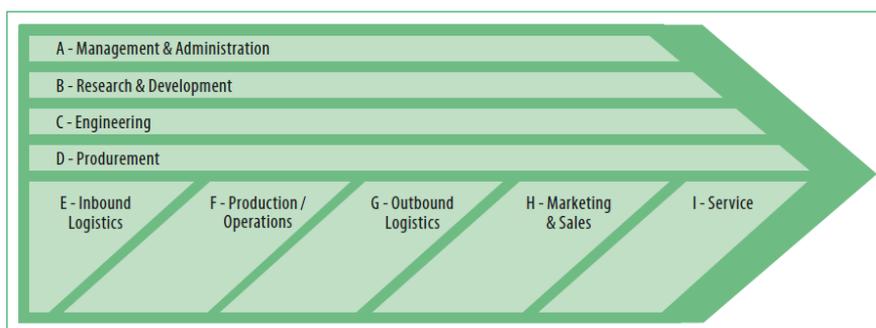


*Figure 1: A simple value chain*  
*Source: ISO, 2013,1, pp. 14*

The value line of a company represents a logical series of activities which are carried out within a company in the aim of realizing a product or service. The activities of a company are divided into a larger number of key business functions (Figure 2), while a total of nine key business functions from A to I were identified. Each of these functions is linked with a set of specific activities of value chains. For example, the activities which relate to the production of components and assembling final products are undertaken within the business function of “Production/Operations”.

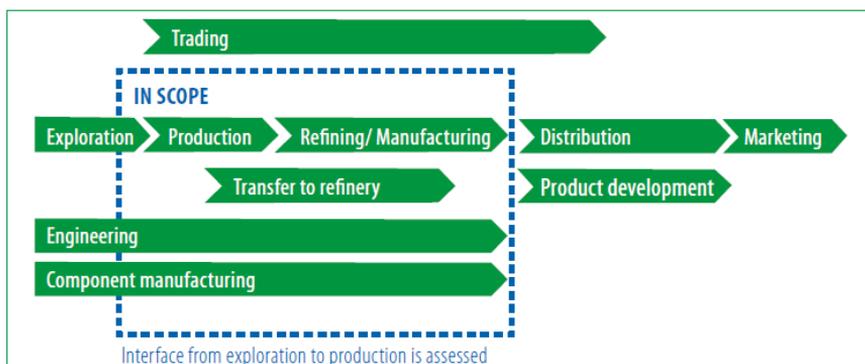
The business functions from E to I are called primary functions, while business functions from A to D are called auxiliary functions. In principle, all products which a company realizes are carried out through basic business functions. Some of these functions can be very complex, when they consist of several stages, while others can be simple, when they consist of only one activity. Auxiliary functions

impact primary functions and help their execution. The value chain of a company shown in Image 4 is generic, and it is realized from the company production model. The value chain model can also be applied to other types of organizations (for example, service companies or social institutions), but in that case adapting may be necessary in order to reflect its specific type of activity in the right way.



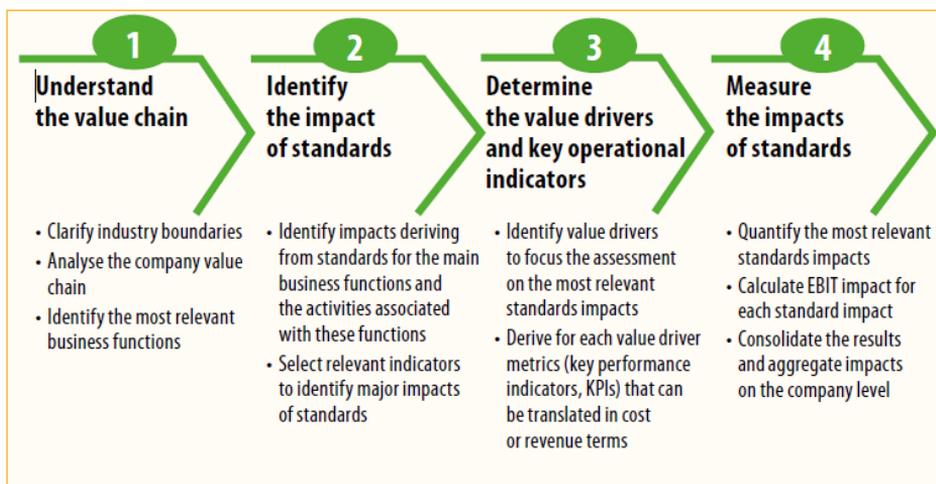
*Figure 2: Value chain of a (production) company*  
*Source: ISO, 2013,1, pp. 15*

The mentioned access to company value chains can be applied to an individual company, but it can also be expanded to the industrial sector (backwards or forwards in relation to the observed company), in which case the supplier as well as the buyer network of the company is included. This is called the “value chain of industry”. Figure 3 shows the application of the industry value chain on the example of engineering for oil and gas production.



*Figure 3: Industrial value chain on the example of the oil and gas industries*  
*Source: ISO, 2013,1, pp. 16*

An assessment of externalities – the economic effects are carried out in accordance with the steps which are mentioned in the further text, as shown in Figure 4.



*Figure 4: Key steps in assessment of standard impact*

*Source: ISO, 2013,1, pp. 23*

#### Step 1: Understanding a value chain

The first step is to determine the value chain in an industry and locate the company within the context of that value chain. The value chain of a company should be understood in the sense of its key business processes which create an additional value. A decision of key significance concerns the assessment of the scale of the encompassed activity, that is, whether the assessment should cover the entire company or it should be limited to one or more of certain business functions, considering that this causes a certain adapting of the analysis. The decision regarding the scale of encompassed activities depends on several factors, of which the most significant are the following: the size and complexity of the company, the available resources for project assessment, access to key information, as well as the experience of the project team members of the assessment.

#### Step 2: Identifying the standard impact

This step consists of determining those business functions (activities) in a company's value chain in which standards have a significant role. Here there is an intensive use of the existing documentation of the company in order to comprehend the processes, business functions and the main activities included in every business function. This step includes the consultation with company experts to determine which standards (or groups of standards) are applied in the activities within the chosen business functions. For an assessment of the impact, the so-called Standards Impact Map is used (Figure 5), which identifies those areas in the value chain where standards can carry out a significant role, and where the impact ensues from the standards. The map shows the impacts on the main business functions in the chain and linked activities.

Functions	Activities	Impacts	Description
Inbound logistics	All activities	Better internal information transfer	Using standardized documents and specifications makes passing on internal information about products and services more efficient.
		Better training of personnel	Inbound Logistics staff can be trained better because relevant specifications for both products and services are standardized.
		More efficient logistics	Inbound Logistics can be conducted more efficiently due to the reduced number of types of supplies.
	In-house logistics	More efficient receiving of supplies	Standardized documentation, packaging, labels or tags of supplies makes receiving more efficient.
Production / Operations	All activities	Better internal information transfer	Using standardized documents and specifications makes passing on internal information about products and services more efficient.
		Better training of personnel	Production/Operations staff can be trained better because relevant specifications are standardized, for both products and services.
		More efficient processing	Due to the reduced number of types of non-standardized products, Production/ Operations can become more efficient.
	Processing	More efficient assembly	Assembly processes are more efficient due to the modular product architecture.
		Better quality of equipment and supplies	Higher quality of equipment and supplies based on standards reduces the failure rate and related costs.
	Quality assurance	Better quality management	Quality management based on standards can be implemented more effectively.
	HSE (health, safety and environment)	Reduced disadvantages from regulations	Influence in standard-setting process helps to reduce disadvantages from regulations.
Better health/safety/environmental compliance		HSE management based on standards can be implemented more effectively.	
Outbound logistics	All activities	Better internal information transfer	Using standardized documents and specifications makes passing on internal information about products and services more efficient.
		Better training of personnel	Outbound logistics staff can be trained better because relevant specifications for both products and services are standardized.
		More efficient logistics	Reducing the number of product types means that Outbound Logistics can be conducted more efficiently.
Marketing and Sales	Packing/shipping	More efficient packing and shipping	Standardized documentation, packaging and labels make packing and shipping goods more efficient.
	All activities	Better internal information transfer	Using standardized documents and specifications makes passing on internal information about products and services more efficient.
		Better training of personnel	Marketing & Sales staff can be trained better because relevant specifications for both products and services are standardized.
		More efficient marketing activities	Marketing & Sales activities can be conducted more efficiently if there are fewer product types.
	Market analysis, research	Better competitor information	Since competitor's products have standardized specifications, market research can be conducted more efficiently.
	Marketing activities, client	Better customer information	Communicating product and service specifications and requirements to potential customers is more efficient.
	Contracting	More efficient contractual agreements	Defined specifications of the company's products and customer requirements makes concluding contracts more efficient.

Figure 5: Map of standards impact, business activities and associated activities  
Source: ISO, 2013,3

For further explanation, Image 8, within the framework of the Standards Impact Map (Figure 5), gives an excerpt as an example of the standards impact only for one function (production/ operations).

Function	Activities	Impacts	Description
Production / Operations	All activities	Better internal information transfer	This section of the impact map contains more detailed description of each of the possible impacts
		Better training of personnel	
		More efficient processing	
	Processing	More efficient assembly	
		Better quality of equipment and supplies	
	Quality assurance	Better quality management	
	HSE (health, safety and environment)	Reduced disadvantages from regulations	
Better health /safety/ environmental compliance			

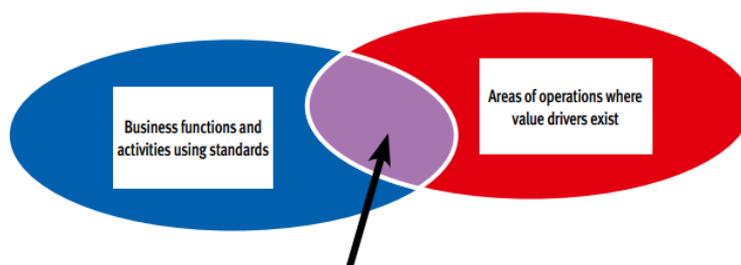
Figure 6: Excerpt from the Standards Impact Map for business functions – production/operations Source: ISO, 2013,2, pp.18

Step 3: Analysis of value drivers and establishing operational indicators

This step analyses company value drivers (that is, drivers of company competitiveness) and determine the operational indicators, which will then be applied to assess the standards impact.

Value drivers are key organizational possibilities which give the company a competitive advantage. If some business activities are tightly linked with value drivers, the impact of standards on creating values with this activity can be significantly larger than with activities which are not closely linked with value drivers. Thus, for assessing standards impact those activities which are linked with value drivers should be chosen.

For example, if one of the company value drivers is “low-cost production”, it is more likely that standards will be used in the production process which will directly contribute to that ability, and thus have a greater impact. Similarly, if another company value driver is at stake of an “innovative and superior product quality”, the standards used in engineering and R&D which contributes to realize this aim is more likely to have a bigger impact, and so on. In Image 9, the intersection presents the area where standards contribute to key activities and support value drivers (ISO, 2014).



*Figure 7: Intersection: standards generate larger benefits which support value drivers*

*Source: ISO, 2014, pp. 6*

The value driver map in Table 1 has been derived from several study cases. Table 1 gives the connection of business functions (activities) of the company with value drivers.

Table 1: Value driver map

Business functions	Value drivers
<b>Primary activities/Primary business functions</b>	
All	Focused value chain coverage
All	Continuous improvement
All	Efficiency
All	Safety compliance
All	Flexibility
All	Transparency
All	Economies of scale
All	Qualified workforce
All (mainly: Inbound logistics, outbound logistics)	Efficient logistics
All (mainly: Inbound logistics, Production, Marketing and Sales)	Quality of products
All (mainly: Procurement, Marketing & Sales)	Global reach
All (mainly: R&D, Engineering, Production)	Knowledge leadership
All (mainly: R&D, Procurement, Production etc.)	Partnerships
Marketing & Sales	Control over high-margin after-sales markets
Marketing & Sales	Sales effectiveness
Marketing & Sales	Reputation
Marketing & Sales	Client orientation
Marketing & Sales	Sales effectiveness
Marketing & Sales	Reputation
Production / Operations	Quality of production processes
Production / Operations	Efficiency of production
Production / Operations	Production capacity
After-Sales Service	Service quality
<b>Support activities/Support business functions</b>	
Management & Administration	<i>Ownership structure of the company</i>
R&D	R&D effectiveness
R&D, Production / Operations	Product innovation
Procurement	Partnership with suppliers
Procurement	Local access to key inputs
Procurement, Inbound Logistics, Production, Outbound Logistics	Pest and disease control

Source: ISO, 2013,4

Operational indicators are used in the aim of impact assessment which ensues from standards use, and in that sense one or more operational drivers should be identified. Operational indicators are quantifiable sizes linked with company activities which show an improvement or deterioration of performances (for example, time and costs, number of defects, waste, sale, satisfaction of buyers, etc.). The chosen operational indicators must be relevant, that is, they should cover the relevant aspects of activities within an analysis, for which the standard impacts can be observed and measured. Where it is possible, they should be linked with company value drivers. Thus, it is crucial to gather information regarding operational activities on a level nearest the location where the standards are actually used.

In a general sense, it is possible to make a difference between two extensive categories of operational indicators:

- Indicators which relate to business efficiency, Table 2;
- Indicators which relate to market development, Table 3.

*Table 2: Examples of operational indicators of business efficiency*

<b>Business function</b>	<b>Operational indicators</b>	<b>Impacts of standards</b>
Management & Administration	Legal compliance	Due to the use of standards, awareness has been built into management systems so that legal requirements can be easier traced
Research & Development	Manpower	Due to the use of standards, the amount of work needed to develop a new product has decreased. This means that the cost for design engineers (hours × average cost) was reduced
Inbound logistics	Non-conformant supplies	Due to the use of standards, specifications for supplies can be met by more suppliers leading to more competition: a) rejections and b) product failures. The value is calculated as a reduction of a certain cost over time
Production	Conformant products	Reduced failures result in higher quality output, less re-work and less warranty claims
All business functions	Accidents	Reduced number of accidents and consequent injuries, deaths

*Source: ISO, 2014, pp. 25*

*Table 3: Example of operational indicators of market development*

<b>Business function</b>	<b>Operational indicators</b>	<b>Impacts of standards</b>
Marketing & Sales	Sales	Due to the use of standards for new or modified products or improvements in production, the company increased sales revenues and profits
	Access to existing markets that are new to the company	By meeting certain requirements stated in standards (regulatory or market expectations), the company can access markets that were previously closed to it
	Creation of new markets	Using certain standards, the company developed markets for a new type of product for which it occupies a monopoly position for a certain time

*Source: ISO, 2014, page 26*

#### Step 4: Measuring of impact of standards

The purpose of the entire assessment process is the following:

1. Quantifying the impact of standards by applying operational indicators and aggregating their impact for each of the chosen business functions;
2. Converting the quantitative results which ensue from the use of standards for each of the chosen business functions, in financial statistics;
3. Summing up the data for all chosen business functions in a given moment, to establish the total contribution of standards in relation to the gross company profit or EBIT (Earnings Before Interest and Taxes).

The aim of this step of the assessment process is to determine the impact of using standards, which is measured through operational indicators – in a quantitative way. This is achieved in this final assessment stage by determining the impact of standards in the financial sense. It is the expectation that standards use leads to a change of values in the chosen indicators in such a way that the realized effect by the company is manifested through a contribution of cost decrease, through a contribution of income increase, or a combination of both.

Depending on the operational indicators, the financial impact can be directly measured, or it can be determined indirectly based on other company data. For example, “saving” for material procurement and components are an operational indicator measured directly in financial conditions. On the other hand, the reducing of “the labour force needed to complete product design” is an operational indicator which must be converted into assessed savings based on other company data, such as average prices of staff, project numbers, and so on. For assessing the changes in values expressed in financial statistics, the key indicator used is EBIT. EBIT is expressed as the gross company earnings, that is, the income minus the expenses (Figure 8).

If there are not enough data at disposal to calculate the effects, or the data are not considered reliable enough for such a calculation, the methodology also disposes with methods of approximation to fill in the gaps, which are based on data obtained from assessments of similar functions in other organizations.

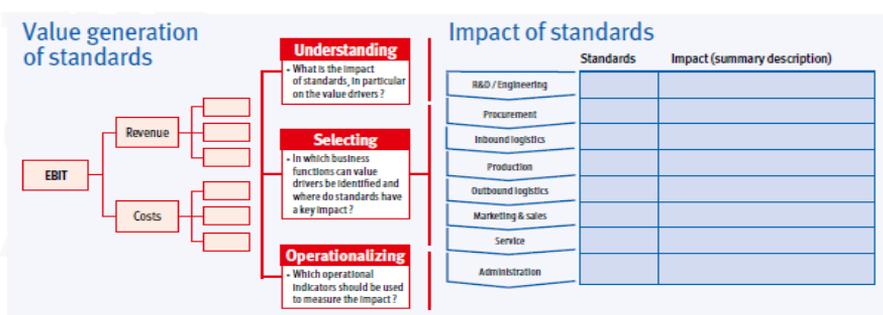


Figure 8: Impact of standards on company business functions and their calculating based on creating company values, expressed as EBIT contributions

Source: ISO, 2014, pp. 7

Along the value chain, that is, within the business functions in the company, various cases of standards impact can be assessed (Figure 9).

#### Model cases of the impact of standards

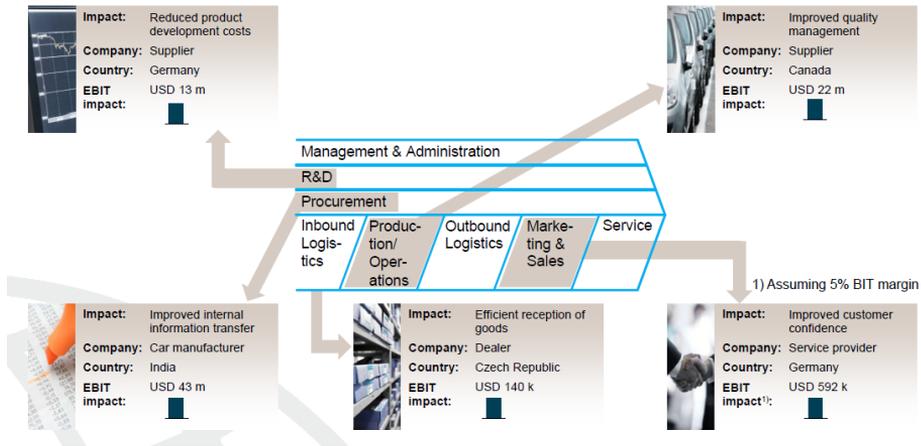


Figure 9: Outline of results – various cases of standards impact assessed along company value chains

Source: Gerundino D., Hilb M., 2010, pp. 22

The pilot projects for assessing and quantifying the effects which companies can realize from applying standards have been realized by ISO and its members in more than 20 countries. These projects have been carried out in close cooperation between ISO members, academic institutions, companies as well as staff in member-states, and case studies have been carried out in the period from October 2010 to June 2012. The choice of companies to realize the pilot projects have been made by ISO members in their countries. The only condition was that the company in the recent years was a standard user, and that the member had a good relationship with the company, in order to secure that the project teams have at their disposal key staff from the company for interviews and consultations. Table 4 presents industrial companies in which 21 international case studies were realized, according to the presented methodology (ISO, 2012).

*Table 4: Industries and countries covered by case studies*

Industries	Countries
Agri-food business	Cameroon, Peru
Chemical industry	Thailand
Construction & construction materials	Botswana, Indonesia, Italy, Lebanon, South Africa, Sri Lanka
Electrical appliances	Vietnam
Electrical power transmission	Germany
Food retail/food logistics	Singapore
Heating, ventilation, air conditioning	Jordan
Industrial automation equipment	Brazil
Information & telecommunication	Germany
Juice production	Egypt
Pipes and piping systems	China, Colombia, Mauritius
Shipbuilding	China
Water supply	Senegal Water supply

*Source: ISO, 2012, pp. 8*

### ***METHODOLOGY FOR ESTABLISHING ECONOMIC EFFECTS OF THE IMPACT OF STANDARDS ON A MACROECONOMIC LEVEL***

When it comes to reviewing standard externalities on a macroeconomic level, that is, the impact of standards on economic effects, then the issue of globalization becomes an unavoidable factor.

Globalization is a phenomenon of the modern age which is represented by the process of humankind converging in a distinctive common economic, political and cultural area, and which is featured by an increase of interaction, the growth of the number and variety of participants, as well as incessant changes.

Within the economic area, globalization has an impact on trade (exchange of goods and services), especially on global trade which is realized by way of national and regional borders, as it demands the harmonizing of national regulations which leads towards creating international regulations and conditions international standardization, which further results in producing international standards.

In that way, international standards facilitate economic, scientific and technical cooperation on a global level and become an effective instrument for regulating the market, for removing barriers for free trade, that is, liberating from routine tasks (Krstić et al., 2012).

Generally speaking, standards provide the necessary help in communication between economy, technology, science and public services, which contributes to total economic growth.

The imperative for sustainable economic growth has produced numerous economic research of standards impact on a macroeconomic level, for a better understanding of its factors.

On a macroeconomic level, the role of standards is a multiple one and in a direct connection with the degree of productivity. Specifically speaking, standards impact the protection of the community, they facilitate international trade, improve the interoperability of technology and processes, and ease technological changes and economic development, by reducing the asymmetry of information.

From the standpoint of international standardization, the most important benefits from standardization are the following:

- Improvement in universal technical communication and mutual understanding;
- Facilitating international exchange of goods and services;
- Removing technical obstacles in trade;
- Innovations and transfer of technology.

The significance of technological activity, as a relevant determinant of economic effect in industrialized economies is mostly acknowledged today. It is without doubt also, that technical standards are very important for speeding up the diffusion of innovations, especially new technologies.

An increased economic efficiency, occurring as a consequence of implementing international standards, creates an economic benefit not just for the supply industry by increasing profit but also for the users by lowering the price of goods and services. Also, the application of international standards can reduce the risk and increase the quality of services. Thus, international standards are able to improve the economy and contribute to the benefit of society as a whole.

Standards produce externalities – different economic effects (positive and negative), which can be classified according to several foundations, as shown in Table 5.

Table 5: Categorizing standards based on economic effects

Type of standard	Positive effects	Negative effects
<b>Standard compatibility</b>	<ul style="list-style-type: none"> <li>• Network externalities</li> <li>• Avoiding lagging in old technologies</li> <li>• Increasing the variety of product system</li> <li>• Increasing the probability of interoperability</li> </ul>	<ul style="list-style-type: none"> <li>• Monopoly</li> </ul>
<b>Standards of minimum quality and security</b>	<ul style="list-style-type: none"> <li>• Correction of negative selection of supply quality</li> <li>• Reducing transaction costs</li> <li>• Correction of negative externalities</li> </ul>	<ul style="list-style-type: none"> <li>• Limiting of competition</li> </ul>
<b>Standards of reduced variety</b>	<ul style="list-style-type: none"> <li>• Economy of scale</li> <li>• Building of focus and critical mass</li> </ul>	<ul style="list-style-type: none"> <li>• Reducing choice</li> <li>• Market concentration</li> </ul>
<b>Information</b>	<ul style="list-style-type: none"> <li>• Facilitating trade</li> <li>• Reduced transaction costs</li> </ul>	<ul style="list-style-type: none"> <li>• Limiting of competition</li> </ul>

Source: ISO, 2012, p. 8.

The classification is based on compatibility, quality, reducing variability (unification) and information. Table 5 sums up these four different dimensions of standardization and stresses the positive and negative effects of each one:

- The compatibility of standards is of a key significance for the development of network industries such as the sector of Information-Communication Technologies (sector ICT), as they enable the interoperability between different users and the compatibility between the hardware and the software systems;
- Standards which specify the minimum of the needed quality and security limit the risk from production of goods and services of a poor quality, which in turn increases consumer trust;
- Standards for reducing variability eliminate an undesired variety in processes or product design;
- Standards which specify information and product description improve compatibility between products and variability between product types.

Having in mind the advantages of applying standards for the country as a whole, its quantitative impact for the development of international trade, economic growth and finally, realizing social aims can be reviewed. In that sense, and in the aim of analyzing the economic effects of standards on a macro plan, several studies have been carried out ((Blind, 2004), (Blind, 2011), (SA, 2012), (Miotti, 2009)).

In defining the methodology for determining the economic effects of standards on a macroeconomic level, the Cobb–Douglas production function is used.

Cobb–Douglas production function is a special form of function which is widely applied in economics to present the technological correlation between the values of two or more inputs, a specially engaged physical capital and invested labour as the amount of output which can be produced from these inputs (wiki, 2014).

The Cobb–Douglas production function in its standard form in the case of production of individual goods in whose realization only two factors participate (labour and capital), has the following form:

$$Y = AK^\alpha L^\beta \quad (1)$$

where: Y is the output – the total production (the real value of all goods produced in the year); L is the input – representing labour (the total number of work hours of those who worked during a year); K is the output – the representing capital (the real value of capital expressed through the value of machines, equipment and facilities); A is the multifactor, that is, the total productivity factor;  $\alpha$  and  $\beta$  are the coefficients of capital elasticity and labour, respectively, representing constant values which determine the available technology. The outputs of elasticity measure the responsiveness of the output during a change of levels of either labour or capital used together in the production function. For example, in the case of  $\alpha = 0.45$ , the growth in used capital of 1% would lead to an increase of the output by approximately 0.45%. If  $\alpha + \beta = 1$ , this involves the presumption of “ideal competition”, and  $\alpha$  and  $\beta$  can be considered sharers of capital and labour at the outlet. In this case, the production function has a constant income, which means that if used capital K is doubled, labour L with also double the output. If  $\alpha + \beta < 1$ , the production function has a decrease of value at the output, even if  $\alpha + \beta > 1$  - the production function has a value increase at the output.

The further text presents two examples of calculating the economic effects of the standards at a macro-economic level based on the Cobb–Douglas production function, but with basically have different models.

#### Example 1

In this example, and let us mark it as Model 1, for calculating of the economic effects of standards on a macroeconomic level (Haimowitz, 2007), which will here be looked at more closely, the Cobb–Douglas production function has the following form:

$$Q_t = A_t K_t^\alpha L_t^{1-\alpha} \quad (2)$$

The output for the realized value of production ( $Q_t$ ) is a non-linear function of production multifactors ( $A_t$ ), of basic capital ( $K_t$ ), and the amount of labour ( $L_t$ ). In this production function, input capital and labour are combined to produce an output. The ability of capital and labour to produce an output is increased by the level of technology and efficiency in the economy, which is represented by the productivity multifactor ( $A_t$ ).

If the left and right sides of the equation (2) are divided by  $L_t$  we get the following correlation:

$$\left[ \frac{Q_t}{L_t} \right] = [A_t] \left[ \left( \frac{K_t}{L_t} \right)^\alpha \right] \quad (3)$$

In this model, the correlation from the left side in fact represents labour productivity, or the realized worker output per hour, and it can be considered as if it ensues from two outputs, that is, it represents a combination of two contributions, as shown in the equation (4):

$$\left( \begin{array}{c} \text{Labour} \\ \text{Productivity} \end{array} \right) = \left( \begin{array}{c} \text{Contribution} \\ \text{of} \\ \text{Multifactor} \\ \text{Productivity} \end{array} \right) + \left( \begin{array}{c} \text{Contribution} \\ \text{of} \\ \text{Capital} \\ \text{Deepening} \end{array} \right) \quad (4)$$

Multifactor productivity is composed of two components: *knowledge and efficiency*. The factors which impact knowledge or technological capacities are standards, patents, activities or research and development (R&D), as well as the import of foreign technology. The factors which impact the level of efficiency in the economy are standards, improving the infrastructure and structural changes in the economy, such as the mobility of world labour between industries, and other. Thus, standards can potentially have an important role in strengthening multifactor productivity. The mentioned can be interpreted in the example of realization of railway transportation services. One railway train can realize a certain number of services (transporting goods, passengers, etc.) with 6 cars. However, 12 cars can realize a significantly larger number of services in comparison to 6 cars. Let us presume that at the beginning there were services rendered with one railway composition, one train engine and 6 cars. An addition of another 6 cars represents a significant capital increase. Thereby, standardization may indirectly secure that the mentioned increase of capital is transformed into an increase of output, due to the fact that if the rails of 6 newly added cars are incompatible with the previously used cars, the additional capital will not lead to an output increase.

In this study, the multifactor productivity multifactor is modelled as a function of time and the number of standards, and in that sense it is presumed that it has the following functional form:

$$A_t = \exp(\lambda T_t) \varepsilon (STA_t)^\varepsilon \quad (5)$$

where  $\exp$  is the Euler number  $e$ ;  $T_t$  - is the vector of the time trend,  $STA_t$  - the number of standards in year  $t$ . Additional variables, which in principle can be important in explaining multifactor productivity, are excluded from the analysis, due to a short time period for analysis.

If in relation (3) first the multifactor productivity ( $A_t$ ), is replaced by the relation (5), and then on the left and right sides of the equation the natural logarithm ( $\ln$ ) is applied, then an error is introduced ( $u_t$ ), as well as the  $\beta$  constant for defining the initial conditions, and the final functional form is obtained (6).

$$\ln\left(\frac{Q_t}{L_t}\right) = \beta + \alpha \ln\left(\frac{K_t}{L_t}\right) + \lambda T_t + \varepsilon \ln(STA_t) + u_t \quad (6)$$

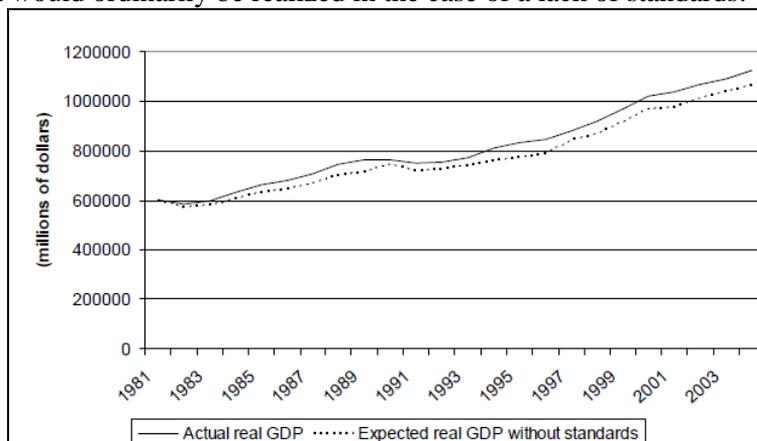
The equation (6) is used to estimate the economic effects of standards in the Canadian economy. The analysis involved the period from 1981 to 2004, during which the time trend vector ( $T_t$ ) included two deterministic periods in the Canadian economy which divided 1994 (before and after the entry into force of the North American Free Trade Agreement - NAFTA). The results of calculating the coefficient by equation (6) are presented in Table 5.

*Table 6: Estimation Results for Existing Number of Standards (in logarithms)*

Sample: 1981 to 2004				
Method: Least Squares				
Variable	Coefficient	Std. Error	T-Statistic	P-Value
Constant	-1.058	0.697	-1.516	0.1459
Log (Number of Standards)	0.356	0.070	5.070	0.0001
Log (Capital-to-Labour ratio)	0.550	0.069	7.984	0.0000
Trend 1	0.003	0.001	2.733	0.0132
Trend 2	0.023	0.002	13.369	0.0000
Adjusted R-squared:	0.976725			
Durbin-Watson statistic:	1.851447			
ADF test of the residual:	-4.3227			
P-value for ADF test:	0.0028			
Notes:				
a) Standards errors are White heteroskedasticity-consistent standard errors.				
b) The P-Value represents the degree of certainty with which we can reject the hypothesis that the variable has no impact on labour productivity.				
c) The ADF test of residual included a constant and lag lengths were chosen using the Schwartz Information Criteria.				

*Source: Haimowitz, 2007, pp. vi*

During the observed period in Canada, the number of standards grew per an average rate of 0.69 percent annually, which had as a consequence the increase of the growth rate of production (the real GDP) by around 9 percent. The implications of these findings point to an increase of the actual realized GDP in relation to the GDP which would ordinarily be realized in the case of a lack of standards.



*Figure 10: Actual Real GDP and Expected Real GDP Without Standards*  
*Source: Haimowitz, 2007, pp. viii*

### Example 2

Let us mark the example as Model 2 for calculating the economic effects of the standards on a macroeconomic level (Blind, 2004) which will be looked at closely here. Here too the starting point is the Cobb–Douglas production function, equation (1). If we add to the mentioned function a time dimension, the equation becomes:

$$Y_t = A K_t^\alpha L_t^\beta e^{\lambda t} \quad (7)$$

where:  $Y_t$  represents the output,  $K_t$  the capital factor,  $L_t$  the labour factor (the number of workers),  $\alpha, \beta$  the coefficients of elasticity which represent a partial participation of the capital and work force factors.  $A$  is here the efficiency parameter, and its change, while other parameters remain constant, leads to a uniform proportional change of the output for every factor combination. Usually, technological progress in the Cobb–Douglas production function is budgeted separately from the function itself and in a neutral form by a time-dependent equation, where  $t$  is the linear time trend, namely:

$$A_t = A * \exp(\lambda T_t) \quad (8)$$

When on the left and right side of the equation (7) a natural logarithm is applied, the production functions become the following:

$$y_t = a + \alpha k_t + \beta l_t + \lambda t \quad (9)$$

in which now the lower-case letters ( $y_t, k_t, l_t$ ) represent logarithm variables, while  $a$  is the constant which is being introduced to determine the initial conditions.

The weakness of this equation is determining the technological progress via a time-dependent equation, that is, a  $\lambda t$  member, which can be removed if it is replaced by suitable members, which more closely represent technological progress via R&D activities, in the specific case, by way of the number of patents  $pat_{t-3}$ , cost of licenses and patents  $lex_t$ , as the number of standards  $std_t$ . After the mentioned transaction and adding the member for an error the following equation is obtained:

$$y_t = a + \alpha k_t + \beta l_t + \gamma pat_{t-3} + \delta lex_t + \varepsilon std_t + u_t \quad (10)$$

in which the introduced members are calculated based on recursive formula (11) and (12):

$$pat_t^{end} = pat_{t-1}^{end} + pat(basic)_t^g - pat_t^c - pat_t^f \quad (11)$$

$$std_t^{end} = std_{t-1}^{end} - std_t^p - std_t^w \quad (12)$$

where:  $pat_t^{end}$  is the average number of patents at the end of the current year  $t$ ,  $pat_{t-1}^{end}$  number of patents at the end of the previous year,  $pat(basic)_t^g$  representing the number of grant patents,  $pat_t^c$  the number of revoked patents,  $pat_t^f$  representing the failed patents,  $std_t^{end}$  the number of standards at the end of the current year  $t$ ,  $std_t^p$  representing the number of newly printed standards,  $std_t^w$  representing the number of withdrawn standards.

If it is taken that  $\alpha=1+\beta$  equation (10) is simplified, after mathematical organizing, it has the final form:

$$y_t - l_t = a + \alpha(k_t - l_t) + \gamma pat_{t-3} + \delta lex_t + \varepsilon std_t + u_t \quad (13)$$

Based on empirical data from Germany and by using the presented equation (13) values presented in Table 6 were obtained. The results in the table have undoubtedly confirmed that the role of standardization is very important. Standards have a special responsibility for an effective diffusion of innovation, as their impact, calculated by years, amounts at an average from 0.2 to 1.5 percentage points from the average degree of annual growth (framed in the table). When comparing all three factors together (the number of patents, costs of licenses and patents, as well as numbers of standards), it is clear that standards are equally important for technical innovations as well as patents. Even though the innovative potential is not the only decisive factor which contributes to economic growth, it is a fact that must be widely disseminated via standards and technical rules.

*Table 7: Sources of growth in the business sector from 1961 to 1996*

Source	Average annual percentage changes							
	61-90	61-95	66-70	71-75	76-80	81-85	86-90	92-96
$k_t$	1.6	2.6	2.0	1.7	1.3	0.8	1.1	1.1
$l_t$	0.2	0.6	0.1	-0.6	0.5	-0.6	1.1	-0.7
$pat_{t-3}$	0.1	0.2	0.2	-0.4	0.3	0.2	0.0	-0.3
$lex_t$	0.5	0.6	0.5	0.4	0.2	0.1	1.3	0.6
$std_t$	0.9	1.5	1.2	0.9	1.1	0.4	0.2	0.3
Total:								
fitted	3.3	5.7	4.1	2.1	3.5	1.0	3.7	1.0
realized	3.3	5.2	4.4	1.7	3.6	1.1	3.8	1.5

*Notes:* Differences between the sums of the individual components of the growth rates and the fitted total growth rates are caused by rounding and by joint effects

*Source: Blind, 2004, pp. 317*

Viewed as a whole, all the national studies realized on this topic show that standards have a positive impact on the economic growth as a result of the improved diffusion of knowledge. The contribution of standards on the growth rate in each country is different: 0.9% in Germany, 0.8% in France and Australia, 0.3% in Great Britain and 0.2% in Canada. This also is indicated by the updated German study whose aim is to recalculate the economic benefit from standardization based on the current data (Table 8).

*Table 8: National studies on the impact of effects of standards on economic growth*

Country	Publisher	Timeframe	Degree of GDP growth	Standard contribution
Germany	DIN 2000	1960-1990	3.3%	0.9%
	DIN 2011	1992-2006	1.1%	0.8%
France	ANFOR 2009	1950-2005	3.4%	0.8%
Great Britain	DTI 2005	1948-2002	2.5%	0.3%
Canada	Standards Council of Canada 2007	1981-2004	2.7%	0.2
Australia	Standards Australia 2006	1962-2003	3.6%	0.8%

*Source: Blind, 2013, p. 18.*

## **DISCUSSION OF RESEARCH RESULTS**

In this study, we started from the following assumptions:

- Active participation in the standardization process and application of standards produces specific economic effects, both for those who apply them, as well as third parties, and these effects can be identified and quantified, both at the level of businesses (micro level), and also at national, regional and global level (macro level).
- Active use of standards contributes to the improvement of the operation of business entities, which consequently results in the enhancement of competitiveness at the national level.

Hereinafter some of the results of the conducted desk research of the economic effects of standardization are briefly presented. The results indicate the following:

1. Generally speaking, it seems that standards and standardization in our economic context have long been unjustly sidelined to the margins of agenda on key economic issues. The reason is probably to be found in the known adverse economic circumstances in which Serbia is in, and the standardization as the higher-order factor does not come on the agenda. Of course, this is not the case in the harmonization of general social standards in the process of approaching the EU, but when it comes to the application of standardization and standards in the business improvement, it certainly is the case.

2. Study results indicate that the standards produce economic effects at the macro economic level and that they can be quantified, which was clearly confirmed by the examples stated in the paper. Thus, in the abovementioned example of the economic effects of the macro-economic level, from equation (4), appears important conclusion that the standards were contained in both components of

multifactor productivity (knowledge and effectiveness). Relevant factors that affect the knowledge (and, consequently, the technological capacity) include patents, research and development (R & D), the import of foreign technology, and standards. Factors that affect the level of efficiency in the economy are infrastructure improvement and structural changes in the economy, labor mobility, as well as standards. In this way, standards are potential field for improving the multifactor productivity. National economy, which seeks to improve the economic environment, among other things, can achieved that through a proactive approach to standards. If this is interpreted in our conditions, it is clear that, among other things, the increasing application of standards can improve the competitiveness of the Serbian economy.

3. Experience of developed countries shows that national economies that innovate are more competitive and successful. Successful implementation of innovation assumes the effective diffusion of innovation. However, the effective diffusion of innovation requires a proactive standardization and application of standards, in other words, in the process of innovation diffusion - standards have a special role. Thus, the innovation potential of the economy is a necessary but not a sufficient condition, because an evident increase of the level of GDP growth (albeit unevenly) in most developed countries, is the contribution of standards (as shown in Table 8 presented in the paper). So, the conclusion is that the innovative potential has to be widely disseminated through standards. In this way, the standards represent a specific "catalyst" of the innovation process. In our terms this means the following: first we have to work on increasing the number of significant innovations (especially in industry) and along that to work on the intensification of the activities of standardization.

4. When it comes to determining the economic effects of standardization on the micro-economic level, the research results obtained confirmed that the standards produce economic effects and that they can be quantified, which was clearly confirmed by the examples listed in the paper. Case study analysis (presented in Table 8 of this paper) mentions a number of such case studies. However, the number of possible real case studies is nowhere near exhausted. In this sense it can be suggested that one such study, using the proposed research methodology, is implemented in Serbia, and by the interested business entity and the Institute for standardization. This would indicate what the economic effects can be achieved by applying the standard in our country.

5. The contribution of this research can be reflected in further promotion of implementation of standards and standardization. From the wider context of research, it is found that business entities generally do not give proper attention to the standardization, and it is widely believed that it is a matter for the Institute for standardization of Serbia. However, we often ignore the fact that participating in company standardization processes enables, among other things, networking with partners, users, deliverers, competitors, regulatory organs and bodies for coordination assessment, as well as a direct approach to the knowledge and strategy (tactics) of other participants in that process. Along with this, active participation in this process enables companies not only to directly present their

interests, but also to have an effective impact on the contents (demands) and form of standards and similar documents which are a result of this process (Krstić, Krstić, 2010).

6. This paper presents a methodology for determining the economic effects on macro- and micro-economic level, so selected literature in this paper can serve as a useful bibliography on this topic.

7. This paper may contribute to raise awareness of decision makers at the macro economic level as well as management of business entities in the micro-economic level in the field of further affirmation of standardization and standardization in our context.

## ***CONCLUSION***

Applying standards increases the effectiveness and efficiency of the process of product realization and raises its quality, which meets the demands of the product users and which in turn contributes to the increasing of the level of their satisfaction.

The relevant aspects of applying standards are reducing the variety of products, as well as quality and performances, measuring of standards, compatibility and interoperability, health and security, environment protection, codified knowledge and vision.

This paper reviews the issue of economic effects of standards and standardization on a micro and macroeconomic level. Research has shown that numerous studies have dealt with this issue and they have unambiguously confirmed the assumption that the application of standards and carrying out standardization contributes to externalities – economic effects, as along with the direct interested parties (such as proposers of standards, policy creators and other interested users), other factors of the economic systems also benefit indirectly from their introducing.

The economic effects of standard impact can be positive and negative. Of course, the focus here is on the positive effects.

In regarding the microeconomic level, that is, the level of the business system, positive effects can be expressed by way of direct variable factors (economy of scale, labour division, competencies, barriers for market entry, network effects, transaction costs, precision, trust and risk), as well as via variables which are of direct interest for politics (productivity, inputs, competition, innovations, trade, the object of outsourcing, and market failure). These effects are assessed on the principle of value chains by way of four steps.

As concerns the macroeconomic level, the positive effects of applying formal standards are usually expressed in a percentage from the gross domestic product – GDP, and are variable depending on the industrial branch. Empirical research has indicated that in developed countries (those which apply intense standardization

and standards) that percentage is an average 1% of the GDP. The economic effects of the standards impact in this case is determined by an appropriate modification of the Cobb–Douglas production function.

Considering that the previous research of the economic effects of standards excluded the areas of informal standards (standardization activities which are carried out by industrial consortia), as well as the economic effects of standard impact in the area of the services sector, this could be the area of future research.

Thus, not only do standards contribute to introducing order in the given context, they are also a means which help to speed up the diffusion of innovations, which in turn has a positive reflection on competitiveness. Analysis has shown that the higher a level of development of a country, especially technological development, the more it uses standards and standardization, which has a synergic effect.

The positive macroeconomic effects of applying standards significantly override the sum of individual benefits of particular business systems and have a wider significance for the economy, which justifies standardization in its entirety.

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## **COMPANIES RESTRUCTURING - MYTHS AND MISCONCEPTIONS**

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### **ABSTRACT**

*In the last 30-40 years numerous companies in the world passed through the various forms of restructuring. In the EU each month is registered 90-100 restructuring of large companies. In Serbia, the restructuring process is quite muted. EBRD in 2013. evaluate the situation in this area with modest 2 + and no progress for several years. The aim of this paper is to show how to implement the restructuring process, as it usually involves the loss of jobs and large investments. Some companies made a change in the legal form of joint-stock company and began the process of corporatization. The most common problems in enterprise restructuring are huge budget allocations, frequent protests of workers, lack of interest of potential investors. The restructuring process carries a dilemma whether restructuring is "makeup" and how to attract investors? In the restructuring process of public enterprises were achieved modest results. Some of them carried out a process of organizational restructuring, and some companies made a change in the legal form of joint stock companies and started a question of redundancy. The output is increasingly seeking out through in advanced prepared programs of reorganization that are a wish list or realistic plan of action.*

**Key words:** *Restructuring, Enterprise, Investment, Economic Development*

**JEL Classification:** *G34*

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## ***INTRODUCTION***

The restructuring is the company reorganization, which aims to achieve greater efficiency and to adapt to new market and business conditions. Restructuring of the company resorts to when there are problems with the debt servicing which threatened its collapse. It can be said that the restructuring process is an attempt to achieve a turnaround in the business. Turnaround in business must include more than the debt restructuring and capital structure. If a company is exposed to such problems where restructuring is considered as best solution, it is difficult to say that the management that led the company in this not-so-enviable position, will be able to take him out of it. The company, which is in the restructuring process, needs external assistance. Help can be in the form of a new management that has experience in creating and managing changes or consultants who will transfer knowledge and focus the existing management on the way of changes or even both of them in combination. A consultant assists company in creating a unique and sustainable competitive advantage in the market which is based on a successful business, inside and outside the company. Consultants establish cooperation with clients to identify opportunities for development and implementation of new and more effective strategy, business processes, knowledge and systems that create value for both the owners and the customers and employees.

The restructuring process involves analyzing and formulating new strategies for business transformation, enterprise evaluation and consideration of various financial alternatives that are available. The restructuring implementation involves tasks that should be fulfilled : an analysis of operational performance and dynamic turnover of funds ; stabilization operations and the elimination of the financial crisis ; financial obligations restructuring; strategies formulation including marketing and related plans ; business units rationalization, distribution channels and levels in the management structure ; development plan for turning operations and its execution ; analysis of available alternatives for financing and financial restructuring. Restructuring brings new opportunities and challenges. Some companies focus on survival, reduce costs and redundancies, and more successful look outside the economic framework to reach sustainable ways to improve the business and enter new markets. The time is right to explore all possibilities. However, in order to do so, first you must perform a thorough and effective evaluation of their own weaknesses, strengths and external opportunities considering several alternatives. You do not need to bypass problems such as low productivity and inefficient operating systems because they can be causes of business problems. In the restructuring process a new perspective must be based on the fast and sustainable change that will be of critical importance. All this means the diagnostic work on defining the strengths, weaknesses, external opportunities and threats compared to major competitors. ([www.poslovnastrategija.rs](http://www.poslovnastrategija.rs))

## ***RESTRUCTURING OF ENTERPRISES***

The restructuring involves the sale of public enterprises to the private sector and is associated with a privatization program of modern economy. In developed economies, privatization involves: the development of market structures, deregulation and increased activity of markets, greater capital market activities, sale of public enterprises to private capital and increasing the economic efficiency. Many governments are not satisfied with the economic efficiency of monopolized companies or branches, low motivation of managers in public enterprises, bureaucratization and politicization of enterprises, poor quality of products and services, high costs and prices. The economy restructuring should enable greater control, market discipline, efficient capital management and ensure the political and economic effects (Komazec, 1996, pp. 22-25).

Restructuring is present in more than 50 countries in the "center ", " semi-periphery" and the "periphery" of the world capitalist system. Many international institutions such as the International Monetary Fund (IMF) and World Bank (World Bank), after the International Conference on Privatization (1986) especially encouraged and financed those stabilization programs that introduce restructuring elements. For a successful restructuring program is required political consensus, which will confirm that a political coalition that was able to implement a restructuring program. To economic restructuring oppose all those who see in the restructuring endangering their monopolistic position. Some believe that the restructuring will result in the reduction of production and quality of services, increase prices, others see the danger of leaving the public control over the production of certain goods, the third point out possible efficiency reduction, fourth warn of rising unemployment etc. (Komazec, 1996, pp. 22-25).

The company restructuring achieve opposite results: improving products and services quality, meeting the needs, increasing employment, price reduction etc. Services and goods produced by the public sector can more effectively take the private sector. The last ten years, we observe the process of appreciation of the market structure and competition, improving management and encouraging privatization. The aim of the restructuring is to create favorable conditions for privatization.

## ***OWNERSHIP RESTRUCTURING COMPANY***

One of the key causes of the economic system inefficiency of the Republic of Serbia is not optimal ownership structure of a market economy. This situation in our economy produces inefficiency and inertia, and it is necessary to implement ownership restructuring. Ownership restructuring has more capital objectives: First, raise additional capital; Second, changes management system - instead of unprofessional and in many aspects of amateur management, the introduction of professional management; Third, the establishment of a favorable ownership structure of a market economy; Fourth, the creation of conditions for the capital mobility; Fifth, establish a

positive identification of the ownership of companies whose employees are co-owners; Sixth, the establishment of compatible types of companies with businesses in developed market countries; Seventh, the establishment of efficient and competitive - type basic enterprise (Vasiljević, 1995., pp. 155-159).

Ownership restructuring ways, are " tiled " with many issues: First, the tempo of restructuring - fast or gradual. Accelerated restructuring produces a system that implements the goals of equity restructuring, but it is objectively impossible in terms of material limitations because it causes a huge drop in the value of social capital in high supply and low demand ; Second, identifying the subject of social ownership of social enterprises in which extent are the workers, citizens or the state ; Third, if the process of ownership restructuring should be spontaneous or with a specific regulatory role of the authorized state organization; Fourth, the restructuring of the company at book or the appraised value; Fifth, whether the company should always be an autonomous entity decisions on ownership restructuring in the selection of models for restructuring ; Sixth, the restructuring of loss-making enterprises ; Seventh, the role of the so-called institutional investors (development funds, mutual funds, pension funds, underdeveloped social security funds, financial holding companies, banks, insurance companies, funds for employment) ; Eighth, the actual achievements of the ownership and management restructuring (Vasiljević, 1995., pp. 155-159).

## ***OWNERSHIP RESTRUCTURING MODELS***

The legislation establishes several models of ownership of restructuring enterprise, which leads into a corporation (a stock company or a limited liability company). According to Ownership Transformation Law, ownership restructuring is done in the company and any other form of organization that has social and state capital under the conditions and in the manner provided by law. Ownership restructuring object is a social enterprise and the state capital. A company that has a social or state capital determining by assessment the total capital value, social and state capital value and the capital value of other owners and the estimated capital is expressed in shares. Capital value is expressed in dinars and foreign equivalents. Ownership restructuring is done by selecting one or more models (Law on Amendments to the Law on Ownership Transformation, 2001. )

1. Sell the company or the ideal part of the company is the model of ownership transformation in which the company can fully or partially in the ideal area fined the owner. This model is recommended for small and medium enterprises ( in terms of regulations on accounting ) and may be particularly successful in financial support from banks and development funds using mortgage loans to real estate companies (fixed assets), to secure payment of these claims. This sale is done usually by public auction or by collecting offers, and exceptionally with direct negotiation. In this way the company can be sold to domestic or foreign legal or individual person. Under certain special conditions, which is a special variant of this model, the company may be sold

(in whole or at least the prescribed percentage) to persons who take management of the company, as well as special customer (a world famous company that introduces a new technology and open access to attractive markets). Since the subject of sale is a non-equity type of company, agreement on the company sale on the seller side concludes legally authorized entity (Fund for Development, etc.). (Vasiljević, 1995., pp. 155-159)

2. Sale of stock to raise capital (discounted) is a model of ownership transformation whose essence consists in the fact that the funds generated in this way belong to the company, that on this basis increase their capital and change its ownership structure.

3. Debt conversion into shares of creditors (with discount) is a model of transformation which characteristic is to give the workers of the company a discount to the nominal value of shares that have the right to purchase in a certain period and to a certain amount. The company's capital is reduced by the amount of shares sold without a discount (which bought the company workers and other citizens outside the quotas which can be purchased with a discount, as well as other domestic and foreign legal and individual persons) (Vasiljević, 1995., pp. 155-159).

The state established the companies that have no purpose. The state would have to return to the social sphere, but the social sphere is solved in profits. No social problem can be solved with the help of Forge, which will make huge losses, but the other way around. It is contrary solving social problems. Ownership and management are two important resources for success in microeconomic. Why property? Because it still need to get to the property by funds. The money can be debited and must be repaid. Money is very important, capital is extremely important, and the management is even more important because there are many who have invested a lot of capital ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)).

### ***THE RESTRUCTURING MODEL OF THE COMPANY IN LIQUIDATION***

Institute of conventional bankruptcy leading cashing of debtor and establishment of bankruptcy pending among the masses from which creditors are paid, all the less used in modern conditions. Institute of programmed bankruptcy, opposed to classical, doesn't lead cashing of debtor and the suspension of its business activities. Active cooperation of creditors, the bankruptcy debtor and the bankruptcy court allows the continuation of the business and financial consolidation of debtor. Objectives programmed bankruptcy can be achieved in two ways: First, by creating a new social capital from assets of the debtor, which warrant the fulfillment of the debtor's to other creditors; Second, the financial consolidation of existing businesses and identifying the owners of social capital (ownership transformation). This other way of programmed bankruptcy may be achieved by: downloads debt, debt relief or delay payments through voluntary or forced settlement and will bind all creditors, except for includes debt assumption, voluntary settlement, and

voluntary conversion of receivables and guarantees and warranties claims, which is implemented by special rules and commits only creditors who enter into such a legal transaction (Vasiljević, 1995., pp. 155-159).

### ***FINANCIAL RESTRUCTURING***

Money has the biggest influence in business and is an essential prerequisite for survival. Companies that are in the process of restructuring will need to monitor the inflow and outflow of funds, as well as their turnover at least once a week, or maybe every day. Each payment must be pre-checked and delay as possible. Credit departments in many companies will have to change their mode of operation and service regulations. They will need to centralize control over the money that is available i.e. withdrawal of funds from the operating units. The next step is to optimize the capital structure. With decreasing sales and profits, many companies have difficulty in paying interest i.e. servicing current debt; improvement of the balance sheet would certainly be useful ([www.poslovnastategija.rs](http://www.poslovnastategija.rs)).

Consensual Financial Restructuring is implemented at the latest prior to the bankruptcy proceedings. Financial restructuring is re-edit the debtor-creditor relationship between the company in financial difficulties as debtors and creditors. Financial difficulties are insolvency or over-indebtedness. Sleep debt is a temporary suspension of obligations fulfillment and prohibitions startup performance by the company in respect of creditors who participate in financial restructuring. Financial restructuring is introduced to re-edit of debtor-creditor relations, and claims which the debtor and creditor freely dispose of. This type of restructuring is carried out voluntarily, based on the written consent of creditors and debtors, with the participation of institutional intermediate.

Creditors who have agreed to participate in a financial restructuring are required to cooperate with each other in order to create conditions for the debt right to collect and provide data and information about their assets, equity, liabilities, operations and business plans, and to prepare proposals of restructuring measures. Conducting the negotiations with the debtor is the creditor with the largest total claims against the debtor on the date of application for the institutional mediation of financial restructuring. Financial restructuring provide to all creditors equal treatment and equal position in proportion to the amount of their claims. The debtor must provide creditors unrestricted access to data and documents relevant to financial restructuring, which is related to its assets, equity, liabilities, operations and business plans (The law on consensual financial restructuring of companies, 2011).

Financial restructuring can be implemented if it involves at least two local or foreign banks as creditors. Other than banks, in financial restructuring can participate all other creditors. During the financial restructuring is introduced inaction debts. During sleep debt creditors who have concluded an agreement on debt standstill may not take action to collect receivables, except than filing lawsuits to collect receivables in order to prevent obsolescence of its claims (The law on consensual financial restructuring of companies, 2011).

If the creditors and the debtor company during debt standstill period do not agree on the re-regulation of debtor-creditor relations, creditors when debt

standstill period expiry re- emphasize the right to initiate the collection of receivables from the accounts of the company, or the right to start or continue the procedure (The law on consensual financial restructuring of companies, 2011).

Serbian Chamber of Commerce, at the request of the debtor or one or more creditors, assisting in the establishment of cooperation between debtors and creditors, as well as support debtors and creditors in negotiations for successful completion. (The law on consensual financial restructuring of companies, 2011)

## ***ENTERPRISES COVERAGE AND RESTRUCTURING ACTIVITIES***

The restructuring is governed by the Law on Privatization and the Regulation on the procedure and manner of restructuring companies and other legal entities, and it is conducted by the Center for the restructuring at the Privatization Agency. Privatization Law provides restructuring process that preceded privatization. As subjects in certain stages of restructuring appear Ministry of economy and privatization, as strategist, the Privatization Agency as operations officer and controller, a company that is responsible for the accuracy of the presented information and union companies that should actively participate in the creation of a social program, the creditors - giving or approve the restructuring program, and also significant is cooperation with counselors agencies, government institutions and international consulting institutions. Companies that are in the restructuring process are not attractive to potential buyers and that is influenced by numerous factors ( debt, a large redundancy of workers, low productivity, inadequate micro and macro organizational company structure, technical, technological and physical obsolescence of assets). These factors have usually cumulative effect. A restructuring procedure consists the following phases: ([www.kombeg.org.rs](http://www.kombeg.org.rs))

- Initiative for privatization
- Delivery of the prospectus
- Agency announces prospectus
- Interested parties send letters of interest to the Agency
- The agency makes a decision on the method of restructuring and sends to the company
- The company shall submit to the Agency a restructuring program
- Verification of the program by the Agency
- The company removes remarks
- Implement Restructuring
- The privatization of parts or the whole enterprise

Identification of the company to restructure is affected by numerous criteria : First, the lack of interested buyers ; Second, the low companies solvency; Third, the existence of a product range that can stimulate recovery; Fourth, national and

regional significance of the company. A company that fails to meet one of these conditions do not meet the criteria for restructuring, and company probably ahead of bankruptcy or liquidation ([www.kombeg.org.rs](http://www.kombeg.org.rs)).

The privatization process is launched with initiative of the competent authority that is the entity to be privatized, according to the Privatization Law. Privatization initiative is an act of privatization entity which expresses its intention to implement privatization and shall be in writing. Privatization initiative is delivered to the trade union organizations that act in such entity and the employees shall be notified in accordance with the general regulation of the entity to be privatized. The initiative for the prospectus shall be submitted to the Agency within five days of its adoption. The privatization process can be interrupted by the initiative of the Ministry in charge for privatization and buyers. The initiative for privatization in entities with majority state capital Ministry in charge for privatization submitted to the Government of the Republic of Serbia for approval. When the initiative is initiated by the Ministry of Economy and Privatization or interested buyer deadline for submission of the prospectus is 7 days (Law on Privatization, 2012).

The company shall first conduct an analysis of the situation which involves assessment of the viability and success of restructuring, and company can independently perform or by hiring a consultant. For the analysis are necessary the data on the company organization, product range, assets and rights of the company, claims and liabilities, financial ratios and cost structure, the accuracy of which corresponds to the company CEO ([www.kombeg.org.rs](http://www.kombeg.org.rs)).

Assessment report also contains a proposal of restructuring measures. Among other proposed: First, organizational restructuring status is currently organized as a single divisible or indivisible enterprise mixed or holding ; Second, the concept of business units with positive capital whose only problem is insolvency, and business units with negative equity ; Third, the determination of redundancy as a basis for the development of social programs. The report will be presented to the Agency, the management and the union ([www.kombeg.org.rs](http://www.kombeg.org.rs)).

Agency announces the prospectus within 15 days of delivery by the company in newspapers, on TV, the Internet. The prospectus is a document by which a company presents business, financial and market situation, review the financial position and is given on the officially prescribed form. Advertising is done in order to collect data on the number of potential buyers. Potential buyers of its interest in buying capital in the company give it in writing form and inform the subjects of privatization and the Agency within the time limit specified by the Agency in the public announcement. Agency within five days of the deadline for collecting data on the number of potential buyers notify the subjects of privatization on the method of sale or the need for restructuring in accordance with this Act. (Law on Privatization, 2012) After the period of 5 days for collecting customer data Agency shall decide on the privatization method. Upon receipt of the decision enterprise shall submit within 90 days a restructuring program or agency itself conducts restructuring. The decision on the acceptance of the program Agency brings in 30

days from the date of the program delivery. The restructuring program should include: ([www.kombeg.org.rs](http://www.kombeg.org.rs)).

a) Information about the company and its operations : address, organization, association with other legal entities, the state of assets and liabilities, number of employees, product or service program, the structure of expenditure and revenue, the value of capital and property evaluation possibilities of a successful restructuring.

b) The status of organizational changes: a merger, division, change in shape, increase or decrease in capital, selling part or the whole company, the transfer of assets to another legal entity, agreement or compulsory settlement with creditors, rehabilitation through debt assumption, the conversion of debt to equity abandonment of unprofitable operations, changes in staff. The aim of these changes is repeal of non-profit business unit and profit centers reorganization.

c) Regulation program of debtor -creditor relationships: about restructuring process companies notify the Commercial Court and the creditors are publicly notified to submit their claims to the company within 30 days. Company indebtedness, inefficiency of bookkeeping and conflicting debtor -creditor relation require the process of harmonization of receivables with all creditors. If a dispute arises it is solved in a regular court proceedings, but they should do everything to avoid litigation because of high costs. The claims are agreed with the companies record. Possible discrepancies are removed and it is formed a preliminary list of creditors. After the alignment the classification is done on secured and unsecured, matured and not matured claims. Depending on the degree of indebtedness it is necessary to make smaller or larger write-off. Program is approved by the majority creditor or more of them when claims exceed 50 % of the total debt - then it is considered that the program was adopted. If no agreement is reached, the Agency may order the second restructuring process, propose modifications to the program, initiate bankruptcy or independently implement the restructuring.

d) Social program: agency oversees the development of social programs from the company, the Institute for the labor market, the Ministry of Economy and Privatization, and the Ministry of Labor and Employment. The company should give a realistic assessment of the needs for workers. For workers who lose their jobs should consider the age and qualification structure for selecting the right measures for status, define redundancies that will occur in the future as a result of the production modernization. The Government of Serbia has adopted a social program for workers that are redundant which accounts for about 35 % of employees in companies undergoing restructuring. For them is provided : severance pay in the amount of 6000 RSD per year of service, if they decide for a stand-alone business they will receive another 30,000 RSD, if they are brought together and established small businesses they will be encouraged with 300,000 RSD, workers who lose their jobs will receive a cash compensation up to 24 months, the program of the new employment, the program of public Works and preparation for re-training (3). Since the adoption until verification of restructuring program may take 170-210 days and for the implementation of the program at least

90 days. There is a real business need to be made operational business plan for the next 9-10 months from the date of initiative receipt. In order to facilitate the monitoring of the company opens a new account through which operates in this period. This change is recorded in the Commercial Court and the company itself is obliged to notify the business partner that is in restructuring. After making a decision on restructuring under Article 9 of Regulation company requires approval by the Agency for the implementation of certain business transactions such as the disposal of movable and immovable property, the giving and taking of loans, provision of guarantees for the other subject, commitment to another entity, structure changes, status changes, investment, the change in employment. The provided measures should help costs and business efficiency. (www.kombeg.org.rs)

### ***BASIC RESTRUCTURING TENDENCIES IN SERBIA***

Since the beginning of transition in Serbia, through the Agency for privatization has been privatized nearly 2,500 companies and collection was approximately 2.6 billion euro's. Although initially achieved significant results, the privatization tempo has slowed significantly in recent years. Since 2002. by 2008. average privatized 320 companies per year, while in 2009. until 2011. average privatized only 47 companies per year. This deceleration of the privatization process is the result of two factors: first, the remaining companies are relatively problematic, and second, there was a decline of investor interest due to the economic crisis (Arsić, 2012., pp. 133-137).

"Restructuring" status is used to non-privatized and the most problematic companies in order to protect them permanent from bankruptcy. These companies are on indefinite status of "restructuring" in order to avoid the troublesome process of resolving the fate of these companies, or resolving the fate of workers "employed" in them (Arsić, 2012., pp. 133-137).

What is the strategic goal of the restructuring process in the national economy ? Economic growth, sustainable development and exports to less indebted, more debt repayment, and employment (www.politickiforum.org.rs).

There are about 600 enterprises under the jurisdiction of the Privatization Agency, a number of those 600 are actually small and often attached to local governments, but there are about 150 in restructuring. Companies in restructuring employ about 55,000 workers, produces about 1.5 % of our GDP, added value as we make annually. Employ 5 % officially employed. Their productivity is extremely low. Most of these companies were offered for privatization, which failed and now are thinking about the different possibilities of how to use their assets, employment and production programs combined, free of obligations and debts. The point is that restructuring in which you pull out some funds and some employees actually what is everywhere in the world classical bankruptcy or even liquidation, but you are trying to save as much as you can of partners resources,

commercial production relations and of course the employees that the economic value of these companies activities do not lose completely.

Enterprises under the jurisdiction of the Agency for privatization Serbian society cost about 2-2.5 %, they are all state-owned enterprises, including the public. We will concentrate only on the companies in the Agency. The agency costs about 55 million euros per year, that was 2012. In previous years, there were about 100 direct subsidies and € 220 million per year of new debt. These are indirect subsidies, because sooner or later someone has to pay. This figure refers to all companies under the jurisdiction of the Privatization Agency, about 2 /3 to 4/5 of the company officially in restructuring. Accumulated debts of these companies stand in the nearly 500 million, only to public companies, not to mention debts to government, which are usually in the form of contributions for pensions, health, etc.. There are debts that are difficult to capture, and the rest of the healthy economy make business difficulties. When you help them and protect them you create unfair competition to private owners who are trying to produce something that might be in competition with the products of these companies. They are restructuring since 2001., when the decree was made. ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)) From the 179 companies in the restructuring in late August for 26 were declared bankrupt because that companies do not have manufacturing program that can meet the needs of the modern market. Companies which declared bankrupt, paid a social program, and 643 workers that applied was allocated 436.5 million (EUR 3.8 million ). Companies in restructuring cost the state and citizens \$ 750 million. In most enterprises restructuring is five years. Research shows that for the five years was spent 3.750 billion dollars (2.7 billion euro's) as it dumped money on companies that generally do not do anything. Many who are responsible avoiding the question, why tolerated so long these companies, and public secret was that on this way state buying social peace. It is actually the companies that were once pillars of development in cities across Serbia. With the closure of these companies, the state would have to deal directly with 51,000 employees in 153 companies which were in this case. The Action Plan should be to resolve the status of former socially owned enterprises, which reports the loss of his business, and citizens cost about \$ 750 million a year. The other group companies are those companies whose property will be offered for sale. If these companies do not find a partner, its time to find the privatization through bankruptcy. List of companies in restructuring process is as follows.

*Table 1: List of companies in restructuring*

<b>No.</b>	<b>Economic sector</b>	<b>Number of companies</b>
1.	Agriculture, forestry and fishing	18
2.	Mining	4
3.	Manufacturing	63
4.	Electricity, gas and water supply	4
5.	Water supply, waste water, waste disposal process control	1
6.	Construction	12
7.	Wholesale and retail trade, repair of motor vehicles and motorcycles	3
8.	Transport and Storage	5
9.	Accommodation and food services	6
10.	Information and Communication	4
11.	Financial and insurance activities	12
12.	Administration and other services	2
13.	Health and social care	21

*Source: Ministry of Economy of the Republic of Serbia*

The table shows the number of companies from different economic sectors that are in the process of restructuring and soon will be offered for sale. To this list belong companies located in Krusevac IMK October 14 Lubricant Factory, Branko Perisic, Star Garments, Oil Factory, a contemporary home and HI Parish. Listed companies belong to the manufacturing industry and are used to represent the core of economic development of Rasinski county. The assets of these companies will be offered in the future and these companies are likely to find a partner. However, if does not, its time to find the privatization through bankruptcy. You need to put an end to the 150 companies that are restructuring because they only spend money or property. When Privatization Law was adopted restructuring was barred, suspended or banned for a while. The law stated that anyone who buys capital, which had been the social, 2-3 years and sometimes even longer, the agency has contracted, that should not change the activity must not sell the property and buy another, that limited borrowing. The poor owner has actually had to be a bit tricky ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)). There was an opportunity at that time to repair the metal sector, part of the chemical sector and some other sectors, because they have suffered the most because of the ban on exports at a time when our economy was completely excluded from the rest of the world. Extremely important is to them to add some options to do something more creative. Today, after so many years, these companies can not do business in that field, because the business is past time. ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)) Most of the companies in its current state would not be able to survive in the market and would require intensive restructuring or resolution through bankruptcy or liquidation. Resolving the status of these companies requires political commitment, because it is associated with loss of jobs, but also the resistance of managers and some politicians.

## ***RESTRUCTURING PROCESS OF PUBLIC ENTERPRISES***

There are still two major sectors in state hands, two types of companies. One is what economists call the law and public companies, and it is largely, though not entirely, provide some fundamental functions such as power generation, telecommunications, public utility companies. These are some fundamental features that are not actually made from private ownership to twenty years ago and that they have great social and economic importance, and are regulated by a special law ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)). Public or state-owned enterprises are state-owned enterprises. Reasons for the establishment and operation of public companies are as follows: the state's interest in certain business areas (transport, energy, telecommunication, telecommunication systems, etc.) Public agencies have different objectives than private. The most common objectives are: to meet certain social needs, the achievement of social wealth, perform social functions that private equity does not show sufficient interest and others (Komazec, 1996, pp. 22-25). There was a belief that public companies are effective as private. However, the efficiency of public enterprises is necessary to ensure certain assumptions.

Competitive market structure: Inefficient management of the state financial and real resources and a lack of individual responsibility, shows inefficient micro-entrepreneurial function of the state, and the state usually becomes a "bad entrepreneur." Studies have shown that public enterprises are not sufficiently efficient and competitive to private, where the profit motive in these companies can not be more prominent.

Competitive property rights: private and public companies differ in all important elements of proprietary functions. Managers behavior in the public enterprise is less responsible than in private because the public sector is showing less sensitivity to risk than private. Markets and market institutions have an important role in public versus private companies (money market, capital market, investment risk, sensitivity to interest rates and losses, etc.). In public companies there is a tendency toward expansive employment, but also facilitates investment funds, which reduces productivity and efficiency in capital use. Social and political objectives in the public sector reduces the motivation for profit. It is accepted stance that because of the above mentioned reasons public enterprises (economically speaking) are less efficient than private enterprises.

The commercialization of the public sector : The ownership rights of public enterprises are not part of the capital markets resulting in lower entrepreneurial interest developed in the private sector. In all countries, resulting pressures for the privatization of the public sector, i.e. the maximum possible commercialization and market guidance of public sector enterprises. This resulting with the programs of deregulation, privatization and decentralization. Program of deregulation should remove restrictions that inhibit free behavior of economic entities and ensure increase economic efficiency and competitiveness of enterprises, and thereby the efficiency of the national economy (Komazec, 1996, pp. 22-25). In developed countries, the restructuring of the public sector includes: deregulation, privatization - enterprises, institutions and insurers, organizational reform and restructuring ( decentralization, the introduction of operating

mode that is associated with stimulation ), encouraging greater diversity and competition, changing role of services - from spending services switched to offering services, the introduction of discipline of the private sector to the public sector - interest capital is dominant. We can talk about public enterprises, their privatization and restructuring. Again it is worked on their depoliticization. In Privatization Law was given a deadline to complete the restructuring of those companies that are now under the authority of the Privatization Agency and are actually most often still socially owned. There are also state and the public, it usually does not think of them when it comes to public companies. These companies are again divided into those that are in restructuring and those that are not restructuring, but in preparation for privatization. ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)) From an economic point of view, the goal of restructuring is to improve the efficiency of public enterprises, and that will be achieved with the following measures : repairing of corporate governance, the government should complete the corporatization of the remaining large public companies, that the expected benefits of corporatization been achieved, it is necessary to establish and implement a transparent and professional framework for the appointment of directors and members of management and supervisory boards of public companies, for large public companies it is necessary to strengthen the role of the state as the owner, including the manner in which it manages public companies and supervises their activities. One possible approach is a clear delegation of authority and responsibility of a specialized department within the Ministry of Finance, which could help reduce the adverse political interference and allow them to strengthen the capacity to be focused and efficient. An important element in the reform of public enterprises should be the development of an integrated performance management, which would include the development of " key performance indicators ". Actual results would be publicly promulgated. It is necessary to introduce hard budget constraint (ie, to prevent the accumulation of arrears and unwarranted issuance of guarantees) clearly separate the role of public enterprises in carrying out the role of public importance and their commercial operations. One possible model are contracts for providing services in the public interest. Public companies would commit to a certain level and quality of services of public interest, which are not commercially viable, and it would be receiving direct compensation from the state. This compensation should gradually replace all forms of support (eg subsidies for current operations and guarantees of indebtedness) in addition to the reform of the subvention and the issue of guarantees, it is necessary to reform the system of tariff determination, as well as appointing authority so that they are based on actual operating results of the company, measured by both financial and " key performance indicators " The current system of state help is fragmented ; it is necessary to develop a unique and comprehensive database for all forms of state support, that will included public and large state enterprises. Improving the management of public enterprises would increase the chances of their privatization. From the standpoint of economic efficiency, it is justified the privatization of enterprises operating in competitive conditions, such as Telecom, Galenika, Železara Smederevo and others (Arsić, 2012., pp. 133-137).

## ***THE RESTRUCTURING PROCESS OF REAL SECTOR IN SERBIA***

The process of restructuring of the real sector in Serbia is 17 years old. You do not need to go far in terms of restructuring in other countries and other continents, it is enough to look what is happening in the real sector restructuring, draw experience and on that basis bring political and other decisions related to the restructuring of the public sector. The restructuring of the real sector started in the 90s of the last century. No matter in what form, legal and other, and no matter who was in power that restructuring process has produced disastrous consequences to the industry in general. Then government said that companies that will be included in the restructuring process are the strategic enterprises primarily, that have a national or regional significance and which employ large numbers of workers, who have specific problems related for its debts. It was the 1996th year. Criteria were then eligible, it was thought that the process will go in a positive direction. What happened was that the management of these companies realized that they had become white bears of Serbian economy. They did not have to pay various taxes to the state and no bank or any creditor was unable to collect its receivables. For those companies are associated the largest corruption scandals in previous 15-20 years. At the head of the company in a high percentage were the people that were coming from the government structure, i.e. from a certain political party as long as the company was vital and as long as it had nothing to steal and nothing to be dismembered. Because of this behavior, we came to other conclusion, which was that a number of these companies, and the list of these companies in fact was a kind of list for the shooting and killing Serbian industry and economy. Now we hear the announcement of the Government of the Republic of Serbia that this restructuring process should be completed in June of 2014. What do we actually do that welcome 2014. with completely clear situation, that we saved and that we undertake, here we took such and such activities and something we have succeeded and something not ? It is obvious that this process is very mystified and we do not know who is going to survive.

All these activities killing Serbian economy, taking place under the cloak of re-industrialization, creating a new economic development strategy. Why do we say under the cloak? Because it is a mysterious process. The unions do not participate in it, although we were advocates of the process to start. We do not see that professional public is included. On the ministry website you can see that some people are consulted and some experts were involved, but nowhere you can see who is this, if it's an institute, an individual, or something else. From 1996., when the restructuring of the industry began until today have been lost over 200,000 jobs. Hundreds and hundreds of companies were shut down. These companies have gone through the process of a second and third privatization. It is a walk through the agony for the people who are in those companies really honestly and fairly tried, through this process to find a solution for the enterprise that led, although the majority of those directors were the criminal structures that eventually no one is

going to account nor responded why they spent hundreds millions of euro's. All this was done under the cover to preserve social peace and a big concern for employees. Companies with whom we live and of which we are living, using their products; were proud of it, because they were kind of brand of our business and industry. These are the Prva petroletka, FAP, IMT, IMR, Machine Industry Nis, Electronic industry, Dragon, Wagon Factory Kraljevo, Jumko, Beko, Kluz, all companies from Leskovac former Serbian Manchester, Zorka, Župa, Rad, Prahovo, Ljubisa Miodragović, Ivan Milutinovic, etc.. These companies will not exist. Some have gone and some will soon disappear. No one is taken into account, nor will file a liability. ([www.politickiforum.org.rs](http://www.politickiforum.org.rs))

What we have never tried with us, and that's about to let out or parts of assets or the entire business of a company. It is a form of restructuring in the market economy. The restructuring consists of good ideas, choosing the best and the bigger combining the better restructuring. Bigger issue is neoliberals or justification state that does not longer participate. The Republic of Serbia is a country of small economy and for its economic policy is very important to completely separate look at the micro economy and get into the problems of micro economics. ([www.politickiforum.org.rs](http://www.politickiforum.org.rs))

### ***SOCIAL PRICE OF CORPORATE GOVERNANCE IN SERBIA***

We know that will be laid off 80 % of these 55,000 people. They go to the street, many of these companies will fail and therefore these people will become completely unproductive, so far at least something is produced. As a major obstacle to serious solving of unemployment problem is the lack of any long-term government strategy to solve the national burning question. Through future employment strategy should put emphasis on solving problem of poor segmentation of educational backgrounds (Damnjanović, 2013., pp 289-315).

Ten years of privatization on the liberal recipe produced some results where there were sold successful companies. Here and there is a company that was already in difficulties with private capital and packaged privatization failed, but how to deepen the difficulties in which companies are so increases the probability that the liberal response wouldn't be good. The other side says we can not just like that put people on the street. We had ten years and there is no answer, there are no results. Why are they there ? We think it is not true that public property can not be managed well. We could see that this country has a successful state and socially-owned enterprises. A good part of the German economy depends on the banks that are state-owned. Let us not be blind to the fact that the management of the state or public property, including the social itself did not have to be a failure ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)).

When the social, public, state-owned enterprise or organization, show poor, it is followed by the transformation process. In Serbia, we have " restructured " companies that we recognized finished state. We do not know if someone took

organizational functional unit, the reality is restructured, and we recognized. The moment when on the serious market stage a company sees that they can not cover the costs, they sit at the table and think what they have and how much to keep, with what vision and in what they have to put to change something. It is true that at first some people lose their jobs, it is true that some countries help these people and some do not, but the one who is given the task of leading an economic unit is tasked to find a solution. He is seeking for a solution within the resources that he have and going away. Sometimes the state and public institutions know to work that. One of the problems are these companies that we have put in the restructuring of ten years or more. Why do we put them? The intention was to do with them what was happened in the developed and established market economies to private. That is a process that is extramural, that it is actually under bankruptcy legislation and eventually get something healthy or liquidate.

We knew that we couldn't do that by legislation that we had. It had to be done under proper legal bankruptcy. This was a pretext and cover the regulator to do something that was extremely logical, necessary and best for all. Very soon the effort to really restructure the company has died. Others said it was actually a form of subsidies, direct and indirect. We all know that this means that one part going to the salary, which are social security, but largely go to corruption or the fact that no one is really responsible and really have some hope of creating something. Why it happened and what now? We are in 1965. abandoned central planning, and then forget that kind of capacity in public institutions for economic thinking, analysis, guidance, coordination must be built.

Than from 1965. until 1990. and especially after 1974. there were mechanisms in Yugoslavia which primarily relied on a quasi- state institutions, economic institutes, centers, but the State Administration, especially at the national level, during time absolutely left every effort and thus the capacity to be able to do an economic analysis. When it happened 2000th we were actually what is left at the federal level and finish them off, and on the republic level we begun to make two types of institution: what we proposed by international financial institutions, such as the Privatization Agency, which should lead as in the private economy, and what Europe said to us, and that is what is needed to harmonize our law with theirs. No one was involved in our ability to perform the most basic way of economic direction of our development, and so over the next ten years.

Today in Serbia we do not have a single institution in the state that follows what happens in the real economy or research center. All those former that we had, Institute of Economics, Institute of Economics science, market research, became consulting firm. People were not guilty. The company management of social companies and all employees had to develop their own restructuring programs. In their interest was to don't do anything, and if it was in their interest, in the short term, of course they do not know what to do. That's why capitalism succeeds in restructuring and socialism never. Because when something does not work comes second owner. The neo-liberal model is not only and dominant, but when carried on he is working, because you have the opportunity, a lot of capital and because the sale comes much earlier. No one there is buying the company in a state in which

our companies was in 2001., and certainly not now. Whatever discussion we make today, we have to answer to the means, what, and how, if you do not want illiberal model. If you do not have an answer with what means and how than neoliberals model is better. Hundred million, two hundred million a year by infecting the rest of the economy in that it is free of charge, by promoting unfair competition, by the distracting State Administration in solving problems in a company that can not solve their own problems, it costs entire society too much. In the end, the children of people who will one way or another have a social problem of restructuring will have a better chance to get a job if you do it before, nor if you do it later. It is not true that it is not possible to do something, it is true that we never began the task of training ourselves as a society to do something if we do not want to be a neo-liberal model ([www.politickiforum.org.rs](http://www.politickiforum.org.rs)).

### ***THE ROLE OF STATE AND ECONOMIC DEVELOPMENT***

American economist Moses Naim made the concept of liberal economic reforms that being implemented in two phases: the "first generation reforms" and "second-generation reforms". In the first phase, the priorities are to reduce inflation and economic growth, in the second phase it is necessary to increase the international competitiveness and maintain macroeconomic stability. Changes in business strategy in the first phase relates to macroeconomic policy, reducing the role of government in economic life and the elimination of protectionism. The second phase of reform is building institutions of a modern market economy. "Second-generation reforms" involve the construction of market institutions, increasing the competitiveness of the private sector, health, education and other public services. Instruments used to implement "second-generation reforms" among other measures include restructuring different sectors of the economy and building institutions for the exports promotion (Moses, 1994., pp. 59-63). "Second-generation reforms" include the construction of legal, regulatory and political institutions. Some of these measures in order to advance the realization of the "first generation reforms" (for example, " careful liberalization of the capital account " is aimed at macroeconomic stability and financial stability, which is liberalized in the first phase of reforms. During the discussions that are taking place in the Serbia about the role of state in a modern market economy, it is necessary to point out what is the role of the state in the "second generation reforms". "Second-generation reforms" require strengthening the role of the state in terms of strengthening the regulatory functions of the state, the role of the judiciary within the " rule of law" and ensuring social security of the population. Within the "second generation reforms "it's about defining" small but efficient government" in a modern market economy (Stojanović, 2008., pp. 84-88). The group of economists gathered at the Washington Institute for International Economics, led by John Williamson in 2003., thoroughly analyzed the economic development of Latin America and formulate proposals for a new beginning of development and

economic growth in Latin America. Recommendations are important not only for the countries of Latin America, but also due to changes in the development strategy of the former socialist countries that are building a market economy, including Serbia. Gradually are changing views on the relationship between government and economic development (Stojanović, 2008., pp. 84-88).

A World Bank report in 1997. among other things, says that "the completed development under the domination of the state, has been completed and development without the state. Good government is not a luxury but a vital necessity. Without successful country sustainable, economically and socially growth is impossible. "In all the above discussion still lacks a definition of the economic role of the state. The theoretical basis of the regulatory functions of the state in the economy, is based on the " theory of market imperfections " and " theory of asymmetric information " market aggregates, for which Stiglitz won the Nobel Prize in Economic Sciences. (The World Bank, The State in a Changing World Development Report, 1997., pp. 95-100)

Serbia needs a change of economic philosophy, respectively a new development paradigm. We need a new concept, an alternative model of development, but as it is appropriate to "small open economy". It is required a shift from the "neo-liberal concept" towards the idea of efficient markets and state regulation. Sequencing of reforms depends on the objective assessment of the situation in the national economy. We need the export orientation in order to reduce the dependence of the Serbian economy from the influx of foreign capital, mainly foreign loans, but also to achieve higher rates of economic growth. To make this happen requires proper policies, aimed at increasing exports of goods and services. The most successful transition from a socialist to a market economy and the best development successes was achieved by those countries that have their own programs of economic development, which corresponds to the specific circumstances of a given country (Stojanović, 2008., pp. 84-88).

## ***CONCLUSION***

In Serbia, the restructuring process is delayed and there is no agreement on how and when to implement it, because the restructuring rule means a loss of jobs or requires substantial investments. The focus of the restructuring process is the ownership, organizational and financial restructuring of public enterprises in the real sector. In the restructuring field of public enterprises were achieved modest results. In one part of the company carried out a process of organizational restructuring. Some companies made a change in the legal form of a joint stock company, started a labor surplus and implemented some forms of financial restructuring. The public sector is facing problems of overstaffing, above average wages, poor financial results and party influence. What to do with too large, inefficient public sector and how to implement the management professionalization? In 2013. number of " in restructuring " has reached 179 ( 54 000 employees). The basic form of "restructuring" was financial,

which basically came down to protect the company from payment of submitted bills. Direct subsidies to the state of 2013. they have reached 3 billion, and through the support of about 4.5 billion. Companies "in restructuring " have the following problems : huge budget allocations (but each company of modest means ); frequent protests of workers ( " all eyes " are upon state employees, often the highest state officials, who are required (soft ) solution to numerous problems in the short term ) and the lack of interest of potential investors for privatization. Exit from the crisis are increasingly asking for the "pre- planned restructuring programs " - a wish list or a real plan of action.

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## ***BUSINESS NEGOTIATION***

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### ***ABSTRACT***

*This paper describes business negotiation, as an essential part of a business process. It deals with the concept and notion, goals, participants, forms, course and phases of negotiation process.*

*Negotiation is defined as a process of discussion between two or more parties, which often have different interests, in order to achieve a commonly acceptable solution.*

*The goal of negotiation is to reach an agreement, acceptable to all participants. This is achieved through cooperation and compromise between parties involved in the negotiation. Negotiation is the art of adapting. It is the art of giving in order to get more in return.*

*There are different forms of negotiation: internal and external; intuitive and rational; positional, principle and opportunistic, and depending on the positions taken by each party in the negotiation process, there are the following forms: win-win, win-lose, lose-win, lose-lose, win and win-win or no deal.*

*The entire negotiation process takes place through two main phases. The first step involves planning and preparation, and the second stage is the negotiation process. In some cases, there is the third phase. This happens only when one of the parties deviates from the agreement reached. Then the negotiation enters a new phase – repetition of negotiation.*

***Key words:*** *Negotiation Process, Participants, Goals, Forms, Concessions*

***JEL Classification:*** *M21*

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## ***THE CONCEPT OF BUSINESS NEGOTIATIONS***

Negotiation is a process of discussion between two or more parties, which usually have different interests, in order to achieve a common, acceptable solution. It is based on the assumption that it is a controlled communication process with the aim of resolving the conflict of interest between two or more reasonable negotiating parties, where each party can block the achievement of the goal of the other. If one side cannot block the achievement of the objectives of the other side, then it is not a negotiation. Negotiation is a special form of social interaction, a life skill, with differences and conflicting interests. Negotiation means to seek agreement through dialogue. That is the way people solve their differences and disputes. This is a basic form of human communication which is often used, but people are not always aware of it.

There is also the notion that negotiation is a form of interaction in which a group of subjects with conflicting interests are trying to reach a mutually acceptable agreement on the distribution of limited resources.

In the simplest terms, negotiation is a discussion of two or more parties who try to find a solution to their problem. It is an interactive process of communication that may happen whenever we want something from other people or they want something from us. It must be borne in mind that negotiations are reached by a voluntary consent of the negotiating parties and that each party has the right to veto the final result.

It is recommended that all disputes are resolved by reaching an agreement, regardless of their nature (disputes between political parties, between religious sects, between companies and trade unions, among researchers in an institute, between parents and children, between teachers and students, etc.).

Business life is full of such situations, and all managers must negotiate on daily basis and seek solutions to problems. Negotiation can be even fun if they know how to do it. The real problems and difficulties arise if, in most cases, someone comes out with the feeling that he failed in negotiating.

Factors of negotiations are: subject of negotiation, participants in different roles (buyer-seller; investor-contractor; owner-manager; lender-borrower; management-strikers, etc.), goal to be achieved, ambient (location) in which the negotiations are conducted, general atmosphere, as well as many situational factors that may influence the outcome of the negotiations and the prospect that the agreement is reached (Pokrajac, 2008, p. 281-291. This interpretation of business negotiation significantly relies on the cited text).

Ethical considerations require that one should always be well prepared for the negotiation process. Preparation is the main factor of the success of the negotiation. One needs to supply the arguments, data, and even the occasional jokes. One should not be too hard, unyielding at all costs. Stubbornness is a sure path to failure

of negotiations. Negotiations can be considered successful only when both negotiating parties are satisfied with the outcome. Otherwise, our seeming success may, as a boomerang, return to our heads. Therefore, you should skillfully apply a strategy that clearly separates goals to be achieved and those which can be "sacrificed". Every experienced negotiator must know his goals and his possibilities, to be able to determine his expectations. Negotiation is not imposing one's will, and does not solely serve to fulfill one's own interests.

For each of the phases it is possible to identify and extract certain elements and their application and knowing them lead to a successful final outcome. Negotiating skills, therefore, are no longer viewed as an innate talent. In today's complex and changing environment, it is of course still necessary, but it is no longer sufficient. Successful negotiating behavior increasingly depends on the knowledge of proven theories and good negotiation practice. Negotiation should be regarded as one of the key business processes that increases the value of the business enterprise and its participants.

### ***GOALS OF BUSINESS NEGOTIATION***

The main goal of negotiations should be a mutual agreement. From the moral point of view only cooperation and compromise can lead to an agreement acceptable to all participants in the negotiation. Negotiation is the art of adaptation. It is, in fact, the art of giving away in order to get something more. In order to achieve this goal it is necessary to leave various prejudices related to gender, race, ethnicity, physical characteristics, financial status, religious, political, ethnic, or other affiliation. All this may limit our possibilities of easier and more effective communication with other participants, and thus the success of negotiations. Women are not stupid, all men are not good negotiators, good-looking might not be intelligent, poor people are not less capable. We must not think that way. It may create a prejudice that it will be too easy or too hard to reach the goal of negotiation. To reach the goal we must use rational approach and flexibility. If we use flexibility, crucial feature of successful negotiators, we will always find a way to dispel prejudice that, during negotiations, may jeopardize the ability to adapt. All people have their own psychological and mental characteristics that make them more or less suitable for a successful negotiation. However, the existing human resources are a reality of any organization and it cannot change overnight. Of course, in the long term, it is to some extent possible, primarily in the context of building organizational culture.

## ***PARTICIPANTS OF NEGOTIATIONS***

From the point of negotiation, people as negotiators can be divided into seven psychological types (for further reading see URL: [www.poslovniforum.hr](http://www.poslovniforum.hr)):

- Dominant negotiators are those who want to dominate negotiations. They use rough tactics and tend to command. They suffer from an inferiority complex, refute the arguments of others, mostly by being loud. In fact, their negotiation essentially comes to persuasion, including the extortion.
- Extrovert negotiators have a similar approach as dominant ones. They are superficial, they use rapid and short negotiation to achieve their goals only. They devote too much attention to appearance and material environment.
- Introvert negotiators do not confide in anybody, they do not have confidence in anyone. They rarely agree to negotiations and are very difficult to open. That is why they need more time and patience from others.
- Innocents are pleasant, polite negotiators. They look like they will do anything just to end negotiations peacefully. But if negotiations continue for more than 5 minutes, they turn into dangerous negotiators. On the basis of calmness and confidence of the other side, they create a feeling that they will agree on everything. In fact, they turn other negotiators to a subjected position. In negotiation with them, the other side gets the impression that they achieved what they wanted, but they soon realize that the agreement was more suited to the others.
- Actors are negotiators who use all kinds of acting, from a recognizable image, to unusual behavior. It may seem that they more appreciate the form than the outcome of negotiations. Yet, they prefer the effects of negotiations to the form.
- Philosophers are negotiators recognizable by their unpredictability. They are for something, and then, in a second, they change their mind and are against it. They look like they do not know what they want, but they know it very well.
- Guardians are conservative negotiators, full of common sense. They believe in traditional values. Their goal is to have a positive result of negotiations, to keep both sides satisfied. They do not like persuasion. From the ethical point of view, they are the fairest.

After enumerating the characteristics of individual negotiators, there arises a logical question about the main characteristics of a good, real negotiator.

Characteristics of real negotiators are:

- Knowledge (intelligence)
- Negotiating skills (experience),
- Honesty (fairness). They take care of their own as well as the interests of the other negotiating party.
- Pragmatism. They do not ask the impossible, they set realistic and achievable goals.

- Flexibility. They use a variety of options, including trade-offs and compensation from both sides.
- Inventiveness and creativity. They have an idea of the various possible alternative solutions to problems.
- Visioning. They bear in mind cooperation in the future in order to resolve the current negotiations quickly, easily and favourably.

## ***TYPES OF NEGOTIATION***

There are different forms of negotiations.

1. By the location of negotiation, it is divided into internal and external negotiation (Jovanovic, 2005, p. 232-233).

Internal negotiation is performed within the company. They include negotiations with management about current and developing enterprise, about the distribution of resources between different departments, negotiations between management and unions over pay and conditions, negotiations of different levels of managers on how to organize a joint venture, negotiations of managers and their subordinates about solving of a problem, negotiations and discussions on the reorganization, etc.

External negotiation is done with stakeholders, with people outside the company. This is related, for example, to the sale of certain products or services, the purchase of certain raw materials, negotiations about securing the financial means, joint work and realization of certain enterprises, information on integration, etc.

2. Due to the factor on which they base their thinking and reasoning, there are intuitive and rational negotiation.

Intuitive negotiation is based on emotions, self-confidence, intuition, the "voice within". In practice, a much larger number of people uses it than it is commonly believed. When deciding on some minor issues, it can be understood and justified. But when deciding on some crucial issues, with major consequences, it can be very risky. Some managers negotiate this way, due to their overload, overwork or lack of time.

Rational negotiating is based on facts, conscience, understanding, knowledge and experience. It means calm immersion in fact, reflection and necessary consultation. It is thorough and much safer.

The main difference between these two modes of negotiation is that intuitive negotiation is: fast, easy, effortless, automatic, under the influence of emotions (positive or negative), quite risky. Rational negotiation is: slow, difficult, hard, logical, conscious, less risky.

3. Given the nature of negotiation, it is divided into: positional, principle and opportunistic.

In positional negotiation participants have limited powers. The negotiation process is usually very long and agreement can be achieved only after hearing all the controversial details connected to reaching a mutual agreement. These are usually difficult and lengthy negotiations. Examples of this form of negotiations are bargaining negotiations between employers and trade unions on wages, negotiations between buyers and suppliers, territorial disputes, long-term development programs, and so on.

In principle negotiation, we must first determine the basic objectives and principles of negotiation and when the participants agree about them, then they try to reach an agreement. In order to successfully negotiate and obtain an acceptable agreement, it is necessary to first establish all possible options and to consider each separately in order to reach an agreement. This is a more favorable form of negotiation, because both negotiators have a sense of reaching a positive solution and not a loss, as is usually the case with positional negotiating.

Opportunistic negotiation is a specific form of negotiation that can sometimes precede positional and principle negotiation, or can be done during breaks or interruptions, and in the course of negotiations. This form is done indirectly through secret messages, indirect impact on other negotiators through a third party, press, media and the like. This type of negotiation can shorten the time of negotiation, which, especially in positional bargaining, can be very long. It may also help to avoid interruption or failure of negotiations.

4. Depending on the attitudes that in the negotiation process the two parties apply, there can be defined different forms of negotiation (Corey, 1994, p. 188-213).

According to Steven Covey, there are the following options:

- Win / win (both sides win)
- Win / Lose (I win, you lose)
- Lose / Win (I lose, you win)
- Lose / Lose (both sides lose)
- Win
- Win / win or no deal (both sides win or no deal).

Win / win. All parties involved are satisfied with the decision and wish to participate in the activities. There is enough for everyone, and the success of one side does not mean the failure of others.

Win / Lose (I win, you lose) is the negotiating process in which there can only be one winner. Most people look at life in this way since birth, which later becomes their life philosophy. Of course, if we are in a situation that is really based on a low level of trust and there is a limited amount of resources to divide, there is a place for this kind of thinking.

Lose / Win (I lose, you win) is according to Covey worse than win / lose, because in this case there are no requirements, standards, expectations or vision. People who have this approach to relationships only want to appeal to others. In negotiating, such an approach is considered surrender. It is used by those whose only goal is a good relationship with the other party, regardless of the result of

negotiations. According to Covey, both win / lose and lose / win are weak positions that are based on the uncertainty and personal insecurity.

Lose / lose (both sides lose) - When both participants have win / lose mindset, both sides will inevitably lose. Some negotiators so much focus on the opponent, to become blind to everything but their desire that the other side loses, even if it means they lose, too. Divorce is a typical example of this paradigm.

Win - People with this mentality do not consider it necessary for someone else to lose or win, it's irrelevant. The only thing that is important for them is to get what they want. According to Covey, this is probably the most common way of thinking in everyday life. There is practically no real negotiation.

Win / win or no deal - "no deal" basically means that if you cannot find a solution from which we all benefit, it is better to separate as friends and break up the negotiations. According to Covey, when we have this option, we feel to have more freedom. We do not have to come up with a solution at all costs, and we can really try to understand the other side.

All of these solutions can be reduced to two basic forms of negotiation: competitive (win-lose) and consensual (win-win).

The first form, the so-called competitive negotiation, is based on the principle "win - lose", which means that one party wins and the other loses. This is a negotiation that takes the form of competition of two opposing sides, each trying to impose their interests. Negotiation is hard, conflicting and usually long, often with an uncertain ending. The most common negotiation endings when one side achieves a significant advantage, or when a party deviates from its hard line and wants to put an end to negotiation. This occurs when one party knows the goals of the other side and the final point where it wants to go to. It also happens when one side is pressed for time and wants to finalize the negotiation process.

The second form, the so-called consensual negotiation, is based on the principle of "win - win", which means that nobody loses, both parties win. It is a negotiation that takes into account interests of both sides. To make this form of negotiation successful, it is necessary that both sides want to reach a mutually acceptable solution and that they are ready to analyze reasonable and advantageous solutions for both parties. It is believed that this is the most advantageous form of negotiations, which leads to the satisfaction of both negotiators.

From the ethical point of view, consensual form of negotiation is the most acceptable form. In order to be successfully used in practice, the negotiating parties are advised to follow the following principles.

- Viewing the problem from the point of view of the other side. Trying to understand the other side and its needs.
- Identifying the main issues involved in the negotiations (not positions).
- Identifying the results that would be perfectly acceptable.
- Identifying possible new options to reach these results.

From the ethical point of view, negotiation should not be directed solely at achieving the highest possible economic effects. Sometimes non-economic effects may be more important. You need to look at long-term goals and interests -creating trust, advertising, winning the market, understanding the position of a business partner important to us that can sometimes be unfavorable. This form of negotiation is from the ethical point of view the most acceptable solution. It arises in a situation with a high degree of trust among negotiators. It is based on reality, benevolence and understanding of the situation.

## ***CONCESSIONS IN NEGOTIATING***

Concessions are also an element of negotiation. They have a very important role in this process. Some even believe that they have a central role. They are the heart of the negotiation process. If there were no concessions, there would be no negotiations. If one of the negotiating parties is not ready for any compromise, then the other must give in, or they will reach a stalemate and there can be no negotiation.

That is why people who begin negotiations always expect to get some concessions. They are also prepared for demands from the other side, respectfully.

Concessions are changes of the original offer in the direction of interests of other negotiating party, which also reduces its already stated demands in return.

There are different types of concessions: by size (large, small), by the amount (much, little), by the time they are given (initial and final stage of negotiation), by the speed (fast and slow), by the way (all at once and gradual) (Petkovic, (2011), p. 53-55).

Different people (different cultures, religions, customs) have a different attitude towards concessions. In fact, everyone understands their importance as an essential element of negotiation. However, they have a different attitude toward the act of concession. Some believe that we should make concessions but should not bargain much. Other people enjoy in it. This is especially true of Oriental people. For example, if one accepts the full offer immediately or accepts it quickly, easily, without much bargaining, they are not happy. They think that they did not make a good job, because they initially set very modest conditions.

In practice, each negotiating party in the beginning of negotiation process starts from its own area of interest. This zone has the lowest critical point as the "last price", "final offer" and so on. This means that they know exactly how far they can go, and where to stop with concessions. Each side tries to keep a secret about their interests of negotiation, while trying to find out more about the area of interest of the other. This once again confirms that the process of negotiation, and the concession process connected to it, is very complex and requires a lot of patience, knowledge and skills.

There is also strategy and tactics. According to our strategy we know that we must give in, how much, to what extent. Tactically, we estimate when and how to make concessions.

Negotiation takes place slowly, in stages. In the way of negotiations, there appear concessions. In the beginning, we give small, less significant concessions, and later – bigger ones. It is determined when to make the biggest, or the latest concession. It depends mainly on the behavior of the other negotiating party.

Given the importance and great presence in the business life of the negotiation process and related concessions, there are many books written about it. There are a number of ideas and suggestions. Some have even attempted to systematize and make certain models, templates for making concessions. However, just as all negotiations and almost all their elements are specific, so is the case with concessions that accompany them. That is why these specific, diverse and dynamic processes cannot be shaped into the form of a template. Bargaining and concessions are among the very few functions in a company, which cannot be fully standardized. However, this does not mean that some recommendations in this regard should not be known and used in practice. Such recommendations are usually the following:

- It is good to plan concessions ahead. Planned concessions are less painful than those that are unplanned, given under pressure.
- When planning any negotiation, we should leave enough space for concessions.
- As much as it is possible, we should try to open the other side, to find out its basic intentions, interests and possibilities.
- For our part, we should give some information so that the opposing party gets the impression of our willingness to cooperate. However, the information should not be the most important, but some less important.
- It is good to be the first to give a smaller concession, but last when giving the biggest concession.
- We should exaggerate every concession given and attach greater importance to it than it objectively has.
- For each concession given we should try to get something in return - "tit for tat".
- During the time of negotiation and exchange of concessions, we should watch the other side's "body language", non-verbal communication: eyes' reaction ("eyes are the mirror of the soul"), changing the face colour, nodding, hand gestures, posture, etc. These things can lead us to conclusion whether the other party is satisfied and whether the end of negotiations is near.

## ***ETHICS OF NEGOTIATION***

Ethics as a science of morality, among other things, determines the moral norms that prescribe what is moral and what is immoral, what is allowed and what is forbidden, illegal. There are certain norms that are universal, applicable to all civilized societies. There are also certain moral norms that are related and are valid only for a particular culture, religion, nation. There are even narrower moral norms that are connected only to specific structures, professions-ethics of doctors, professors, judges, customs officials, military officers, sportsmen, etc.. There are individuals who, because of their origin or the educational system, have moral standards that are lower or stricter than the officially accepted moral norms.

Problems in business arise when some individuals accept the principle that everything that is not forbidden is allowed. There especially arise problems in international business, where members of different religions, cultures, nationalities meet. Such is, for example, the case with corruption, which is in the countries of Europe or America considered not only immoral but also illegal, compared to most countries in Asia, Africa and South America, where it is almost legalized.

Such is the case with signing and respecting of contracts. Countries of Europe and America are for strict observance of all provisions of the contract, while in most countries of Africa and Asia (China, Japan, Korea) a contract regulates only general cooperation, and details must be further discussed.

That is also the case with tax paying or tax evasion. In the first group of countries, tax evasion is considered one of the gravest violations and is strictly punished. In a significant number of the second group countries, it is considered normal that companies do the book-keeping in three ways, in order to avoid taxes.

There are differences in terms of basic elements of business ethics and corporate culture: respect of deadlines, punctuality of arrivals at business meetings, relation to business gifts and so on.

Because of these differences, there are also differences in the process of negotiation. The first group of countries has maximum respect for the ethical principles of negotiation, while others believe that it is not immoral to use unethical means (fraud, bluffing, lying, etc.). Some countries even think that there is no negotiation ethics that should be respected, but one should be free to negotiate and use all means available.

Today, under the influence of globalization process, individual countries and continents connect and the negative views are seen as relicts from the past and are increasingly being overcome.

For normal and successful completion of the negotiation process, it is essential that there is adequate environment. The environment should be characterized by an atmosphere of trust, safety, relaxation, good faith, optimism, hope of success. Participants in the negotiations should be on an equal footing, free, without any pressure, obligations and restrictions. They should freely expose their views and protect their interests.

Such a good negotiating environment can sometimes be compromised. Disturbance is usually seen in the form of disorganization, tension, hostility and too friendly atmosphere (Petkovic, *ibid*, p.55-62).

Disorganization manifests when one or both of the negotiating parties come to negotiations unprepared or under-prepared. It is clear that without a good preparation there can be no successful negotiations. In this case, one should stop disorganized meeting and immediately start organized preparation for the meeting. Having done the necessary preparation, one should define the agenda, start the meeting and work strictly according to the previously defined agenda.

Tension may occur due to various reasons. Again, the most common is inadequate preparation. If everybody is aware of it and agrees that negotiation process is not performed in a satisfactory manner, tension can be relieved by having a break, by informal conversations, so that people get to know each other and relax, and then start over the negotiation.

Hostility also occurs when negotiators are not prepared, when agenda and goals of the meeting are not clearly defined. Negotiator who initiated the meeting should take more decisive position, and find and analyze reasons that created hostile atmosphere. When things are clear, hostile atmosphere will evolve in a friendly and relaxed, and conditions for normal work will be created.

Too friendly atmosphere is created by inexperienced negotiators. Because of the importance and responsibilities of the job, as well as lack of knowledge and experience, and sometimes lack of information, negotiators are afraid, they don't have confidence. To cover it up, they try to be overpolite. They forget that professionalism has its principles. Kindness cannot be a substitute for professionalism. It can only emphasize it and make it more elegant, more acceptable. Someone with more experience should direct and animate the negotiations.

To avoid these things from happening, a proper preparation of the negotiation process must be done beforehand.

The negotiation process is not simple and routine communication, it involves certain preparations (cognitive, mental, psychological, ethical, etc.) of negotiator, designing a specific environment and overall atmosphere of the negotiations. This may significantly affect not only the ease of negotiations, but also their very outcome.

The results of research show that the success of a meeting is directly related to its preparation. This relation is obvious, so that for every hour of the meeting "face to face", you need to spend at least four hours preparing it. Of course, it is not just about professional and mental preparation, but also a complete environment of negotiations. It is very important that the space is adequate, clean, ventilated, sufficiently heated or cooled.

The location of negotiation is very important, too. It may be at one or the other negotiating party or at a neutral location. Every possible solution has its pros and cons.

It is believed that the party who is hosting has a slight advantage. As negotiations are conducted in its premises, it has the advantage of all the data at hand. A negotiator can use a break to consult with his/her superiors. But the other side also has certain advantages. It does not have to make the final agreement, it may seek to delay the final decision because of the need for consultations. Also, it is good for it to see the whole potential and infrastructure of the other company, which will give it a more complete idea for bargaining and the next cooperation. It is also very important to see the contacts, the credibility of a person who is participating in the negotiations. This information will be valuable for taking a position in negotiations.

To make negotiations successful, we should pay attention to the following:

Never be late for negotiations. Negotiations begin at the moment when you appear (you send the first messages by your looks, your movement, your clothes, your perfume). You don't have much time to leave a good first impression. Negotiations are based on communication (sound, words, voice, movements, body language - presentation equipment, video beam...).

Be well informed. Before negotiations, a good negotiator should gather all the necessary information on the subject of negotiations, on the other party, metaphors and quotations that can be used. The strongest weapon of negotiators are facts that are used to win the other side. Therefore, you should collect the data and store them methodically, and you should know where to look for information or data that may be needed during negotiations. Professional negotiators write down all interesting things that they notice or read every day, and at the end of the day, they arrange them. It is good to write down the thoughts that you hear during a conversation. You should make your files and archive them.

Creating trust. You should believe in yourself and have self-confidence and thus you will make others believe that you are the person to be trusted. Present yourself as a reliable, responsible, organized and efficient person who knows how to achieve your goals, but also make for others possible to achieve their. It is easy to fool someone who trusts you, which is immoral. But, usually, it can happen only once. Lost trust is difficult to regain.

Creating a sense of importance. Someone can call this praising, some flattering and some obsequiousness. You should praise other people in their presence. Find something in the other party which you truly admire and praise it to the skies. Flatter other side and entrust them to a secret to show them they are trustworthy. Mix the bitter with the sweet, because if you put a little bit of criticism with praise, it will sound more honest. Compare them with somebody better, for example, tell them they are a lot smarter than someone who has a better car or more money, etc.

Creating a relaxed atmosphere. The feeling of confidence and personal significance can lead to relaxation and pleasure. Relaxed and happy man will more easily accept the terms of the negotiations and allow you to reach your goal. Create a relaxed atmosphere. Choose a calming color of walls, soft music in the background. Your voice should be calm, comprehensible and pleasant.

For clear communication during the negotiation, try to apply some of the following tips. Let your speech be comprehensible, attractive and reliable. You should watch the other negotiator, maintain eye contact, but avoid the hypnotic stare. Avoid interrupting other negotiators, allow them to express themselves fully and freely. Then ask questions related to facts, to clarify your observation.

Analyze nonverbal signals. Do not let the voice, looks or gestures of other participants influence the content of the message. In the case of conflict of interest, keep calm, professional attitude. Always let the other participants know that their goals are important to you and that you strive to find a solution good for everybody. Your behaviour must be believable, and always acceptable.

Do not take gifts to negotiations, or if you feel the other side may be happy for them, then let it be only symbolic signs of attention. Expensive gifts can be understood as attempts at bribery, which weakens or completely hinders your negotiating position.

### ***UNETHICAL BEHAVIOUR AT NEGOTIATIONS***

In addition to the normal, ethical, professional behaviour, there is also unethical behaviour. In some cases, there is a lot of such behaviour, and sometimes it is rare. In civilized, more established, reputable environment, such behaviour is almost non-existent, and in primitive communities there is a lot of it. Sometimes even more than we can imagine and expect.

With the advent of various crises and generally turbulent business conditions, there appeared such behaviour even in some countries where it was unusual before. This also happens when there is a meeting of negotiators from different civilizations, cultures, religions, value systems.

Unethical behaviour in negotiations are manifested through various forms of the so-called "dirty" negotiating tactic. These are different forms of manipulation, bluffing, lying. There are various forms of exploitation and abuse of power, pressure, ultimatums, blackmail, creating a stalemate or different types of impediments.

It starts with creating a bad negotiating atmosphere and ends with extortion of certain demands or fulfilling some interests. This is most often achieved through one of the following forms (Petkovic, *ibid*, p. 63-65):

Creating an atmosphere of mystery and expectation. Do not let the other negotiator put you in a state of anticipation, creating an atmosphere of secrecy and mystery. Ask for an explanation of what you do not understand, even ten times if necessary. You have the right to get accurate and clear picture of what you negotiate about.

Using pressure. Pressure may be seemingly decent, and it can be rough. The most common form of pressure is force. Threatening a business partner, standing too close to his face, and other forms of force are a thing of the past. Psychological

pressure may force someone to agree to some conditions, but dominant negotiators will always look for something more. In this case, you must learn to say no, stand up to the pressure and say no, I do not accept it.

**Creating discomfort.** Discomfort is the kind of pressure which some negotiators use to force the others to promptly stop the unpleasant situation, often accepting unfavorable solutions.

**Creating anxiety.** Dissatisfaction with the opinion of others about ourselves, over-reliance on the opinion of others, fear and uncertainty can make you withdraw into yourself or start a conflict with the environment. Anxiety, as such, is fertile ground for taking control over you, in which case you lose negotiations.

**Creating the feeling of dependence.** Dependence on other people's opinion and expectations of their acceptance creates fear of the person whom we depend on, leading to uncertainty. Therefore, make a list of the people whose opinions you care about, and do not allow others to influence your mood.

**Creating fear.** Fear affects behaviour, blocking the nervous system and makes us more sensitive to other people's goals. The most common fears of negotiators are fear of oneself (of being ignorant, of not be able to understand the other side and fear of physical reactions) and fear of the other side. Fear of being ignorant starts from ignorance of the issues you negotiate. Being unprepared and lack of knowledge can lead to the fear of unknown and from the start, put a negotiator into a subordinate position.

The notion that you are in a subordinate role will block you with fear that takes control of your nervous system, and can lead to serious physical consequences, as panic attacks. Negotiation requires knowledge and constant readiness to creative improvisation in expressing ideas and thoughts. Negotiations should be planned, using notes or plan of presentation can prevent fear. A good negotiator relies on facts, good presentation, confident demeanor and proper use of voice. All this leads to self-confidence that is a prerequisite for the successful presentation of thoughts.

**Creating and encouraging aggression.** Aggressiveness in negotiations usually occurs as a result of fear and insecurity. Negotiators who have high expectations and low opportunity of exercising them, will resort to aggression to achieve their goals. It is possible that they will try to induce aggression in others in order to make them subordinate to their goals. Aggressive man may lose control and react without thinking about the consequences. And that is what your opponents want, they want you to make a decision without thinking about the consequences. If your opponents affect your behavior, they will also affect your decisions.

**Creating stress.** Stress is often a consequence of short time and set deadlines, regardless of whether you specify them or someone else imposes them on you. People who have fast pace of life become victims of pressure and they do not have enough time for all that must be done in a day. Stress also appears when the other side tries to make you think or act faster than you are capable of (insisting on quick decisions, quick change of proposals or opinions). Under such pressure, you may make wrong decisions, which is the goal of your opponent.

You should avoid stress with good self-control and using some of the relaxation techniques. You should never try to negotiate when you are tired and discouraged. Do not accept the imposed pace of negotiations if you cannot follow, but choose the pace that suits you.

## ***THE PROCESS OF NEGOTIATION***

Although a lot of different elements are present in negotiation, the key element is still speech, language, word, meaning, as means to communicate our intentions and hinder intentions of others.

If, during negotiations, you notice that respondents do not understand or do not think too much about the topic of conversation, you may use louder speech, movement and gestures to make them more observant. In case the other side is intelligent and interested in the topic, you should apply a more subtle approach, filled with, for example, humor, communication that you will convey with the appropriate tone, words and movements. If your voice is flat, without expressive and powerful tones, you will give away the impression of fear and insecurity, or even indifference. The lack of coordination between thoughts and voice makes an indecisive voice, which occurs mostly with the negotiators that are not sure what they are talking about. The cure for such things are notes, which should help the speakers establish a connection between the brain and voice.

Style of speech is a matter of personal choice of each negotiator. It involves a good knowledge of grammar, knowledge of word meaning and skill in formation of sentences. Your respondents expect of you expertise, knowledge of grammar, which is visible from the correct stacking of words in a sentence, proper separation of words and proper use of pause. Rhetorical pauses retain the attention of participants, dramatic pauses stress the importance of that part of speech, and pauses for air intake must not interfere with fluid discussion. Fast talking negotiators, who are in the habit of talking before they could think, are difficult to understand and people may get the impression that they just want to quickly wrap up the negotiations. Do not accumulate unnecessary words in the debate in order to impress others as a learned person. Some will see it as your attempt to get more time because you do not know what to say at that moment. Your speech should contain no unnecessary words, it should be clear, simple and easy to understand, but never dull.

The meaning of words. In preparing for negotiations you must be sure that you know the meaning of words you may use. Do not use Latin words to impress the other side if you did not check their meaning in a dictionary. The first time such a mistake may be taken as a cute mistake, but frequent errors could lead to negative reactions of the other side. Do not use words that, in the local vernacular, may have a different meaning (often vulgar and offensive).

Caring for the listeners. Tactics is important for a positive acceptance of your thoughts and arguments. Do not use the speeches and presentations that cannot be doubted, you could create aversion. The message will be the same, but the level of non-acceptance will be lower. Make easy for your listeners to understand your words by repeating important facts. Avoid mumbling and repeating various catchphrases like hmmm, well, you know. Use warm and gentle humor and good spirits. Speaking without listening is a one-way street. Hearing someone does not mean listening. Physical act of listening does not mean that words are understood. Sometimes the pace of listening is faster than pace of speaking, so a listener has time for his own thoughts, and sometimes the listener estimates that there is no use of listening and rather amuses him with his own thoughts.

When does not-listening occur? When your listener keeps silent and listens to you, but shows no signs of interest, does not comment on your words or ask questions.

People often listen to only what is interesting to them, and sometimes they listen to what they do not want to hear. During the debate, while listening to others, some people use that time just to clear their minds and start talking as soon as they have the chance, and sometimes they listen lurking for the wrong words of their opponents. Remember that those who do not know how to listen, cannot make others listening.

What to do when your listeners indicate that they hear you, but they are not listening to you? If they are not interested in what you are saying, change the subject. If you speak monotonously, try to sound more emotional and speak faster, and if you start repeating yourself or you speak too much about yourself, again change the subject. Turn not-listening to listening so that your listener understands your message and begins speaking and you start listening.

Show to the other speaker that you are listening by repeating and describing what he said, ask questions, try to guess his thoughts and emotions, ask for explanations of what you do not understand, and finally repeat his key thoughts and messages.

The effectiveness of listening will significantly increase if we decide in advance that we will listen, if we do not talk too much during negotiations, if we do not use silence to think, we keep eye contact, ask and repeat the main ideas, we do not interrupt speakers and avoid movements that interfere with negotiations. We should not forget that good negotiators listen carefully, and the best negotiators do not miss anything. During negotiations, we must not allow others to interrupt us with comments, but listen what we want to listen, think in advance and model our expectations to it and not let emotions put us out of balance. If necessary, check things two or more times, ask appropriate questions, so that the other speaker sees that we are interested in the solution. Only if we receive the full message, we will be able to handle it effectively. People have two ears and one mouth, so let it be the proportion in which they should be used. So, it is more important to listen than to talk.

Sense of time is an extremely important characteristic of a good negotiator. We need to know how long our speech will be before we begin to speak. Some negotiators deliberately ignore the sense of time in order to create pressure on the other side. When negotiating, you should plan no more than one quarter of the time for introduction, two quarters for the main part of negotiations, and the last quarter for conclusion. Even in negotiations that are not limited by time, you should not leave more than 10 minutes for conclusion. Always leave several safety minutes for unpredictable situations during discussion. Do not show before the other party that you are a slave to time, so as not to leave the impression that negotiations are done worrying more about the time than the other negotiator and the actual situation.

Other processes such as phonics, panting, trembling of voice, facial spasms, etc. are complex processes in which there is a series of voluntary and involuntary movements, which are not desirable. The movements that we do unconsciously (frowning, licking of lips, loud swallowing, brows lifting, twitching of lips) - reveal some of our internal states. The other negotiator will understand this as our weakness and a sign of crisis, and try to use it against us. In this regard, the extremely negative phenomena are tics - unpleasant, little, repetitive, involuntary movements.

Dressing and personal hygiene. We make our judgment about our surrounding on the basis of what we see. Although it is said that clothes do not make the man, it still says a lot about him or her.

The fact is that your satisfaction with someone's appearance will affect your opinion. And the other way round, if you make a good first impression, you are on a good way towards the successful completion of negotiations. There is no second chance to leave a good first impression. So, you should not wear brown shoes with a black or dark blue suit, checked tie with a striped shirt, white socks, cowboy hat and so on. But also, do not wear your best evening suit if you negotiate with people who can barely make ends meet, with union strikers, and so on. Although it goes without saying, it is good to be reminded on the importance of personal hygiene (clean and tidy nails, washed hair, no bad breath, neat beard and mustache, etc.), which can only contribute to your self-confidence, and with that – easier and more successful negotiation.

## ***PHASES OF NEGOTIATION***

Every day there is a growing number of participants in business processes, especially the key ones: owners, managers, entrepreneurs, advisors, etc., which puts them in a variety of negotiation situations with different participants. It is expected that they have a considerable degree of communication skills and all the other prerequisites for successful negotiation. This is the reason that modern books on this topic pay more and more attention to knowledge and skills of negotiation as

a subtle "tool for fine-tuning" of the business enterprise towards its successful realization.

So, negotiation cannot be obligation or privilege of only a few selected and certified, high-quality, experienced professionals, as it used to be. Today, the strategic emphasis is placed on managing relations with suppliers, customers, contractors, financiers, government bodies, etc. Therefore, negotiation has become a very important process that has a direct impact on the achievement of the overall business success of companies.

The important novelty in the approach to negotiation is systematics, which, among other things, means that the negotiation process is broken down into several phases: the preparation phase, the course of a negotiation and the phase of revision of a negotiation. In this way, using different techniques and resources, we try to achieve maximum possible additional value to each of negotiation activities.

The first, and, in the opinion of many scholars and practitioners, the most important phase of every negotiation process, is the preparation and planning of the negotiations. Generally, this stage is attributed to the 70 to 90% of the success of the negotiation (Tomašević-Lišanin, 2004), Negotiation - business process that gives value, "Proceedings of the Faculty of Economics in Zagreb," year 2, No. 1).

At this stage, it is necessary to identify and study the available sources of information, and based on that, determine our needs, demands and possibilities, and based on them better evaluate business partners with whom we negotiate. In this phase, we should take into account not only organizational demands, but also individual characteristics and demands of people who participate in negotiations. We should not forget that although negotiators present their organization and try to achieve specific organizational goals and needs, each of them enters negotiations as a person and an individual with their own individual needs. Both of these should be taken into account. A good analysis of needs of both sides means the ability to find a "win-win" solution that will satisfy both sides, no matter they enter negotiations because of the existence of disputes or conflicts of interest.

Prior to the commencement of negotiations, we need to determine how far we can go in giving away, i.e. what we want or can give to the other party. In addition to the established baseline, maximum, minimum and target positions, we should predict expected objectionable points that could be crucial or problematic in the way of coming to an agreement. Also, it is necessary to consider and anticipate different scenarios and alternatives, acceptable, positive outcomes. The collaborative, or "win-win" approach to negotiations, preparations should include a lot of seemingly minor issues such as the determination of location for negotiations, setting equal number of members of the negotiating team, the ambient and seating arrangements of negotiators, refreshments and short breaks, with the aim of making stimulating and pleasant atmosphere for all parties involved. In the "win-lose" approach, in preparation they usually think about various traps, the ways of expressing power, as well as the number of available manipulative techniques that will help with the attempt to put pressure and be dominant over the other side.

The second phase of negotiations is a negotiating session or meeting where two sides are trying to reach an agreement. At the beginning of the meeting it is necessary to do everything to reduce tensions and to express intent and desire for a successful outcome of the negotiations for all parties involved. A negotiating session essentially consists of the following elements: coordination and confirmation of the agenda, expressing of views on the situation, presenting concrete proposals, debate about the differences in viewpoints, arguments, discussing possible solutions, compromises and attitudes that are the subject of possible exchange, and finally negotiating the terms of exchange. When making concessions, we should always try to get the same value in return not agree on what we do not like. Otherwise, we may come out of negotiations with bad results. At the beginning of a negotiation process, we should clearly express what we want to achieve with negotiations and ask the other side to do the same. It depends on pre-approved tactics what will be presented as our wishes. It is usual not to expose immediately the desired final goal, but to start with bigger demands and thus leave some space for later concessions and negotiations.

When both sides express what they want, it is time to start with the determination of similarities and differences. To make the process of negotiating effective, it is necessary to start with solving the problems and discussing the differences. It usually starts with smaller problems and differences.

The discussion should lead to reducing the differences and preparation for making compromises. From minor differences and easily solved problems, we should go to bigger differences and larger problems and solve them patiently and slowly, one by one. It is very important that the atmosphere in the negotiations is good and that both sides are willing to make compromise and agreement. Compromise is a key part of the negotiation process, and without it there can be no agreement.

The aim of the whole process of negotiation is to reach an agreement. The agreement is finally reached when all differences are removed and all important issues are resolved. To end the process of negotiation effectively, the agreement needs to be formulated accurately and clearly and written down in a form of a contract, agreement, etc. This is especially important and necessary in larger purchases and sales, realization of major enterprises, etc. In this case, drafting of a contract requires special procedures and time for completion.

The third phase occurs only if there is a unilateral deviation from agreement of one of the negotiating parties or there appear new or changed circumstances which require new, redefined negotiations.

When concluding this review of the business negotiation as an important element of the business process, i.e. the factor of the success of a business enterprise, we should say that each business subject should see negotiation as a powerful tool, which can help to win a lot, but also lose a lot. It is always important to set clear goals, to aim high, to target the best possible result. Therefore, in addition to being clear, business objectives must also be attainable and time

determined. Also, the more we know about the other negotiator, the more we can accomplish during negotiations.

Finally, it should be noted that there is an opinion, which is empirically confirmed, that knowledge contributes 15% to the success of a negotiation, and the ability to communicate 85%. In addition, verbal communication contributes only 45%, and non-verbal communication 55%.

## ***CONCLUSION***

The entire process of the analysis shows that business negotiation is a heart of every business process. Without negotiation, any human activity would be impossible. That is why negotiation is sine qua non of every human activity and survival of society in general.

With the development of human society in economic and civilizational terms, the negotiation process becomes more complex, complicated and sophisticated. Therefore, we must constantly study, develop and improve negotiation process.

Studying and developing of the process of business negotiation must be conducted from different aspects, and above all, from technological, organizational, economic, socio-psychological and ethical aspects.

In the future, human society will primarily develop as an information society. In advanced information society, negotiation in general, and, especially, business negotiation will be faster, better, more complex, and also more humane and dignified.

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## **AMICABLE FINANCIAL RESTRUCTURING OF COMPANIES IN REPUBLIC OF SERBIA**

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### **ABSTRACT**

*Legal consequences of an amicable financial restructuring of business companies are important both for the corporate debtor and for its creditors. According to the order of creation, they can be divided into those that act independently of the outcome of the restructuring process and prior to its completion such as debts stand-by (moratorium), and those that are arising from the conclusion of the contract on financial restructuring, following the successful completion of the procedure. An effective protection measure of creditors' claims during the moratorium is limitation of powers of statutory representatives in the form of mandatory countersignature. The consequences arising from the conclusion of the contract are reflected, primarily, in redefining of debtor – creditor relations, foreseeing of repayment in instalments, modifying terms of maturity, interest rates and other terms of the loan or collaterals. An important result is the retention of the order of priority of mortgage.*

*Tax incentives for the banks and other creditors, the participants in the financial restructuring, are provided. Absolute right transfer tax was abrogated on the transfer of shares in legal entity and securities, which refers to the measures of converting receivables into capital of the business company – corporative debtor.*

*Contract on financial restructuring constitutes legal grounds for the reclassification of banks' claims, thereby reducing the mandatory reserves for the potential losses and has a positive effect on capital adequacy of the banks.*

**Key words:** *Financial Restructuring, Sebts Stand-by, Mortgage, Tax Incentives, Reclassification of Claims*

**JEL Classification:** *K12, K34, K41*

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## ***INTRODUCTION***

Amicable (out-of-court, non-insolvency) financial restructuring of a company represent first in a series of measures which are possible to conduct in relation to a company which has financial difficulties. Order of measures in such situation in our legal system is the following: amicable (out-of-court, non-insolvency) restructuring; plan of reorganization prepared in advance; bankruptcy reorganization; bankruptcy (Kozar, 2011, pp.8). These institutes, except bankruptcy, represent ways and forms of recovery of companies, which can be lead under institution of recovery which is developed for years, and now is not existent in our legal system (Mićović, 2011, pp.54).

Law on Amicable Financial Restructuring of Companies (Official Gazette of Republic of Serbia, 2011, a.18) regulates conditions and manner of amicable financial restructuring of companies in Republic of Serbia, which is conducted prior to initiating of bankruptcy proceeding at latest.

Purpose of amicable financial restructuring of companies is timely recognizing and resolving of financial difficulties and creating conditions for normal continuance of business activities of a company (corporate debtor). Amicable restructuring of activity of a company occurs in case that relevant creditors assess that survival and recovery of a company which has financial problems is economically justified and manageable, that it should be able to recover and continue sustainable long term business, and that relevant creditors, primarily banks, will be able to acquire favourable settlement of their claims. This way, a company which faces financial difficulties is granted survival and continuance of business, and at the same time the bankruptcy proceeding is avoided regardless of the fact that there is long term inability for payment as reason for bankruptcy from articles 11 and 12 of the Law on Bankruptcy Proceedings (Đukić-Mijatović, 2010).

Legal consequences of amicable financial restructuring of companies reflect in inactivity of debts, which is a result of a proceeding, and if a proceeding is completed successfully, an agreement on financial restructuring is being concluded, which defines relations between debtor and creditor.

## ***MEASURES FOR PROTECTION OF CLAIMS OF CREDITORS DURING MORATORIUM***

One of base presumptions for successful managing of amicable financial restructuring of companies is temporary suspension of obligations fulfilment, and prohibition of initiating of execution proceeding, i.e. postponement of fulfilment of obligations of corporate debtor towards creditors, primarily banks (delay of payments, moratorium) (Kozar, 2012, pp. 226). "Delay of payment" is temporary suspension of fulfilment of obligations, including suspension of execution during

enforced collection from the account of a company, and prohibition of initiating of execution proceeding, i.e. postponement of execution towards company concerning claims of creditors who participate in financial restructuring.

During financial restructuring, delay of payments (moratorium) is being established, including all executive court decisions, other executive decisions and legal authorizations, as well as tax, customs and bill of exchange debts from Article 47 of the Law on Payment Operations (Official Gazette of SRJ no. 3/2002, 5/2003, Official Gazette of RS no. 43/2004, 62/2006, 111/2009, 31/2011), which has legal effect as from the date of conclusion of an agreement on delay of payments (delay of payments is regulated by Article 12 of the Law on Amicable Financial Restructuring of Companies). Therefore, the law does not prescribe moratorium as legal consequence of process of amicable out-of-court restructuring, which would incur by operation of law, it is necessary that creditors conclude with a debtor relevant agreement.

Beside general prohibition of conducting acts which could prevent or aggravate collection of claims of creditors who concluded agreements on delay of payments, which is integral part of legal principle of acting in a good faith (Kozar, 2012), it is possible to prescribe special measures of protection of creditors' claims in the agreement on delay of payment.

Although it is non-mandatory element of an agreement, prescribed by law – Rule on Contents of the Agreement on Delay of Payments, allowing stipulation of special measures of protection of creditors' claims represents very significant instrument which contributes to reduction of business and legal risks of creditors who engage in a project of amicable financial restructuring, whose outcome cannot be predicted with certainty, with a moratorium as its mandatory phase (Kozar, 2012, pp. 619).

Measures of protection of creditors' claims include in particular: limitations and follow-up of payments, settlements of liabilities, debts and other transfers and transactions of debtors, such as prior or subsequent consent (approval or permission) or appointing a person authorized for countersigning of documents by which debtor makes monetary transactions during delay of payments, including arrangement of matter of responsibilities of this person (Article 3 paragraph 1 point 2 of the Rule on Contents of the Agreement on Delay of Payments). This way, the autonomous use of various institutes is allowed, by which creditors can control and follow business of a corporative debtor, e.g. new debts by raising loans, giving guarantees, establishing mortgages, and concluding other agreements and businesses which would, by the means of accepting new main or accessory obligations, burden assets or worsen position of creditors who participate in a process of amicable financial restructuring.

Prior or subsequent consent (approval or permission) as a measure of protection of creditors' claims from an agreement on delay of payments, has certain similarities with an institute of consent for conclusion of an agreement from Article 55 paragraph 1 of the Law on Obligations, which prescribes when a general act of the legal entity specifies and in the registry stated that his representative may

conclude certain contract only with an approval of an authority, the approval may be given previously, concurrently or subsequently, unless otherwise stated in the registry. The difference is that in the first case there is no limitation prescribed by the general act of the corporate debtor, nor to be registered at the Company Registry. Also, when it comes to restructuring the limitation refers to the corporate debtor as the legal entity, and the limitation from the Law on Obligations refers to its statutory representative. In the first case consent (approval or permission) is given by the creditors, and not debtor's authority. Therefore there is a question of scope of this limitation towards a third, conscientious person with whom the corporate debtor would conclude a contract or any other legal business on new debt, without the consent of the creditors provided by the agreement on delay of payments. In any case, such limitation should be registered so it could have the legal effect on third parties.

The appointment of the person authorized to countersign documents with which the debtor performs financial transactions during the delay of payments, as a measure of protection of creditors' claims, has greater legal and practical significance, considering that such person is obliged to deposit its signature at the bank that maintains the account of the company, and limitation of the countersign of the documents is registered at the company registry (Article 3 paragraph 2 and 3 of the Rules on Contents of the Agreement on Delay of Payments).

The Rules on Contents of the Agreement on Delay of Payments uses the term "countersignature" and this limitation ties to signing of "the documents with which the debtor performs financial transactions during the delay of payments". There is a question to which legal transactions the limitation of "countersignature" refers to. The term "financial transaction" is similar to "payment transaction" which is being used in the Law on Payment Operations, thus we come to conclusion that by agreement on delay of payments one can appoint person authorized for countersigning of payment orders, which the corporate debtor issues to its bank with instruction for transfer of funds from its account to the creditor, or to the account of the creditor ( In Article 4 paragraph 1 of the Law on Payment Operations provides that the payment transaction can be approval transfer or debit transfer, while in paragraph 3 of the same article defines that the approval transaction of the payment transactions initiated by the debtor, which payment order is issued to its bank and given instruction for transfer of funds from its account to the creditor, or to the account of the creditor.) However, since the terms "financial transactions" and "payment transactions" do not match "countersigning of the documents" as the measure for protection of creditors' claims who participate in the procedure of amicable financial restructuring, they may be applied to other legal transactions which govern or provide cash flows, and above all to conclusion of the new loan agreements, granting guarantees, the establishment of mortgage, which would worsen the positions of the creditors, the participants of the restructuring. In this way the creditors are enabled to perform direct control and influence the business of the corporate debtor, above all through substitutionary function, and indirectly to the management function.

There is a question of scope of this limitation towards a third, conscientious person with whom the corporate debtor would conclude a contract or any other legal business which performs the financial transaction, without the countersign of the person appointed by the agreement on delay of payments, when the limitation of the countersign of documents is registered at the company registry.

The Company Law (Official Gazette of RS“, no. 36/2011, 99/2011) in article 33 stipulates that the representative is obliged to act in accordance with limitations of its powers determined by the company acts or decisions of the competent company authorities (paragraph 1). Considering that the signing of the agreement on delay of payments precedes the decision of the competent company authorities, it is clear that the representative is obliged to act in accordance with limitations of its powers which are determined by the agreement on delay of payments, and with limitation of countersigning of the documents. However, the Company Law does set the rule that towards the third parties registered limitations of the powers of the representative (and thus those unregistered) have no legal effect (Vasiljević, 2011, pp.78), stipulating that the limitations to the authority of a representative cannot stand out to third parties (paragraph 2).

Exceptionally this law prescribes that the limitations of the authorisations of the representative in terms of the mandatory countersigning can be pointed out towards third parties, if they are registered in terms with the law on registration (paragraph 3), so in accordance with the Law on Procedure of Registration at the Business Registers Agency (Official Gazette of RS, no. 99/2011). This is a limitation that consists of joint closing a deal by multiple representatives and procurators (countersignature) (Vasiljević. 2011, pp. 78).

Cited provisions of the Company Law on the effects of the registered limitation of the countersignature towards the third persons, may be applied to the effect of limitation of “countersigning of documents with which the debtor performs financial transactions during the delay of payments” as the measure of protection of creditors’ claims in the procedure of amicable financial restructuring. This indicates that the “countersignature”, i.e. mandatory co-signature, is the only effective limitation of the debtor, i.e. authorisations of its representative, of course provided that it is registered at the Company Registry.

The Rules on contents of the agreements on delay of payments allow contracting other measures of protection of the creditors which are not explicitly stated in them, in accordance with the principle of freedom of contracting, which must be within the limits of the mandatory provisions, public order and good practice (The principle of the autonomy of choice from the Article 10 of the Law on Obligations).

In addition to the measures of protection of the creditors’ claims, the stated rules enable contracting additional security instruments, i.e. guarantees and warranties.

## ***THE CONTENTS OF THE AGREEMENT AND MEASURES OF FINANCIAL RESTRUCTURING***

The financial restructuring ends with the agreement on financial restructuring (Article 14 of the Law on Amicable Financial Restructuring of the Companies). The debtor is obliged to deliver the agreement on financial restructuring within the two days from the day of conclusion to the company registry for registration of the note on existence of such agreement, pursuant to the principle of legal security. The agreement on financial restructuring is being notarised at the Serbian Chamber of Commerce and recorded in a special book (according to Article 12 paragraph 2 of the Rules on terms and manner of institutional mediation in amicable financial restructuring of the companies).

The agreement on financial restructuring may contain the following measures: prediction of repayment in instalments, amendment of maturities, interest rates or other terms of the loans, credits or other claims or security instruments; encashment of the assets or transfer of such assets for the purpose of settling the claims; discharge of the debt; execution, amendment or waiver of the lien; giving additional security instruments by the debtor or third parties, including granting warranties and guaranties; converting claims into capital; conclusion of the loan agreement; issuance of the securities; other measures significant for realisation of the financial restructuring.

Therefore, the law does not prescribe mandatory contents of the agreement on financial restructuring, but lists the most often measures as an example, and allows the possibility to contract other measures significant for realisation of the financial restructuring.

The listed measures of the amicable financial restructuring are similar to the measures within the homonymous institute of the privatisation process (Kozar, 2008, pp. 64-70), as to the measures for realisation of the plan on reorganisation from Article 157 of the Law on Bankruptcy.

## ***LEGAL NATURE OF THE AGREEMENT ON FINANCIAL RESTRUCTURING AND EFFECT OF THE INNOVATION TO THE TERMINATION OF THE PLEDGE***

By its legal nature, and depending on the measures envisaged for the realisation of the financial restructuring, the agreement has legal nature of a settlement from the Article 1089 of the Law on Obligations (e.g. if it provides repayment in instalments) or innovation from the Article 348 paragraph 1 of the Law on Obligations, if the existing obligations are replaced by new ones (e.g. if there is a conversion – conversion of claims into capital) (Kozar, 2011, pp. 56).

In addition, it is possible to combine settlement and innovation, because by settlement one can perform innovation of the obligation, and in such case the guarantor is freed from liability for its fulfilment, and the pledge given by a third party ceases (Article 1095 paragraph 1 of the Law on Obligations). If by a settlement where was no innovation of the obligation (such as e.g. partial discharge of the debt or repayment in instalments), the guarantor and third party who gave its thing to a pledge remain still bound, and their liability can be reduced by settlement, but not increased, except if they have agreed with the settlement (Article 1095 paragraph 2 of the Law on Obligations).

However, when it comes to the effect of the innovation to the termination of the pledge in general, even the pledge given by a third party, and not the debtor of the secured claim, the Law on Amicable Financial Restructuring of the Companies in article 15 makes a significant exception in relation to the cited general rule of the obligation law by establishing the rule of continuity of the lien, and as it is in the case of the mortgage, so when the claim is secured by a pledge on movables and rights (Kozar, 2012, pp. 236-250).

### ***SUBSTITUTE OF THE “SECURED CLAIM WHICH IS BEING RESTRUCTURED” “BY A RESTRUCTURED SECURED CLAIM”***

The Law on Amicable Financial Restructuring of the Companies distinguishes two types of the claims: “secured claim which is being restructured” and “restructured secured claim”. Even though the used terminology may lead us to think that it is a play on words, it is important to distinguish the difference between these terms and two types of claims which are marked by them. For “secured claim which is being restructured” is replaced by “restructured secured claim”. In this way the legislator gave the restructuring unambiguously legal nature of the innovation, because one claim which existed between the creditor and the debtor is now replaced by new claim (Kozar, 2011, pp. 59), which corresponds to the definition of the innovation from the Article 348 paragraph 1 of the Law on Obligations which regulates substitution (innovation) by prescribing that the

obligation ceases if the creditor and the debtor agree to replace the existing obligation with a new one and if new obligation has different subject or different legal grounds. Article 350 of the same law, within the regulation of the effects of the substitution, in paragraph 1 it is prescribed that by an agreement on substitution the earlier obligation ceases and a new one comes into being, and in paragraph 2 that with previous obligation the pledge and warranty also cease, unless the guarantor or pledger agreed otherwise, and in paragraph 3 the same goes for all other secondary rights that were related to the previous obligation.

In order to avoid the stated unfavourable effect of the substitution (innovation) in the financial restructuring to the security instruments, which would come to occur according to the cited general provisions of the Law on Obligations, unless otherwise was agreed with the pledger that with previous obligation do not cease pledge or warranty, the Law on Amicable Financial Restructuring of the Companies establishes continuity of the lien. The claim which is being restructured and which is secured by a mortgage, i.e. lien on movables and rights (hereinafter referred to as: a secured claim which is being restructured), is replaced by a restructured secured claim, to that the mortgage, i.e. lien on movables and rights, as secondary right related to the secured claim which is being restructured, continues to exist as the security instrument of a restructured claim, in accordance with the agreement on financial restructuring (Kozar, 2012, pp. 236-250). Real estate cadastre, or other registry of lien, performs the amendment of the data of registered mortgage, i.e. lien on movables and rights, according to the amount of the restructured secured claim, and other terms of the restructured secured claim. The mortgage, i.e. lien on movables and rights, represents a security instrument of restructured secured claim to the amount of secured claim which is being restructured, and in case that the amount of restructured secured claim is reduced in relation to the amount of the secured claim which is being restructured, the real estate cadastre, or other registry of lien performs the amendment of the data of a registered mortgage, i.e. lien on movables and rights.

### ***KEEPING THE ORDER OF PRIORITY – CONTINUITY OF LIEN***

Considering that in the amicable financial restructuring of the companies several creditors, above all banks, simultaneously conclude with a company as debtor agreement on debt restructuring, which implies redefinition of the debtor-creditor relations between the corporate debtor and creditors, this agreement replaces the existing obligation with a new one, which, accordingly, has a new, i.e. different legal ground. In terms of the mortgage, and in accordance with provisions of the Law on Obligations, the Law on Mortgage and Law on State Survey and Cadastre, as well as accompanying by-law regulations, due to this substitution of the obligation, the creditor whose claim is secured by a mortgage, in lack of stated special provisions on continuity of lien from the Law on Amicable Financial Restructuring of the Companies, would be forced to re-register the mortgage in the

public records, which would make him lose the order of priority of already registered mortgage. Having in mind a greater number and difference (often and conflict) of interest of creditors, in practice it is rarely contracted the ability to keep the existing mortgage in case of substitutions (innovations), in terms of the article 350 paragraph 2 of the Law on Obligations. The same problem would exist in relation to the liens on movables and rights. Because of all this, the creditors, and especially banks, would be discouraged to participate in amicable corporate restructuring of debts, which would lead to bankruptcy of many companies and other forms of businesses, which could financially recover and continue business, and which could end in bankruptcy and discontinuance of business.

In addition, the costs of establishment of new mortgage are additional demotivating factor for creditors, especially having in mind provisions of tariff number 8 item 15 of the Tariff of fees for service provision, which is an accompanying part of Rules of the amount of fees for service provision of the Republic geodetic authority, in which it is prescribed that for registration of the mortgage the fee is paid, which depending from the amount of secured claim, amounts from 20,000 up to 150,000 dinars. However, in tariff number 21 it is prescribed that for the change of data in registered mortgage (creditor, debtor, repayment period, interest rate, grace period, currency) fee in the amount of 2,600 dinars is paid. In this way significantly lower fee is prescribed for service of change of data of registered mortgage, and established the “change of data in registered mortgage” as a procedure, i.e. process operation.

## ***TAX INCENTIVES***

The Law on Amicable Financial Restructuring of the Companies does not contain specific provisions on incentives in the process of financial restructuring, but points to other legislation, which proposing and passing is in the jurisdiction of the National Bank of Serbia, the Ministry of Finance and the Ministry of Economy and Regional Development (Kozar, 2012, pp. 85-90). The tax incentives for financial restructuring, in terms of tax exemption of debt discharge with the creditors, and possibilities of reprogramming of debt based on taxes and other public revenues, are determined by law which regulates tax on corporate profit, i.e. law which regulates tax procedure and tax administration, while the National Bank of Serbia in regulations from its jurisdiction regulates incentives for financial restructuring (Article 16 of the Law on Amicable Financial Restructuring of the Companies).

Amendments to the Law on Property Tax from 2009 (Article 8 of the Law on amendments and supplements of the Law on Property Tax, Official Gazette of RS, no. 5/2009) deleted item 3 in article 23 paragraph 1 of the basic legal text, which provided that the tax on transfer of absolute rights is payable during the transfer with compensation of the share in the legal entity and securities. Thusly measures of conversion (replacement) of claims in the company’s capital (the corporative

debtor) were exempt from this type of tax, which represents significant incentive for amicable financial restructuring of the companies, and for bankruptcy reorganisation (Kozar et al., 2013, pp. 267). Such solution was maintained even after the latest legislative amendments from May 29<sup>th</sup> 2013.

Also, amendments and supplements of the Law on Corporate Income Tax, which is now called Law on Profit of Legal Persons amended Article 22a paragraph 1 so that at the expense of expenditures in the tax balance of a bank an increase of adjustment of claims of balance sheet assets and reserve for losses on off-balance sheet items are recognised, which are in accordance with internal acts of a bank stated in the balance sheet at the expense of expenditures in the tax period, up to the amount determined in accordance with regulations of the National Bank of Serbia, which provides tax incentives for banks as creditors of a corporate company with financial difficulties.

Regarding the process tax law, amendments and supplements of the Law on Tax Procedure and Tax Administration provide incentives for amicable financial restructuring, so that by added Article 74b it is prescribed that the competent authority may, upon written and reasoned request of the taxpayer who had concluded an agreement on financial restructuring, in accordance with the law that regulates amicable financial restructuring of the companies, approve delay of payments of tax debt in equal instalments up to 60 months, with possibility of using delay of payments for the first 12 months. Approval of the delay of payments of tax debt terminates the statute of limitations for collection of the tax debt whose deadline was postponed, and time for which the delay of payment was approved does not count into the statute of limitations, which means that in that period there is a delay of statute of limitations. Minister or person authorised by him decides on delay of payment of tax debt – based on written proposal of the head of the organisation of the Tax Administration based on the principal place of business, i.e. place of residence of the taxpayer – except for the source public revenues of the local government units, when the decision is brought by the mayor or the municipal president or person authorised by him, the local government units to which the public revenues belong to whose collection is being delayed (Article 73 paragraph 3).

In this way, through delay and enabling the payment of the tax debt in instalments, with grace period of 12 months, the same tax incentive was introduced for amicable financial restructuring, which in the previous legal amendment was provided in the procedure of the bankruptcy reorganisation. Additional benefit for taxpayers who conclude the agreement on financial restructuring is that it does not require provision of the security instruments when the amount of debt whose payment is delayed up to 500,000 dinars (Article 74b paragraph 2 regarding the article 74 paragraph 6 of the Law on Tax Procedure and Tax Administration).

## ***RECLASSIFICATION OF THE RESTRUCTURED BANKS' CLAIMS***

New Decision on Classification of the Bank Balance Sheets Assets and Off-Balance Sheet Items (Official Gazette of RS, no. 94/2011, 57/2012, 123/2012, 43/2013, 113/2013), and especially its amendments from December 2012 envisaged incentives for *reclassification* of banks' claims based on concluded agreement on financial restructuring.

The said decision determines which balance sheet assets and off-balance sheet items are classified, criteria for classification of the banks' claims, and the manner of calculation of reserves for estimated losses which may arise based on the bank's claims, and for adequate and efficient management of the credit risk to which the bank is exposed in its business (item 1). The bank's claims are classified into categories A, B, V, G and D, according to the criteria for classification described in item 20. Into the most favourable category A stand classified claims from debtors with whom, based on the estimate of the financial status or creditworthiness, no problems are expected, then claims secured by first-class security instruments (cash deposit, pledge on gold along with fulfilment of some other conditions) and claims according to which the debtor settles its obligations timely or is overdue no longer than 30 days. In the most unfavourable category D stand classified claims from debtors in liquidation or bankruptcy, then claims from debtors who do not act according to the adopted plan of reorganisation, and claims according to which the debtor is overdue longer than 180 days and similar.

Reserve for estimated losses is calculated on the gross carrying amount of the claim, depending on the classification of the claim (item 34), and from 0% of the claims classified into category A, 2% of the claims classified into category B, 15% of the claims classified into category V, -30% of the claims classified into category G and 100% of the claims classified into category D. Therefore, mandatory reserve for estimated losses ranges from 0% up to 100% of the claims, depending on the classification. The more favourable classification of the claim, the lower mandatory reserve for estimated losses is, which represents deductible item from the banks' capital (The amount of the required for estimated losses per balance sheet assets and off-balance sheet items is deductible from the basic capital – item 12 paragraph 1 under 6 in relation to the paragraph 3 under 4 of the Decision on the Adequacy of the Capital of Banks, Official Gazette of RS, no. 46/2011, 6/2013 and 51/2014) and affects adversely the adequacy of the bank's capital. The bank is obliged to maintain a prescribed amount of capital for the sake of stable and safe business, or fulfilment of the obligations towards the creditors, in the amount not lower than the dinar equivalent of 10,000,000 euros. Capital adequacy indicator represents ration between capital and risk-weighted assets. The National Bank of Serbia prescribes the manner of calculation of capital and adequacy of the bank capital (Article 21 paragraphs 1 and 3, Article 22 paragraph 1 and Article 23 paragraph 2 of the Law on Banks, Official Gazette of RS, no. 107/2005, 91/2010).

Therefore, concluded agreement on financial restructuring is a basis for more favourable *reclassification* of the banks' claims, because delay is calculated to subsequently agreed maturity date, and thusly accomplish more favourable classification of the claim which is being restructured, or restructured claim. Item 23 paragraph 4 of the Decision on Classification of Bank Balance Sheet Assets and Off-Balance Sheet Items it is provided that the provisions of paragraph 1 and 2 of this item, which regulate calculation of the delay in payments according to the original maturity date, are not applied to the restructured claims or to the restructured claims which are restructured for the second time, only if the second restructuring is made in accordance with the law which regulates amicable financial restructuring of the companies, under the condition that the debtor, for at least three months, i.e. three consecutive months made the payments according to the agreed plan of repayment of its debt with delay no longer than 30 days. In order to literally apply the cited provision, it would be desirable to provide in the agreement on financial restructuring that the debtor in the first three months pays a smaller part of the debt at once or in three instalments.

If the said conditions are met, the delay in collection of restructured claims is calculated according to the subsequently agreed maturity date, which means that according to the amended maturity dates from the concluded agreement on financial restructuring.

This way the claim based on which the debtor was in delay longer than 180 days, and which was classified into the most unfavourable category D, based on the agreement on financial restructuring is reclassified into one of more favourable categories with far lower rate of calculation of the reserve for estimated losses.

Mortgage on real estate is considered an adequate security instrument, in terms of the item 29 of the Decision on Classification of Bank Balance Sheet Assets and Off-Balance Items only under the condition that the debtor settles the claims secured by this mortgage with delay no longer than 720 days, or that the debtor is not in bankruptcy, i.e. acts in accordance with the adopted plan of reorganisation in terms of the law which regulates bankruptcy. The bank's claims secured by adequate security instruments can be classified into one category more favourable than one in which it would be classified. That means that in case of delay in payment of the claim secured by mortgage, which is longer than 720 days, the claim is classified into the most unfavourable category D, with obligation of calculation of the reserve for estimated losses from 100% of claims. The same situation occurs when the debtor is in bankruptcy or if the debtor does not act in accordance with the adopted plan or reorganisation. The obligation of reservation is increased for 70% of claim secured by mortgage, in relation to the category G, for which the prescribed rate is 30%.

The conclusion of the agreement on financial restructuring with repayment in instalments, amended maturity dates, interest rates or other loan terms, at the same time eliminates permanent inability to pay as the reason for bankruptcy from Articles 11-12 of the Law on Bankruptcy, and thusly the opening of bankruptcy proceeding over the debtor, which represents a criteria for classification of bank's

claims into the most unfavourable category D with obligation of calculation of the reserve for estimated losses to 100% of the claim.

This way the company in financial difficulties is enabled to survive and continue business, bankruptcy is avoided, and banks as key creditors are given incentives in terms of the more favourable classification of the claim and lower obligation of the calculation of the reserve.

In item 2 paragraph 2 the definition of “restructured claim” is given so that it is prescribed that by restructured claim, in terms of this decision, it is considered a claim regulated by the agreement which redefines debtor-creditor relations of the bank and debtor due to his financial difficulties. In addition, this agreement must fulfil three cumulative conditions, namely: 1. that it replaces all balance sheet claims from the debtor, or their greater part, 2. that it substantially changes terms under which this claim is approved (under which it is especially considered prolongation of the term for repayment of the principal or interest, reduction of the interest rate or amount of the claim, substitution of the fulfilment, as well as other changes of conditions which facilitate debtor’s position) and 3. that adequate program of financial consolidation of the debtor is adopted simultaneously. In case of debtor who is a natural person – that the bank, based on creditworthiness of the debtor, estimated that the debtor is able to settle its obligations towards the bank regularly in the following period, reduced the amount of the claims for the amount of deposit placed in the name of securing claims in case that this deposit is placed and contracted that the debtor after performed restructuring shall not be further indebted.

Therefore, the stated three conditions must be cumulatively fulfilled in order for the agreement on financial restructuring from Article 14 of the Law on Amicable Financial Restructuring of the Companies represent valid legal basis for reclassification of claims which is regulated by it, by redefining debtor-creditor relations between bank and debtor, and thusly considered restructured claim in terms of the Decision on Classification of the Bank Balance Sheet Assets and Off-Balance Items (Kozar, 2011, pp. 66).

If the restructuring satisfies only the conditions from the Decision on Classification of the Bank Balance Sheet Assets and Off-Balance Items, and at the same time does not represent the financial restructuring in terms of the Law on Amicable Financial Restructuring of the Companies, e.g. if at least two domestic or foreign banks as creditors participate in it, then for securement of restructured claim it is necessary to register new mortgage, considering that restructured claim is defined as new claim (which replaces all balance sheet claims from the debtor, or their greater part), and by that new mortgage ensure redefined bank’s claim (Standpoint of the Legal Affairs Committee of the Association of Serbian Banks from June 20<sup>th</sup>, 2011).

## CONCLUSION

Purpose of amicable financial restructuring is to timely recognize and resolve financial difficulties and to create conditions for normal continuance of company's business (corporative debtor) if relevant creditors assess that existence and recovery of a company which has financial difficulties economically justified and doable.

One of basic assumptions of successful implementation of amicable financial restructuring of companies is delay of payments (moratorium). Allowing to contract special measures of protection of creditors' claims is very important instrument which contributes to decrease of business and legal risks of creditors who engage into amicable financial restructuring, result of which cannot be foreseen with certainty, and moratorium is its mandatory phase. Appointing a person authorized for countersigning of acts by which a debtor performs monetary transactions during moratorium, as measure for protection of creditors' claims, is of a greater legal and practical significance, since this person is obliged to deposit his signature in a bank where a company's account is, and limitation of countersigning of act is being registered in business companies register.

Financial restructuring is completed by an agreement on financial restructuring. Law does not prescribe mandatory content of an agreement on financial restructuring, but indicates most common measures, the most significant of which are: payment in installments, amendment of due dates and interest rates, release of debt, conversion of claim into capital, and also allows possibility to contract other measures which are significant for realization of financial restructuring.

This agreement's legal nature is settlement (e.g. if prescribes payment in installments) or novation in case that current obligations are replaced by new ones (e.g. if conversion is made – transforming claims into capital). Besides this, combination of settlement and novation is also possible. Secured claim which is being restructured is replaced by restructured secured claim. Legislator has indisputably given to the restructuring a legal nature of novation, because one claim, which is existent between creditor and debtor, is now replaced with new claim, which corresponds to definition of novation. Continuance of a lien is established, so that a mortgage, i.e. lien on movables and rights, as secondary right in connection with secured claim which is being restructured, continues to exist as mean of security of restructured claim, in line with the agreement on financial restructuring.

Tax incentives for financial restructuring, in the sense of tax exemption of debt release with creditors, as well as possibility of debt reprogramming on the basis of tax and other public revenues, are prescribed by the Law on income tax of companies, i.e. Law on tax procedure and tax administration. Also, in new Decision on classification of balance assets and non-balance bank items, and especially their novels from December, incentives for *reclassification* of claims of

banks based on concluded agreement on financial restructuring have been prescribed. Based on analysis of said regulations it can be concluded that in Republic of Serbia, a solid legal frame for amicable restructuring of companies has been created, which is used in practice unjustifiably rare because of inaction of companies, primarily banks as major creditors.

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# **THE ADOPTION OF OPEN INNOVATION PRACTICES IN SERBIAN ICT INDUSTRY**

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## **ABSTRACT**

*The main aim of this paper is to present the adoption of open innovation concept in information and communication technology industry (ICT), and to analyze key practices, strategic motives and concerns with its implementation based on case study of Serbian ICT industry. The main reason for conducting research in ICT industry is that Serbian ICT companies have understood best that competition is no longer based on traditional resources, combining raw materials, labor and capital, but that the competitive advantage is based on knowledge and innovation. Also, many authors argue that knowledge-intensive industries are incubators for innovation, and that open innovation practices are the most advanced in high-technology industries. Our starting research questions were: 1) What are the key practices of open innovation in Serbian ICT companies?, 2) What are the strategic motives for engaging in open innovation practices?, 3) Which partners are shown to be of the most importance in open innovation activities?, and 4) What are the key concerns of companies when engaging in open innovation practices. At first, we used desk-based research to analyze the open innovation literature including academic publications, government reports and news articles, and after that we designed a questionnaire in order to gather qualitative empirical data about open innovation practices in Serbian ICT companies.*

**Key words:** *Open Innovation Concept, Open Innovation Practices, Information and Communication Technology Industry*

**JEL Classification:** *O31, O32, M15*

**UDK:** *005.591.6:[004:007 005.591.6:654*

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## ***INTRODUCTION***

The environment of organizations has significantly changed comparing to their surroundings few decades ago, challenging managers to achieve flexibility, innovation and collaboration with others as factors that will guide towards a long-term competitive advantage. Managers are aware that organizations cannot deal with business using old routines, nor efficiently manage everything under their own roof. In past, collaboration among partners is used as transitive step to enter to new markets, reduce risks, share the costs of research and development (R&D) activities (Porter, 1986), while today collaboration and partnership represent the key components of corporate strategy (Koput, Powell, 2004). To achieve and sustain competitive advantage in global economy, the need for collaboration with various organizations, regardless of factors such as time, space and culture is of tremendous importance (Mankin et al., 2004). Many organizations have shifted their activities toward external sources of knowledge, developing more extensive relationships with universities, public research organizations, customers, external consultants, suppliers, manufacturers, and even competitors. In 2003, Henry Chesbrough introduced open innovation concept and defined it as “the use of purposive inflows and outflows of knowledge to accelerate internal innovation, and expand the markets for external use of innovation, respectively” (Chesbrough, 2003, p. 1). Many organizations have recognized superiority of tearing traditional boundaries (which lead to extensive separation of people and business processes) down and collaborating with others striving for constant innovation, improvement, quality, learning, new technology, new markets.

The aim of this paper is to examine the practices of open innovation in Serbian information and communication technology industry. At first, we used desk-based research to analyze the open innovation literature including academic publications, government reports and news articles, and after that we designed a questionnaire in order to gather qualitative empirical data about: general information about companies - age, number of employees, key characteristics in conducting their businesses; the key practices of open innovation in Serbian ICT companies; strategic motives for engaging in open innovation activities; the satisfaction with individual partners in open innovation practices; and the key concerns of engaging in open innovation activities.

## ***THE EVOLUTION OF OPEN INNOVATION CONCEPT***

Innovating in today's environment characterized with hyper-competition, increased technological advances, greater mobility of human capital requires from companies to tear down their traditional boundaries and collaborate with other organizations and individuals. Companies realized that creating organizational unit for research and development (R&D) and forming cross-functional teams cannot be stimulus for radical innovations and competitive advantage in the 21<sup>st</sup> century, and that the locus of innovation is placed beyond their own roof. The concept of open innovation points out that the purposive inflows and outflows of knowledge can be used to accelerate internal innovation, and expand markets for external use of innovation (Chesbrough et al., 2006) reducing the cost of innovation, sharing the risks and rewards of innovation, and accelerating the time required to deliver innovations to the market (Chesbrough, 2007). Regarding to traditional, closed innovation concept, there are clear differences which are summarized in table 1.

*Table 1: Closed versus open innovation concept*

<b>Closed Innovation</b>	<b>Open Innovation</b>
A company should hire the best and smartest people	A company does not need to employ all the smart people, but rather work with them inside and outside the firm
Profiting from innovative efforts requires a company to discover, develop and market everything itself	Internal innovation activities are needed to claim some of the significant value which can be created by external innovation efforts
Being first to market requires that research discoveries originate within the own company	In order to win the competition, it is more important to have the better business model than getting to market first
Being first to market also ensures that the firm will win the competition	Winning the competition does not require coming up with the best and most ideas, but to make the best use of internal and external ideas
Leading the industry in R&D investments results in coming up with the best and most ideas and eventually in winning the competition	Proactive intellectual property (IP) management allows other companies to use the companies' IP. It also considers to buy other companies' IP whenever it advances the own business model

*Source: Adapted from Chesbrough, 2003*

Many of the terms like collective, distributed, cumulative, democratized innovation are focused only on users and thus make just the part of a broader phenomenon – open innovation. Open innovation, beside customers and consumers involves the collaboration with manufacturers, suppliers, universities, public research agencies, and even competitors.

Innovations will need to be aware of and solve many societal challenges in domains such as climate change, sustainability, healthcare, youth unemployment, financial stability, and to ensure benefits for whole society with improved quality of life, and new jobs and services. Thus, the concept of open innovation 2.0 was promoted as new innovation paradigm based on principles of integrated collaboration, co-created shared value, cultivated innovation ecosystems, unleashed exponential technologies, and extraordinarily rapid adoption (Curley, Salmelin, 2013, p. 2). The aim of open innovation 2.0 is to, by tearing down all barriers among public/government, academic, business sector and citizens, create shared value, sustainable prosperity and improvements in human well-being (Curley, Salmelin, 2013). In open innovation 2.0 the citizens are recognized as very important for innovation, so the Triple Helix model has become Quadruple Helix model of innovation which encompasses public/government, academic, business sector, and citizens (Helms, Heilesen, 2011).

The key idea of open innovation 2.0 lies in the concept of shared value which can be defined as set of “policies and operating practices that enhance the competitiveness of a company while simultaneously advancing the economic and social conditions in the communities in which it operates” (Porter, Kramer, 2011, p. 6). In practice, there are three key ways in which companies can create shared value opportunities: by reanalyzing products and markets, redefining productivity in the value chain, and enabling local cluster development (Porter, Kramer, 2011).

### ***OPEN INNOVATION PRACTICES AND TRENDS***

Companies can employ a variety of practices to make use of external and internal knowledge innovation. Generally, there are two directions (Chesbrough, Brunswicker, 2014): one, where external knowledge flows into the company (inbound practices), and other, where knowledge flows out of the company (outbound practices).

Table 2: *Open innovation practices*

<b>Inbound Practices</b>	<b>Outbound Practices</b>
<ul style="list-style-type: none"> <li>• Consumer and customer co-creation</li> <li>• Information networking</li> <li>• University research grants</li> <li>• Publicly funded R&amp;D consortia</li> <li>• Contracting with external R&amp;D service providers</li> <li>• Idea and start-up competitions</li> <li>• Intellectual property in-licensing</li> <li>• Supplier innovation awards</li> <li>• Crowdsourcing</li> <li>• Specialized services from open innovation intermediaries</li> </ul>	<ul style="list-style-type: none"> <li>• Joint venture activities with external partners</li> <li>• Selling of market-ready products</li> <li>• Participation in public standardization</li> <li>• Corporate business incubation and venturing</li> <li>• Intellectual property out-licensing and patent selling</li> <li>• Donations to commons or nonprofits</li> <li>• Spinoffs</li> </ul>

*Source: Adapted from Chesbrough and Brunswicker, 2014*

Open innovation is going to be of great importance for innovation management in corporate practice. Regarding previous research and practice of open innovation, some trends can be identified (Gassmann et al., 2010):

- Industry penetration: from pioneers to mainstream. The principle of open innovation has penetrated pioneering industries such as software, electronics, telecom, pharmacy and biotech.
- R&D intensity: from high to low tech. It can be identified new trend for the low-tech sector to exploit the potentials of opening up their innovation processes. Open innovation's principles have spread to different sectors (machinery, medical tools, fast moving consumer goods, food, logistics), not only in high tech.
- Size: from large firms to small and medium firms. Smaller and medium-sized firms are also opening up their innovation processes.
- Processes: (1) from stage gate to probe-and-learn (highly structured stage-gate process is becoming more interactive probe-and-learn process); 2) from amateurs to professionals (industry is starting to professionalize the internal processes to manage open innovation more effectively and efficiently).
- Structure: from standalone to alliances. It can be identified trend from strong R&D partnership and alliances toward inter-organizational relationships.
- Universities: from ivory towers to knowledge brokers.
- Content: from products to services. The service sector is still underdeveloped in terms of the innovation process.
- Intellectual property: from protection to a tradable good. Companies buy intellectual property - mostly from universities and high-tech ventures and leverage its value through professional management.

Companies must be aware that too much openness can negatively impact their long-term innovation success because they lose control, but on the other hand, without open innovation approach they cannot achieve shorter innovation cycles and reduced time and risk to market. Without cooperation and exchange of knowledge, companies are losing their knowledge base on a long-term basis. It is important for companies to create successful products and services using open innovation philosophy faster than their competitor and at the same time to foster the building of core competencies and protect their intellectual property (Enkel et al., 2009).

### ***EXAMPLES OF OPEN INNOVATION PRACTICES IN ICT INDUSTRY***

Regarding key characteristics of information and communication technologies: enabling better connection between different organizations and partners, establishing and maintaining business-to-business relationships, communication and coordination (Petković et al., 2014), they are one of the key factors that enable pursuing of open innovation activities (Dodgson et al., 2006).

Information and communication technologies provide large amount of real-time data which are simply and faster available (Lukić, 2014a), they facilitate the exchange of ideas and information moving them from one place to another (Zuboff, 1988), and the flow of information through space is enabled, accelerating life beyond the conceivable boundaries (Lukić, 2014b). Advances in ICT “brought the firm to the world, but they also brought the world to the firm” (Walsh et al., 2006, p. 665). Many innovation technologies are specially developed for creating innovation including a wide range of design, simulation, modeling, and visualization technologies, which are increasingly used in innovation processes (Dodgson et al., 2006).

It is clear that in the 21<sup>st</sup> century, ICT represents the key enabling factor for conducting open innovation activities. Many authors argue that open innovation practices are the most advanced in high-technology industries (Chiaroni et al., 2011) and that they are fertile ground for innovation (Fjeldstad et al., 2012).

Practices and maturity of open innovation concept varies by industry. Clear example is status of open innovation in ICT, pharmaceuticals and fast-moving consumer good (FMCG) industry, where open innovation practices are necessary for survival (Golightly, 2012, p. 36).

Table 3: Different sectors and open innovation concept

Industry	Status of open innovation	Drivers of open innovation	Sector characteristics
ICT	Open innovation maturity is high. Innovation in products and processes is usually very high, and moves quickly.	Rapid growth of start-ups, disruption of business and technology, mobile computing.	Very high customer demand, technology innovation by small and medium companies and start-ups.
Pharmacy	Shift from the “chemical paradigm” to the search for innovative therapies requiring mixed disciplines and integration of technologies.	Regulatory pressure, time pressure to bring drug to market, and cost reduction are drivers for innovation.	Driven by incremental and radical innovation where the product and process innovation takes more time than other market sectors.
FMCG	Open innovation maturity is high due to continuous incremental innovation.	Competition is high and the market is very demanding. Short life of products, rapidly moving market and customer needs.	Consumer demand is high. Markets move very quickly, hence product innovation is very high.

Source: Adapted from Golightly J. et al., 2012, p. 35

ICT industry is at the top according to adoption of open innovation practices. In continuation of this paper, we are going to present some of the key examples of open innovations in ICT industry.

The Internet has facilitated mass collaboration as one of the form of open innovation where anyone can participate electronically to solve some problem or challenge, or to give some contribution. Among the best known examples of mass collaboration as one of the practices of open innovation is well-known Wikipedia. Wikipedia represents an online encyclopedia created in 2001 with aim to give a free knowledge to everyone in the world in their native language. As of August 2014, Wikipedia includes over 32.7 million freely usable articles in 287 languages that have been written by over 47 million registered users and numerous contributors worldwide. On average, Wikipedia receives a total of 10 billion global page views from around 495 million unique visitors every month, including 85 million global page views every day ([http://en.wikipedia.org/wiki/History\\_of\\_Wikipedia](http://en.wikipedia.org/wiki/History_of_Wikipedia)).

Among many examples, it is interesting to mention CAS, market-leader in the customer relations management (CRM) software for small and medium companies in Germany, which was founded in 1986 with the aim to achieve a high degree of innovation. Annually, the company spends about 30% of its revenues in research and development. Nowadays, CAS defines itself as a networked enterprise and as an open innovator (Brunswicker, Ehrenmann, 2013). CAS has designed business

model based on principles of modularity – an integrated software system embedding different applications and services in collaboration with over 200 partners in more than 24 countries. The results of CAS commitment to its customers, suppliers, competitors, intermediaries are reflected in fact that more than 200.000 people in more than 7.500 companies and organizations are using CAS software solutions (Brunswicker, Ehrenmann, 2013).

Over the last 20 years collaboration between firms, suppliers and customers has produced open source products such as Linux operating system, Firefox web browser, Apache web server, etc. (West,Gallagher, 2006).

Open source software includes source code which can be modified by geographically dispersed programmers which collaborate using virtual collaboration tools, while at the same time acknowledge the original author's contribution (Raymond, 2004). The first question that we think of is what motivates individuals to contribute to open source projects? The answer can be found in two different types of motivation (Ryan,Deci, 2000):

- Intrinsic rewards include the enjoyment of creating something new, the stimulation of an intellectual challenge;
- Extrinsic rewards include enhanced reputation, the signalling of technical challenges to potential employers and venture capitalists.

*Table 4: Open source approaches, types and results of open innovation*

<b>Approach to open innovation</b>	<b>Types</b>	<b>Results</b>
Structural approaches	Pooled R&D	<ul style="list-style-type: none"> <li>• Linux</li> <li>• Mozilla</li> </ul>
	Spinouts	<ul style="list-style-type: none"> <li>• Jikes</li> <li>• Eclipse</li> <li>• Beehive</li> </ul>
Product centric approaches	Selling Complements	<ul style="list-style-type: none"> <li>• Apache</li> <li>• KDE</li> <li>• Darwin</li> </ul>
	Donated Complements	<ul style="list-style-type: none"> <li>• Avalanche</li> <li>• PC Game „Mods“</li> </ul>

*Source: Adapted from West and Gallagher, 2006*

## ***KEY CHARACTERISTICS OF SERBIAN ICT INDUSTRY***

Serbian ICT industry is an important exporter with rising tendency of software export: in 2011, the software export amounted to 166 million euros, while in 2012 it exceeded 200 million euros ([www.pks.rs](http://www.pks.rs)), and in daily jargon it can be heard that Serbia is "the country of farmers and IT specialists" ([www.rtv.rs](http://www.rtv.rs)). Programming and computer services dominate in the structure of export of computer and information services, followed by embedded systems and system integration ([www.pks.rs](http://www.pks.rs)).

Serbian ICT industry has understood best that competition is no longer based on traditional resources, combining raw materials, labor and capital, but that the competitive advantage is based on knowledge. It contributes to affirmation of a cluster. Vojvodina ICT Cluster (VOICT), Nis Cluster of Advanced Technologies (NiCat), ICT Network Serbia Cluster (ICT Net), integrate companies in this industry, scientific-research institutes and supporting institutions. Financial data for 2010 show that one of the highest turnover is made by the member of two ICT clusters (from ICT NET with around 87 million euros, and from Vojvodina ICT with 44 million euros) (Mijačić, 2011, p. 32).

ICT industry contributes to balanced regional development. Comtrade' software development center has opened in Kragujevac, where is employed 200 IT engineers, with promise that there will be more employees with government support ([www.comtrade.com](http://www.comtrade.com)). Also, the newest cluster in Kragujevac, in the Business Innovation Centre (BIC), that brought together companies dealing with information and communication technologies from Sumadija and Pomoravlje, should get the full support from the Government and become the business model for connecting young talents in the ICT industry (Kartalović, 2013).

Serbian Government adopted certain support policies for the ICT industry, including *The Strategy for development and support of the information technology industry*, that should encourage and support the industry in four segments: startup, outsourcing, development and export of original software products, development centers of large multinational companies (Službeni glasnik RS 72/12). In 2012, the Directorate for Digital Agenda, as an organ of the Ministry of Foreign and Internal Trade and Telecommunications, was established, and it is, among other things, responsible for the use of information and communication technology, providing of information services, research and development in the field of information society and electronic communications, the implementation of standards in information and communication technology ([www.digitalnaagenda.gov.rs](http://www.digitalnaagenda.gov.rs)). The reduction of customs duty on computers to 1% in 2004, the public call of Serbia Investment and Export Promotion Agency for allocation of grants in the field of IT for technological entrepreneurship start-ups and for organizing trainings and networking in the field of IT entrepreneurship ([www.siepa.gov.rs](http://www.siepa.gov.rs)) represent legislation and support measures, which indicate that the Serbian government has recognized the importance and role of the ICT industry. Also, nearly all state institutions have their Web sites. In this way, Serbian government sent a clear

message to potential investors that Serbia works on improving its information space, which should make Serbian national economy more competitive globally.

Generally, ICT industry requires small capital investments, and offers significant revenue opportunities, so some countries took advantage of it, especially Ireland that was one of the least developed European countries and became a real economic miracle by developing and exporting ICT products and services ([www.ictireland.ie](http://www.ictireland.ie)). India where information technology almost did not even exist, is becoming one of the world leaders in manufacturing and software export, as well as Israel, China and Brazil that have achieved impressive results in the production and sales of ICT products and services (Arora, Gambardella, 2005, p. 4). Those countries should be used as a model for Serbia where in recent years the awareness of importance of informatization of economy and society is awakened.

## ***RESEARCH DESIGN***

The aim and the object of research. In practice, there is a lack of clear understanding of open innovation practices. Companies face risks and many challenges when they conduct open innovations. Our starting research questions were: 1) What are the key practices of open innovation in Serbian ICT companies?, 2) What are the strategic motives for engaging in open innovation practices?, 3) Which partners are shown to be of the most importance in open innovation activities?, and 4) What are the key concerns for companies when engaging in open innovation practices? The object of research are Serbian companies in information and communication technology industry (ICT). The main reasons for conducting research in ICT industry are that knowledge-intensive industries have been the fertile ground for innovation, they first realized that the locus of innovation extends beyond the individual company (Fjeldstad et al., 2012), and innovation practices are the most advanced in high-technology industries (Chiaroni, Chiesa, and Frattini, 2011). Also, the fact that large number of Serbian ICT companies are micro and small companies ([www.sito.rs](http://www.sito.rs)) which do not have large financial resources, technological and managerial skills, suggests that it would be of tremendous importance for these companies to use open innovation practices as a source of competitive advantage.

Design of research. Research was conducted by using the questionnaire technique for data collection: the questionnaire was sent via e-mail to 300 ICT companies which are members of ICT clusters and which launched new products and services in past three years. It consists of 14 questions created by using one of free Google services (Google Drive) which, among other things, provides creating anonymous surveys and simple overview of responses.

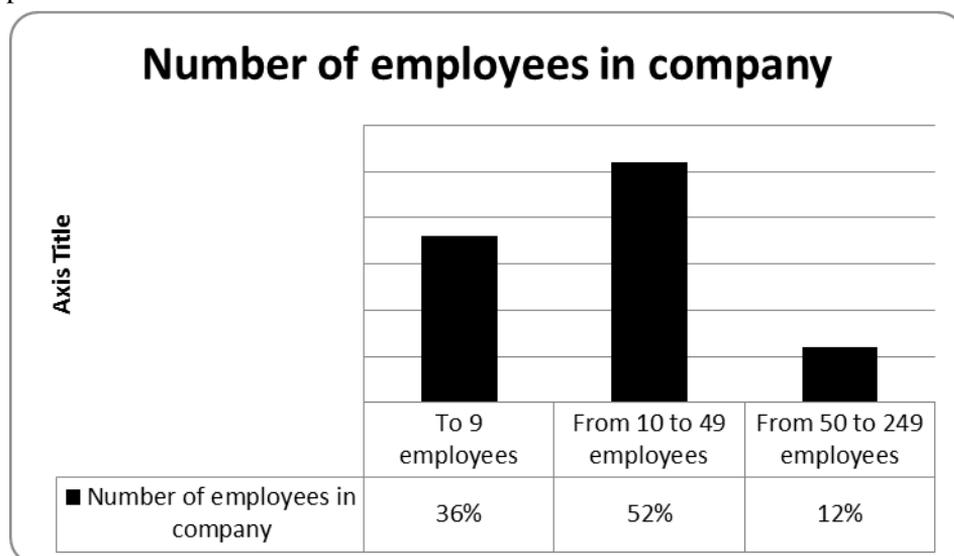
The questionnaire encompassed four sections asking about:

- General information about companies: age, number of employees, key characteristics in conducting their businesses
- The key practices of open innovation
- Strategic motives for engaging in open innovation activities
- The satisfaction with individual partners in open innovation practices
- The key concerns of engaging in open innovation practices

The questionnaire was answered by 25 companies, while 2 companies sent e-mail in which they clearly stated that they do not use open innovation practices. Collected data from the questionnaire were analyzed and interpreted by the description method.

## ***DISCUSSION OF RESEARCH FINDINGS***

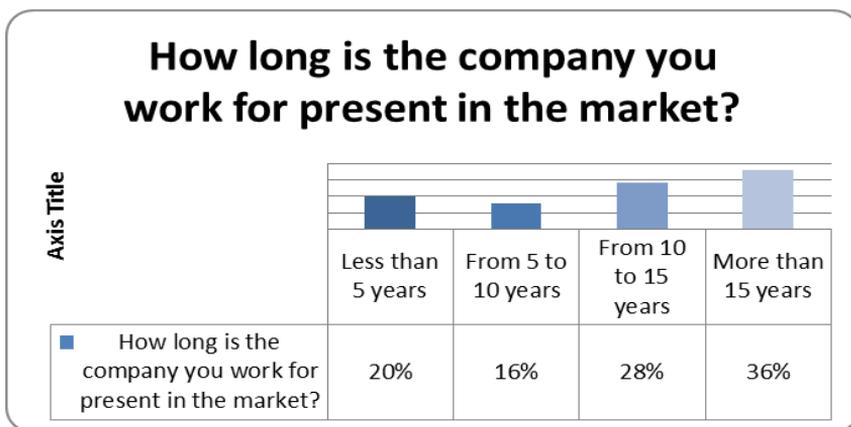
Measured with the number of permanent employees, more than half of surveyed ICT companies belong to group of small companies, while 36% are micro companies.



*Graph 1: Number of employees in surveyed ICT companies*

*Source: Author*

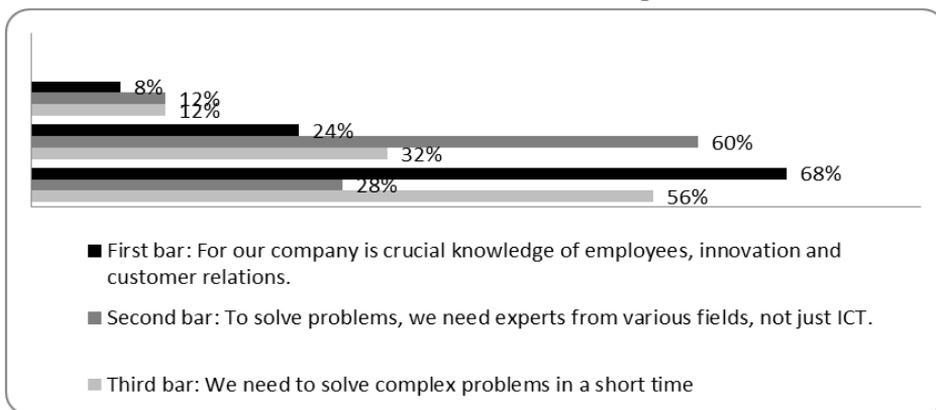
More than one third of surveyed companies work more than 15 years, while 20% represent very young companies which operate less than 5 years.



*Graph 2: Age of the surveyed ICT companies*

*Source: Author*

Key characteristics of surveyed companies can be summarized in the following statement: Serbian ICT companies need to solve complex problems in a short time with experts from various fields, not just ICT, and knowledge, innovation and customer relations are of tremendous importance for them.



*Graph 3: Characteristics of surveyed ICT companies*

*Source: Author*

Bearing in mind all benefits of open innovation practices, it is important to understand how ICT companies in Serbia engage in open innovation activities. We asked them to evaluate inbound and outbound practices that had been identified as most critical in literature and discussions with open innovation practitioners, according to Chesbrough and Brunswicker survey (Chesbrough, Brunswicker, 2014).

Table 5: Open innovation practices in surveyed ICT companies

<b>OPEN INNOVATION PRACTICES</b>	<b>%</b>
<b>Inbound practices of open innovation</b>	
Networking with other organizations without a formal contractual relationship (at conferences, workshops, events)	14%
Involvement of consumers and customers in generation, evaluation, and testing of new ideas for products, services, processes	12%
Licensing of external intellectual property rights (e.g., trademarks, patents, etc.) via formal licensing agreements	11%
Contracting with external service providers for specialized R&D services. Including technology scouting, virtual prototyping	7%
Outsourcing innovation problem solving (including scientific problems) via an open call to external organizations and individuals to submit ideas	5%
Participating in R&D consortia with other public or private organizations in which R&D activities are fully or partly funded by governmental organizations	5%
Funding of external research projects by researchers and scientists in universities to access external knowledge	4%
Invitation of existing suppliers to participate in innovation and submit innovative ideas	3%
<b>Outbound practices of open innovation</b>	
Licensing of internal intellectual property to external organizations via licensing agreements or selling via single payment	9%
Participation in standardization activities via formal standardization agencies (e.g., ISO) or informal standardization consortia	8%
Sale of a market-ready novel product idea to a third party for sale to its customers	6%
Strategic and financial investment in independent joint ventures jointly with external partners	4%
Corporate incubators or accelerators developing potentially profitable ideas and offering supportive environments for entrepreneurs inside the organization to identify novel paths to market	4%
Donations to commons or nonprofits (e.g., open-source communities) to support external R&D	4%

*Source: Author*

Our results show that companies engage far more frequently in inbound open innovation practices where external knowledge flows into the firm. Among most used practices are networking with other organizations without a formal contractual relationships, involvement of consumers and customers in generation, evaluation, and testing of new ideas for products, services, processes, and licensing of external intellectual property rights via formal licensing agreements.

Reasons for engaging in open innovation practices are different. We created a list of some of the most frequently named reasons for engaging in open innovation practices according to JISC study *Facilitating Open Innovation* (JISC, 2009). Answers of surveyed companies are summarized in following table.

*Table 6: Reasons for engaging in open innovation practices in surveyed ICT companies*

<b>Reasons for engaging in open innovation practices</b>	<b>%</b>
We did not have the required expertise under our own roof	20%
We did not have the capacity to carry out the work alone	20%
We wanted to bring “fresh blood” into the project to benefit from their different approach and ideas	14%
Cost saving	14%
We believed that outsourcing of expertise would save money	9%
To enable exploitation of any intellectual property produced into other non-competing markets	5%
Believed a multidisciplinary approach would produce more successful output	5%
Reputation of partners	5%
We wanted to become a member of a consortium to obtain eligible status for funding	4%
We wanted to create revenue by acting as an intermediary to encourage and facilitate open innovation	2%
We required someone else’s intellectual property	2%
We felt it was our only chance of commercializing our ideas	0%

*Source: Author*

Required expertise beyond the company, shortage of internal capacity, need for fresh approach and need for cost saving are main strategic motives for engaging in open innovation practices in surveyed ICT companies.

We also wanted to identify the importance of individual partners in open innovation practices. Answers about satisfaction of individual partners show that companies are most satisfied with their customers.

Concerning fact is that many companies are dissatisfied with universities and public research organizations which indicates that there is a lot of space for improvement of their activities and engagement.

*Table 7: The satisfaction with individual partners in surveyed ICT companies*

Partners	Hugely satisfied	Largely satisfied	Satisfied	Largely dissatisfied	Hugely dissatisfied
Customers	22%	57%	9%	12%	0%
Universities	5%	33%	24%	38%	0%
Suppliers	0%	41%	36%	9%	14%
Public research organizations	5%	14%	32%	36%	14%
Entrepreneurs and start-ups	5%	14%	50%	23%	8%
Competitors	23%	36%	27%	14%	0%

*Source: Author*

When engaging in open innovation practices, surveyed ICT companies are most concerned about the ability to find the right people to be involved, costs, intellectual property issues, and time constraints. Potential cultural differences and trust among partners are of some, little or no concern at all.

*Table 8: The key concerns and challenges in pursuing open innovation practices in surveyed ICT companies*

Answers	Huge concern	Large concern	Some concern	Little concern	No concern
Intellectual property issues	16%	5%	37%	21%	21%
Costs	5%	32%	42%	21%	0%
Ability to find the right people to be involved	26%	42%	21%	0%	11%
Potential cultural differences	5%	0%	26%	37%	32%
Time constraints	5%	32%	21%	37%	5%
Project management	0%	26%	42%	16%	16%
How to build trust	0%	5%	42%	37%	16%

*Source: Author*

Regarding to the durability of open innovation practices in Serbian ICT companies, we asked how long companies had been practicing open innovation. 56% of surveyed companies are engaged in open innovation activities less than three years, while other 44% of the companies engaged in open innovation activities from three to six years. 55% of surveyed companies answered that they would engage in open innovation projects in future, only 5% stated clearly no, while 40% answered that they are not sure about engaging in open innovation practices.

Beside 25 companies that answered to the questionnaire, there are 2 companies that sent e-mail in which they clearly stated that they do not use open innovation practices. Received e-mails indicate that top management manifest resistance to change, it is not informed about all benefits that open innovation brings and that there is a lack of understanding that links with external partners tend to complement rather than replace internal R&D department and activities (Chesbrough, 2006). Some of the surveyed ICT companies have illusion that their internal R&D department is just enough for innovations, which is consistent with some other results on open innovation where employees in R&D departments believe that their technology is the best and requires no further development (Rangus, Drnovšek, 2013).

## ***CONCLUSION***

The aim of this paper was to analyze open innovation practices based on case study of Serbian ICT companies. Results show that Serbian ICT companies engage far more frequently in inbound open innovation practices where external knowledge flows into the firm. Among most used practices are networking with other organizations without a formal contractual relationships, involvement of consumers and customers in generation, evaluation, and testing of new ideas for products, services, processes, and licensing of external intellectual property rights via formal licensing agreements. The key strategic motives for engaging in open innovation practices are: required expertise from partners, shortage of internal capacity, need for cost saving, and need for fresh approach, which is not surprising bearing in mind that large number of Serbian ICT companies are micro and small companies. Answers about satisfaction of individual partners show that companies are most satisfied with their customers which is very positive result according to fact that involvement of customers and consumers in open innovation practices is of tremendous importance for companies. Networking with other organizations without a formal contractual relationships via conferences, workshops, seminars is at the top of open innovation practices in surveyed ICT companies. Bearing that in mind, result that many companies are dissatisfied with universities and public research organizations is very concerning and indicates that there is a lot of space for improvement of their activities and engagement. Results that more than one half of surveyed companies are interested to engage in open innovation activities in future, while 40% are not sure, highlight the importance of all challenges and concerns that surveyed ICT companies are faced with. Surveyed ICT companies are the most concerned with the ability to find the right people to be involved, costs, intellectual property issues, and time constraints.

Taking into account that small number of companies respond on questionnaire (27 companies out of 300 companies included in survey) making response rate of 9%, we can make just limited conclusions regarding ICT companies and their general attitude toward open innovation practices. Some general proposals for

facilitating the practices of open innovation in Serbia are: to raise awareness about key benefits and advantages of open innovation practices through education, workshops and training of open innovation, to change the mentality of management and employees and their understanding of open innovation activities, to establish good regulatory environment, and to provide direct and indirect financial incentives and initiatives for open innovation practices.

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***II PART.  
SOCIOLOGICAL AND SOCIAL PSYCHOLOGICAL  
ASPECTS OF ENTREPRENEURSHIP***





## **ROLE STRESSORS AND ORGANIZATIONAL COMMITMENT: EMPIRICAL RESEARCH**

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### **ABSTRACT**

*Professional stress is a current research issue in modern psychology due to its direct impact on health and subjective well-being of people all over the world. Professional stress also leads to financial losses for the organizations. On the other hand, organizations can benefit from employees who are committed to them. Such employees contribute to the better quality of work and positive image of their organizations. This paper studies the interrelations between the role stressors in the workplace and organizational commitment of the employees in Bulgaria. The research provides valuable conclusions for the employers and it will be helpful for effective management of organizations.*

**Key words:** *Research, Organizational Commitment, Role Stressors, Employees, Organization*

**JEL Classification:** *I15, J24, J28*

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## ***INTRODUCTION***

Professional stress is a widely discussed organizational phenomenon in modern psychology due to its direct impact on health and subjective well-being of people at work. However, regardless of the achieved scientific progress this problem continues existing in professional lives of many employees and gains intensity over the last years that are characterized by frequent changes in organizations – merges and bankruptcies, layoffs, losses of jobs, various anti-crisis measures, decreased costs on healthcare, etc. On the other hand, the high levels of unemployment stimulate minimum tolerance to mistakes employees can make in the workplace and increase the requirements on behalf of the management. The value of human labor becomes lower when the employers believe there are many other candidates willing to replace the employees who do not perform well. Thus we are witnessing a new organizational reality which leads to professional stress and high health risks.

The negative side of stress, distress, is accompanied by a multitude of health problems and risks. Both people and organizations are paying a high price for poorly managed professional stress. For the individuals, the price of stress can be physical, mental, behavioral or emotional. Organizations whose employees and leaders experience high levels of professional stress which they cannot manage suffer enormous financial losses due to absenteeism, turnover, work accidents and decreased productivity.

On the other hand, organizations can benefit from employees who are committed and loyal to them. Such employees accept the goals and values of their organizations, are ready to put more efforts at work and are willing to remain in the organizations. It has been found out that the higher the organizational commitment of employees, the lower the chance of leaving the organization (Пириу, 2006). Committed workforce is also less susceptible to stress as it will be discussed in this paper.

## ***PROFESSIONAL STRESS***

Professional stress occurs when the perceived pressure exceeds the perceived abilities of coping with it (Palmer et al., 2004). Everybody can suffer from professional stress and there has been found no demographic characteristic which puts some group of people in a more favorable position than the others. Stress is ubiquitous.

According to Palmer, Cooper and Thomas (2004), the role in the organization is one of the major risks for professional stress. This role concerns clarity of the functions people perform in the organization and whether the organization guarantees that employees do not enter into conflict with these functions. The authors state that the organizations can manage this risk factor by purposeful avoidance of role conflicts and preparation of clear job descriptions.

Ambiguity at work or role ambiguity is characterized by the lack of clearly defined work duties. When there is uncertainty about the obligations and responsibilities employees experience professional stress (Ригио, 2006). The role conflict also contributes to stress in employees. The simultaneous performance of several roles in the workplace poses the evaluation of employees and their work performance on a difficult test. The role ambiguity and role conflict are considered as some of the factors for development of depression and anxiety related to work (Lowman, 1993). The role ambiguity is most detrimental to work performance (Gilboa et al., 2008). For the organizations, the negative consequences of professional stress are mainly economic. Organizations suffer enormous financial losses due to absences from work of their employees, turnover, work accidents and reduced productivity. All these are consequences of professional stress (TUC, 2004, in Palmer et al., 2004).

Unfortunately, the detrimental effect of professional stress is not observed only in the organizational life. In the modern world, professional stress takes even bigger, epidemic sizes. (Cooper, 2010). From a psychological perspective, the negative consequences of stress at work are worrisome. It affects both physical and mental health of people. The physical conditions caused by acute and chronic stress include: increased morbidity from cardiovascular diseases (Tennant, 1999), hypertension (Ogden, 2007), suppressed immune response (Lazarus, 1993), diseases of the respiratory (Lehrer et al. 2002) and muscular systems (Gevirtz et al., 1996), metabolic syndrome and some types of cancer (Ogden, 2007). In addition, the physiological changes caused by stress lead to poor memory (Sapolsky, 2003) and difficulties in spatial orientation (Ogden, 2007).

Both chronic and acute stress lead not only to changes in physiology but also to changes in behavior. In their attempts to improve their moods people suffering from chronic stress show self-destructive behaviors: tobacco smoking, consumption of alcohol, drug abuse (Sinha et al., 2000), excessive intake of carbohydrates (Greeno, Wing, 1994) and non-observance of a healthy sleep and wakefulness cycle (Ogden, 2007).

Badly managed stress causes physiological changes in the organism by means of which it has a serious impact on the mental health as well. It has been found out that stress is connected to anxiety, and the chronic stress in particular demonstrates a specific relation with the onset of anxiety and depression (Esch et al., 2002).

This is why it is essential that employers pay more attention to creating less stressful work conditions for their employees.

## ***ORGANIZATIONAL COMMITMENT***

In the scientific literature, there are different definitions of the term ‘organizational commitment’ but it is accepted that the original conception is based on the work of Mowday et al., (1979) who identify commitment-related attitudes and commitment-related behaviors. Today, a widely used model of organizational commitment is the three component conception of organizational commitment, which was developed by Meyer et al., (1993).

Organizational commitment can be considered as psychological identification of the employee with the organization where he/she works. It consists of the positive evaluation of the employee of the organization, the intension for contribution to its success, as well as desire and striving for keeping their position in the organization. Often, when the employee is alienated from the activities and life of the organization, we can speak about lack of commitment. Some authors define commitment as loyalty or even patriotism (Marypa, 1997; 1998; Marypa, Кырбатова 2001) and they assume that organizational commitment expresses involvement in the work process and emotional affection to the organization.

The employees’ commitment to the organization is a psychological state determining the expectations and attitudes of the employees. Their behavior to the organization is defined by how they perceive it: if they belong to the organization or are *outside* it. From a managerial perspective, it is enormous success if the managers build commitment to the organization in their personnel. It includes internalization of the organizational goals and values, the ability to work to the benefit of the whole organization and to overcome the individual needs (even in cases when it is not profitable for the employee).

In the specialized literature authors very often connect the term ‘organizational commitment’ with ‘identification’, ‘involvement’ and ‘loyalty’. Identification is acceptance of the organizational goals as the employee’s own goals; involvement is the desire to put personal efforts to the organization’s success, and loyalty is the emotional commitment to the organization, the desire of the employee to be its member (Marypa, Кырбатова, 2007).

Commitment to an organization inevitably includes the above stated factors and assumes their inclusion in the self-image of each employee. By its nature organizational commitment is equal to neither identification nor loyalty. A meta-analysis conducted by Riketta (2005) reveals that although there is some similarity between identification and affective organizational commitment, organizational identification is weaker than commitment, correlates with job satisfaction and intention to continue working in the same organization, and is strongly dependent on involvement in work (Riketta, 2005).

The interrelation between organizational commitment and identification gave grounds to Meyer et al. to develop an integrative model of the processes of commitment and identification (Meyer et al., 2006). According to this model, the various types of commitment are a consequence of the various types of

identification. The model was derived from the idea of Rousseau (1998) according to which there are two levels of identification – situated and deep structural identification.

Research conducted by Lovakov and Lipatov (Ловаков, Липатов, 2011) did not find a relation between the current commitment and identification of the employees and the results confirmed the hypothesis that the two constructs are independent and different from each other.

One of the most popular models considering the essence of organizational commitment is the one of Allen and Meyer (1990) called the three-component model (TCM) (Allen, Meyer, 1990). This model consists of three types of commitment: affective, continuance, and normative, which outline the relation between the employee and the organization. The authors state that, “Employees with strong affective commitment remain because they want to, those with strong continuance commitment because they need to, and those with strong normative commitment because they feel they ought to do so“ (Allen, Meyer, 1990; p. 3).

In their research, Allen and Meyer (Allen, Meyer, 1990; Meyer, Allen, 1991) consider the first component, affective commitment, as consisting of three elements: emotional ties, identification, and involvement in the organization. The second component of commitment, the behavioral one, concerns the losses perceived by the employee in case of a possible leaving of the job. The normative component of commitment relates to the perceived obligations upon staying in the organization.

Organizational commitment is formed in these employees who feel the organization provides them with opportunities for growth and development and the opportunity to do activities which they like. The strong affective commitment leads to the desire of the employees to keep their job positions and to remain employees in the organization. The employees having a strong behavioral aspect of commitment remain at work because they need it. The employees who have a leading normative component of commitment stay in the organization because they believe they must stay. Allen and Meyer (1996) maintain that there is enough evidence for validity of the three-component model of organizational commitment.

Alienation and opposition are an alternative to commitment (Свиридова, 2011). The organization is not perceived as ‘one’s own’ but as ‘alien’. There is a high power distance between the employees and the management. The organizational goals serve the managers’ and directors’ own agenda. The needs of the person are put above the organizational ones.

## ***ORGANIZATIONAL COMMITMENT AND PROFESSIONAL STRESS***

Organizational commitment cannot be directly observed. An expression of commitment to the workplace is the desire of the worker to put more efforts so that the organization functions better, focusing on organizational goals and readiness for self-sacrifice. Stress in the workplace is the harmful physical and emotional responses to adverse and noxious aspects of work content, work organization and work environment. Occupational stress is a very subjective concept, affecting every individual differently and has been linked to absenteeism, decreased productivity, increased health care costs and illness (Yahaya et al., 2012).

The factors of organizational environment play a major part in creating stress in the workplace (Ivancevich et al., 1982; Jamal, 2010) and the employees with various degrees of organizational commitment would perceive this stress in different ways. The employees with a lower degree of organizational commitment are likely to demonstrate higher levels of trust to the organization (Meyer et al., 2002; Ouchi, 1981). Adversities, as, for example, high levels of stress, might not be perceived by them as sufficient grounds for non-fulfillment of their obligations. In contrast, the employees displaying low levels of organizational commitment demonstrate a limited sense of loyalty to the organization (Jamal, 2011). Research conducted by Jamal (2011) found out that organizational commitment acts as a buffer against the aversive effects of job stress on individuals' job performance. Practically, it means that individuals who had high organizational commitment appeared to be better off against the adverse consequences of job stress than individuals who had low organizational commitment (Ibid).

Similar results were obtained by another research indicating a significant and negative relationship between job stress and organizational commitment (Khatibi et al., 2009). As the employees' job stress increases, their commitment to organization decreases and vice versa. According to the authors, identification and minimizing of the stress factors can decline the adverse effects of job stress and promote the organizational commitment of employees. In addition, the research showed there was a negative and significant relationship between job stress and affective commitment (Khatibi et al., 2009). The results of the research of Khatibi et al. (2009) is to a large extent consistent with the research results of Lee (2007), Lambert, Paoline (2008), Omolara (2008), Boyas, Wind (2009), but inconsistent with the research results of Wells et al. (2009) and Yaghoubi et al. (2008).

Organizational commitment should exist within every employee, from managerial staff to non-managerial staff in order to determine the success of an organization. Employee commitment is gained when the organization shows the same amount of commitment as well (Bytyqi et al., 2010). Cooperation and appreciation between each and every members of the organization is needed to achieve the organization's goal. This can be achieved only if strong commitment exists within the members of the organization (Ratmawatti, 2007).

Job satisfaction and employee commitment are not a onetime process but change constantly especially when the organization deals with high level of employee work stress (Bytyqi et al.,2010). Work stress should not be taken for granted but pragmatic measures should be employed to deal with it and void eventual negative effect on organizational commitment.

### ***ROLE STRESSORS AND ORGANIZATIONAL COMMITMENT: EMPIRICAL RESEARCH***

This research is a pilot project aiming to find out the interrelations between job stress and organizational commitment of employees. For the purposes of the pilot project the authors used a heterogeneous sample consisting of 43 subjects. The tasks the researchers set to themselves are to study the interrelations between role stressors and organizational commitment.

The methodology used in this research consists of two questionnaires for assessment of role stressors in organizations and for assessment of organizational commitment standardized by Radoslavova and Velichkov (Радославова, Величков, 2005). The questionnaires are of self-assessment type and were administered to the participants online on a random principle.

For assessment of the role stressors in the workplace a questionnaire of 41 items was employed. The questionnaire comprises two scales: role ambiguity and role conflict. Each scale consists of three subscales measuring the job duties, performance and results. The role perceptions of the subjects are evaluated by frequency of occurrence in their everyday work life. The answers are on a five-point Likert-type scale where 1 being almost never and 5 being almost always. (Радославова, Величков, 2005).

The role ambiguity scale covers statements describing ambiguity of the employees about their job duties, planning of goals, tasks, the ways of evaluating their results, the authorities. The role conflict scale includes statements which show the necessity of the employees to perform unexpected and unusual tasks, to respect different opinions and recommendations of other people concerning performance of employees' duties, as well as to assess the achieved results etc. (Ibid). The internal consistency of the questionnaire measured by Cronbach's Alpha is.94 for the present sample.

The second questionnaire measures organizational commitment and consists of 24 items. The response scale is five-point, Likert-type and the answers vary from 1 being never to 5 being every day. This questionnaire includes 5 subscales: personal importance, emotional involvement, identification, positive exchange and dedication. The internal consistency of the questionnaire measured by Cronbach's Alpha is.83 for the present sample.

Bearing in mind the small sample used, the research hypotheses raised were exploratory. The main research hypothesis is that there are interrelations between

role stressors and organizational commitment. The second hypothesis is that with increase of stress organizational commitment decreases.

The additional tasks of the research is to study the relationships between the above mentioned factors and the demographic characteristics of subjects like gender, age, education, length or service etc. The expectations are that the demographic characteristics will influence commitment to the organization and the subjective evaluation of the role stressors in the workplace.

The demographic profile of the sample shows a relatively young sample. The mean age of participants is 33 years. About 56% of the subjects are women. In terms of education, the sample is dominated by holders of master's degree diplomas (77%), followed by bachelors (11%), persons with PhD degree of other (7%) and only 5% have primary or secondary education. Length of service reveals that most of the respondents have a total length of service between 6 and 10 years (35%), followed by those whose length of service is between 16 and 20 years (21%). 18% have served between 11 and 15 years, 14 percent between 3 and 5 years. The lowest percentages belong to the shortest (between 1 and 2 years) and longest (more than 21 years) periods of service – 5% and 7% respectively. The years spent with the present employer, divide the sample as follows: 67% of the subjects have worked with the same employer between 1 and 5 years; 26% between 6 and 10 years and only 7% above 16 years. In terms of family status, the predominant part of the sample is taken by people who are married (53%) or living with a partner (14%), followed by single people (26%) and widowed or divorced (7%).

## ***KEY FINDINGS***

In order to test the two research hypotheses, correlation analysis was conducted using the statistical software SPSS. The main research hypothesis is that there are interrelations between role stressors and organizational commitment. The second hypothesis is that with increase of stress organizational commitment decreases.

*Table 1: Correlations of Pearson (r) between role stressors and organizational commitment*

	Organizational commitment – personal importance	Organizational commitment – emotional involvement	Organizational commitment – identification	Organizational commitment – positive exchange	Organizational commitment – dedication
Role ambiguity – job duties				-.407**	-.326*
Role ambiguity – performance		-.346*	-.352*	-.363*	
Role ambiguity – results	-.335*	-.340*		-.347*	
Role conflict – job duties	-.417*	-.514**	-.431**	-.428**	-.432**
Role conflict – performance		-.458**	-.326*	-.458**	-.463**
Role conflict – results				-.393**	-.430**

\*\* . Correlation is significant at the 0.01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

The results obtained by means of the correlation analysis demonstrate there is only partial interrelation between the role stressors and organizational commitment. The figures in the table represent only the statistically significant correlations. Most of the correlations are of medium strength while only one correlation has large strength and this is the correlation between role conflict concerning job duties and organizational commitment concerning emotional involvement. The correlation is negative which means that the higher the role conflict caused by inconsistent job duties, the lower the emotional involvement in the organization the person is working in. There are three other correlations which deserve more attention as they are close to being of approximately large strength. These are the interrelations between role conflict concerning employees' performance and organizational commitment concerning emotional involvement, positive exchange and dedication. All of these correlations are negative showing the detrimental effects of role conflict caused by unclear evaluation of employees efforts invested in work. It is worth commenting that all statistically significant and insignificant correlations the analysis yielded were negative. Thus, the two raised research hypotheses were confirmed partially, i.e. there is a negative interrelation between role stressors and organizational commitment but only in some aspects.

It was considered as necessary to study also the following demographic characteristics – gender, education, total length of service, length of service in the present organization and family status of the respondents. The main assumption

about these factors was that they will influence organizational commitment and the subjective evaluation of the role stressors in the workplace.

For studying the influence of the demographic characteristics (gender excluded) on the subscales one-way analysis of variance ANOVA was used.

The only statistically significant influence of a demographic characteristic was found out in the subscale role ambiguity concerning results. It shows the length of service in the present organization influences the role ambiguity in terms of results of the employees. Table 2 demonstrates the specific differences for each group.

*Table 2: Influence of the length of service in the present organization on role ambiguity concerning results - one-way analysis of variance ANOVA*

(I) Length of service in the present organization:	(J) Length of service in the present organization:	Mean Difference (I-J)	Std. Error	Sig.
1 to 5 years	6 to 10 years	-1.05643	1.02916	.565
	Over 16 years	4.03448	1.76264	.069
6 to 10 years	1 to 5 years	1.05643	1.02916	.565
	Over 16 years	5.09091*	1.89302	.027
Over 16 years	1 to 5 years	-4.03448	1.76264	.069
	6 to 10 years	-5.09091*	1.89302	.027

The test Tukey HSD demonstrates that in terms of role ambiguity concerning results at the level  $p < 0.05$ , employees with length of service in the present organization from 6 to 10 years ( $M = 9.09$ ;  $SD = 4.27$ ) are more strongly influenced by the factor 'length of service in the present organization' than in the case of the employees who have served in it for more than 16 years ( $M = 4.00$ ;  $SD = 0.00$ ). Most probably this is due to the fact that with the long years of service in the same organization employees from this sample have learned more about the ways these organizations function and understand better the ambiguous messages concerning evaluation of their work. It is an interesting finding which inspires future research efforts in this direction.

For testing the influence of gender on role stressors and organizational commitment independent-samples T-test was conducted. The results showed no statistically significant differences in the responses of men and women and hence the gender does not influence the role stressors and organizational commitment in this pilot study.

The analyses of the demographic factors show that for this sample, with the exception of length of service in the present organization, the characteristics of the respondents do not influence their responses as only a single statistically significant difference was found out.

## ***DISCUSSION***

The pilot study the authors conducted on role stressors and organizational commitment has two limitations: the sample is modest by its size and it is not homogeneous. Nonetheless, the analyses conducted yielded interesting results which can be very useful to the employers who want committed and healthy workforce.

The correlation analysis demonstrated statistically significant negative correlations between most subscales of the questionnaires on role stressors and organizational commitment. The strongest correlation discovered was the one between role conflict concerning job duties and organizational commitment concerning emotional involvement. This finding clearly demonstrates that employees in the present sample respond strongly by decreasing their emotional involvement in the organizational matters when they have inconsistent job duties. There are three other correlations which have a practical value to employers although coming from a small sample. These are the correlations between role conflict concerning employees' performance and organizational commitment in terms of emotional involvement, positive exchange and dedication. All of these correlations prove the negative reaction of withdrawal when the employees perceive their work efforts have not been evaluated properly.

The one-way between-groups ANOVA analysis of the influence of respondents' demographic characteristics on role stressors and organizational commitment showed no statistically significant influence, with the exception of one demographic characteristic – length of service in the present organization. It proved to influence role ambiguity concerning results of the work done in the direction that employees who have worked between 6 and 10 years in the same organization experience stronger role ambiguity concerning the evaluation of the results of their work as compared to the respondents who have spent more than 16 years in the same organization. Most probably, this result can be explained with the experience accumulated in an organization. However, the modest number of subjects does not allow making definitive interpretations.

## ***CONCLUSION***

Professional stress will remain a challenge for the modern organizations as it cannot be completely eliminated from organizational life. This is one of the most difficult tasks of organizational leaders – to create organizations where stress is well managed. At the same time, they have to stimulate and maintain organizational commitment in their employees in order to keep them loyal and devoted to the organization, on the one hand, and healthy and hard-working, to ensure good financial results, on the other hand.

The results of the empirical research provoke future scientific explorations on the topic. They can also serve the employers by providing them with better understanding how to maintain the levels of professional stress in their organizations low and the employees committed.

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# **DEVELOPING BUSINESS CULTURE THROUGH MOTIVATION AND CONFLICT MANAGEMENT**

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## **ABSTRACT**

*Business culture, organizational culture and corporate culture are all terms that different authors describe as values and norms held in common within a particular business, whereas the “culture development” is a process of shaping business culture over time. Cultural clashes in any international project or organization have in this day and age greatly enhanced the emphasis on the preparedness for potential conflicts residing in cross-cultural collaboration. Corporate culture, at the same time, plays a significant role in providing a framework in which different motivational issues can act. These issues require an assessment of the influence business culture exerts on motivational practices, and an assessment of probably existing differences in motivation management practices. Our study investigates different influences using the sample comprising 247 education centers’ employees in terms of positive and negative motivation factors and two specific conflict categories, namely: 1) real professional differences, and 2) power struggles and personality issues. Consequently, the objective of this research is to establish the relationship between organizational culture and conflict management styles together with motivation approaches in the workplace. Our main conclusions suggest that approaching conflicts with a positive attitude is the best way to make the most of it and emerge at the end of the tunnel with a more creative solution, and that business culture does influence motivational practices that are further determined by whether the culture is task-orientated or person-orientated.*

**Key words:** *Business Culture Development, Motivation Factors, Conflict Management, Cross-Cultural Collaboration.*

**JEL Classification:** *J53*

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## ***INTRODUCTION***

Society development and contemporary socio-economic relations create an increasing need for an advanced business culture in solving a diversity of problems in almost all areas of human activity. Globalization trends, democratization and political decentralization, consolidation of capital and business networking in a common business system, great turbulence in the global financial market, decreasing weight of centralized decision-making, as well as the advancement of science and technology with a highly pronounced practical application of acquired knowledge led to unstoppable changes in the organizational structure and resurfaced the tendency to provide explicit business culture support in order to ensure necessary prerequisites significant for realizing objectives set by any organization.

The stated pursuit toward business culture was at first present only in the developed world, however it has transferred to and engulfed the entire global market of knowledge and goods, making decision-making increasingly mobile from higher to lower parts of the system, namely, from one to several persons, members of the group. For that very reason, collaboration, coordination of activities and teamwork represent prerequisites for developing and successfully running any modern company, organization or organizational system incorporated into one joint business network. The aim of collaboration is to improve relations within an organization, to develop team work and group decision-making climate, to timely and adequately resolve conflicts, and to thereby enable a more efficient and effective work process in order to achieve the set plan of the organization (Martin, 2010, Armstrong, Mitchel, 2007).

Aligning individual and common needs and interests is fundamental in corporate culture in order to express and project tendencies and issues surrounding motivation and conflict as disagreements between two or more members or teams due to different statuses, goals, or perceptions. Fundamentals in any motivational process and any motivational structure are needs, and resulting interests, values and personality traits.

The aim of this study is to examine how motives and conflicts influence business results and business culture projections within an organization with particular respect for individual and general social needs and interests. For that purpose original research surveys were prepared and implemented in accordance with set goals and tasks. Set research goal produced research tasks using questions on motivation and conflicts concerning the following:

- Defining motivation and conflicts;
- Identifying and interpreting motivation structure, main motivation elements and conflict structure;
- Establishing relationships between motivation, conflict and other aspects of a personality;
- Identifying other psychophysical, demographic and professional characteristics of a personality and social socio-economic conditions for life and work of employees.

Active interpersonal cooperation, developed good interpersonal relationships, and an advanced level of corporate culture have proven essential for the development and prosperity of an organization in the new political and economic value system dominating the world today. The very concept of organization has two aspects:

#### INSTITUTIONAL ASPECT

(Organization as an institution or functional group)

#### PROCEDURAL ASPECT

(Method for designing and presenting the system to the members of the organization)

Organizational process involves a detailed description of assigned tasks, division of tasks and activities, coordination of activities and constant monitoring and control of the increasing effectiveness. This requires implementing both internal and external mission (Mićović, 2000).

Implementation of the external mission requires:

- Defining the position and the role of the organization/institution in the society and the belonging environment;
- Defining the position and the role of the organization/institution in relation to set objectives and tasks;
- Aligning the plan of activities with the external mission;
- Structuring the organization based on external demands;
- Appropriately integrating constituent parts for implementing the external mission;
- Motivating its members in furthering the external mission;
- Timely monitoring and controlling achieved tasks;
- Employing necessary resources and caring for their rational use for the purpose of implementing the external mission.

Implementation of the internal mission requires:

- A developed work plan on the most rational use of existing resources of an organization/institution in order to achieve its objectives;
- More efficient execution of planned activities;
- Appropriate control of the assigned tasks and activities completion;
- Organizational structure optimization to facilitate reaching long-term objectives;
- Delegating organizational units' authorities and responsibilities to ensure necessary conditions for performing their activities;
- Creating a positive working environment and motivation for successful operation;
- Ensuring required financial resources for reaching set objectives;
- Rational use of available resources.

Even though developing a system and an organization often involves structural and technological changes, the main goal in the process is to bring about change in people, i.e., in the nature and quality of their working relationships. Successful development of an organization is therefore directed not only toward the organization as an entity, but primarily toward individuals and/or groups significant for the progress and achievement of stated goals of the organization.

In upholding the quality of business activities and depending on the situation on a global, regional or local level as well as within the organization itself, it is quite often essential to make and manage changes. Useful therefore is to be on familiar terms with methods for adjusting to changes regardless of whether the change is induced by external or internal environmental factors. The most important methods that can be employed in the process of change (Mićović et al., 1983) include:

- Problem solving;
- Organization renewal;
- Collaborative management;
- Cultural environment;
- Action research.

The authors additionally propose three approaches in the process of change (Stoner, Wankel, 1986, Grinberg, Baron, 1995, Leavitt, H.J., 1964), namely:

- I. Changes in the organizational structure;
- II. Changes in technology;
- III. Changes in people.

Human resources managers require good understanding of activities and techniques that stimulate organizational development. They may be applied in various situations, such as identifying certain problems and situation in which the intention is to induce changes significant for organizational development. Three main techniques are nowadays cited for stimulating development and prosperity of an organization (DeCenzo, Robbins, 2010), namely:

- I. Technique according to the target group;
- II. Technique of feedback survey, group and network management;
- III. Technique of improving collaboration.

Certain activities implemented with the aim to raise the quality of work in an organization, ranging from individual training to improved general environment and climate in the organization, may be based on the following target groups:

- Individuals - training individuals in small groups in order to improve their skills, especially in the field of interpersonal relations, effective cooperation and increased threshold for tolerance.
- Small groups - two to three persons training through the so-called "transaction analysis" in which they practice communication styles and communication content exchange in order to reduce destructive and accentuate clean and creative messages.

- Teams or groups - training teams or group members to better understand their working relationships. This is done by developing problem solving skills within a team/group.
- Intergroup relations - training for confronting different opinions based on which the situation in the organization is assessed. The ultimate goal is to enable teams and/or groups to prepare action plans and improve job activities and own efficiency. These meetings are organized following either significant organizational changes or introduction of new technologies in the work process.
- The entire organization - either a technique of reverse situation research in the organization or a network technique for identifying different combinations for caring for people and production within the organizational process matrix.

Communication studies and social and cultural studies unmistakably reveal a direct correlation between positive climate in an organization and the achieved level of communication and tolerance between individuals, groups and teams within that organization. Technique for improving collaboration is therefore extremely important and generally accepted in the modern world of management. Main parameters for attaining a high level of cooperation and collaboration in an organization include implementation of joint values and strengths, trust between individuals, groups, teams and top managers, risk taking by responsible individuals and departments, and finally, a clear representation of all stakeholders in the organization in terms of higher goals of importance for organizational development (Cheese et al., 2008, Thill, Bovee, 2011, Dessler, 2011).

## ***BUSINESS CULTURE AND LEADERSHIP***

Answering to many questions this day and age impose may help us to become leaders with a high level of business culture. Introducing culture intelligence in any business is a major challenge. Leaders ought to employ awareness and adaptability skills to assess given business opportunities and align their management with the amount of available power, the nature and values of their followers and tasks to be achieved.

Leadership is generally defined as the ability to influence others to voluntarily aim to realize a common goal. Crucial for every leader is building a leadership style rich in cultural intelligence with a clearly defined and visible performance for the organization. Achieving aforesaid requires utmost care for attaining organization's business and work objectives and care for relationships within the organization, in other words, requires both organizational and business culture.

The above stated indicates a clear correlation between leadership style and organizational performance. A great number of other factors also play a part, them being the structure of tasks resulting from organization's objectives, leader's power and behavior of subordinates, who naturally try to exert influence over their leader

just as often as he/she tries to exert influence over them. There is no defined ‘best leadership way’ that can be applied in all organizations and business cultures throughout the world. However, leadership examples in the world allow us to understand the great complexity and finesse of business culture influencing forces (Đorđević-Boljanović, Pavić, 2011):

#### EXAMPLE 1)

Inherent to Japanese, as opposed to American culture, is a higher level of power distance, in other words, they expect and accept that leader typically conducts power. Japanese show more respect for their leaders simply based on their position, whereas in the USA leaders must earn that respect with their deeds. For that reason the success of leaders in Japan is largely based on their ability to understand and attract followers.

#### EXAMPLE 2)

Leadership in the Arab society is directly ingrained in the historical and cultural heritage, considerably shaping business tradition, management practices and expectations from the leader. The management style emerging from such circumstances is referred to as the “Sheikocracy”. This management style is distinguished by strong elements of personal autocracy. Leaders shall instead of respecting procedures appoint based on family relations and friendships.

#### EXAMPLE 3)

Leader’s legitimacy in Chinese culture is loyalty based, and in a modern Chinese organization a word of the founder or chief executive is interpreted as law, resulting in a specific relationship between the leader and followers.

#### EXAMPLE 4)

Management in France is influenced by a strong emphasis on social development based on established hierarchy. A large group of middle managers dealing with an abundance of rules and regulations acts as a mediator between top management and employees (workers). Even though the system seems confusingly inefficient, French organizations function rather reliably.

#### EXAMPLE 5)

The image of Russian leaders as powerful self-rulers is based on the long history of the country run by centralized authority and responsibility. Centralization of power created strong bureaucracy at the top. While Russian organizations are trying to find their place in the new free market setting, Russian leaders are attempting to bring the responsibility down to the lower hierarchical levels.

Given examples from the United States, Japan, China, Arab Countries, France and Russia show the complexity of forces that influence leadership styles. The significance of historical factors and tradition is not to be underestimated. Individuals with a high degree of cultural intelligence consciously pay attention to said facts and work hard to improve own knowledge. An aspect of leadership that ought to be considered focuses on followers rather than leaders, meaning that in a certain way everyone is responsible and everyone has potential to become a leader.

The leader needs to consider not only how to persuade, but how the interaction between his/her exerted influence and influences exerted by others may lead to a positive outcome. A skilled leader may set goals for his/her followers just the way they expect him/her to do, and still use formal and informal processes ingrained in their culture. Managing an organization or a group with a culturally diverse workforce generally requires strong cultural intelligence.

Respecting diversity and recognizing the principle “Think globally, act locally!” is a positive objective of any organization. Additionally, leaders must possess appropriate knowledge and respect earned based on that knowledge. The advantage of a leader is in the ability to ‘read’ other leaders or colleagues from other organizations by taking into account their national culture and related peculiarities. Thoughts on leadership in most recent decades have shifted towards the idea of a modern leader who ought to transform and improve the management process primarily through encouraging employees to overcome their immediate personal interests and goals, and to not only accomplish the desired outcome, but exceed projected expectations. A leader who truly wants to succeed in this quest must not merely reward a certain performance of his/her employees and thus motivate their further work and advancement, but rather, he/she must present a compelling vision of the future and lead by own example, modeling the desired employees’ behavior and showing personal interest in each one of them.

However, even with the common comprehensive definition of the transformation management, employees from different countries have different expectations regarding their leaders’ behavior. In any case, it is possible that the implementation of the transformation management requires a specific set of personal traits not present in every leader. In short, leader must primarily be familiar with organizational rules. If he/she desires to be recognized as a leader distinguished by cultural intelligence, he/she must use knowledge and awareness to develop behaviors that can be adapted to any particular situation or context.

We can conclude that a leader who distinguishes himself/herself by cultural intelligence can select a management style that will create a balance between his/her usual leadership style, expectations of followers and demands of the situation. A good illustrating example authors use is found in the fact that “when riding the waves, skiing or cycling, in the beginning it is very difficult to find a balance, but over time it gets easier and easier and more natural” (Tomas, Ikson, 2011, 141-142).

## ***MOTIVATION AND MANAGING MOTIVATION***

Working with people by employing effective communication and adequate staff motivation, and managing by authority, responsibility, power and influence today represents a great challenge and task for all managers. Motivation, and in the narrow sense “work motivation” has proven to be one of the most important assumptions for effective performance and achieving set tasks for both individuals and entire organizations. Motivation in an organization is directly proportional to the quality of results achieved and the level of organizational development. For this specific reason, every manager wants to have a large number of motivated individuals and groups in an organization, which is why planned and systematic work on improving employees’ morale and motivation, an aspect falling within the scope of work of experts in human resources management, is of utmost importance. Academically speaking, motivation is an inner impulse that can urge a person to appropriately react to a series of internal events happening on different psychological levels (Mićović, 1983), such as:

- Ensuring basic needs
- Ensuring social needs
- Ensuring personal satisfaction.

From the organizational behavior perspective, motivation is the way in which drives, aspirations or needs manage, control or explain behavior of an organization. If motivation is understood as “an effective network of ideas and thoughts”, then every person has the motivation, although it is either qualitatively and quantitatively similar or different, and very rarely identical with that of other organization and/or team member. If motivation is viewed solely through the lens of a work process and realization of set goals of the organization, then it is either a “process of stimulating people to act to achieve desired goals”, or it is more a “management process that affects people’s behavior with regard to manager’s knowledge on human behavior in a given situation” (McClelland, 1961). The attitude towards defining motivation in an organization has been changing due to changes in the very nature of managerial work, in direct correlation with civilization factors, including: new scientific and technological disciplines, new approaches in applied psychology, introduction of meditation, relaxation and physical exercise skills, changes in the substance of expert-employer relationship, mobility of employment, new jobs, new managerial approaches, computerization of the society in its entirety, high degree of alienation, alteration of ethical awareness and morality, etc. The most influential factors in terms of attitude towards motivation in the workplace include:

- Psychological characteristics of people and their dedication;
- Complexity of work and new technological circumstances;
- Effectiveness of management approaches;
- Social aspects in relation to the organization and its environment.

Previous research on the importance of motivation for improving work processes clearly indicates a direct link between the degree of motivation and the effectiveness of results, even though there are numerous other important parameters that either directly and/or indirectly affect the level of achieved goals of the organization.

These include: personal skills, talent utilization, material resources, level of improved professionalism within the organization, hierarchy of values and positions, morals, ethics, culture, socialization level, personal and collective responsibility, commitment to the idea and assurance in strategic guidelines, and management method of the top management in the organization.

Motivation factors represent different values, situations, standards and norms that either positively or negatively affect the level of motivation. Major positive motivation factors or so-called “motivators” are achievement, recognition, personal work, responsibility, advancement and personal development. Negative motivation factors or so-called “demotivators” include inefficient administration, incompetent supervision, poor interpersonal relations and inadequate personal qualities of a manager, insufficient reward, and poor working conditions.

Common for all demotivators is “deviation from the expected” both in terms of efficiency and accountability of administration, lack of professional qualification of superiors, unfair and unequal managerial treatment in respecting those who really work hard and those with poorer results who, nevertheless are protected from superiors due to managers/team leaders’ inadequate knowledge, integrity and job understanding, unequal or insufficient reward as well as unsuitable work conditions in terms of employees’ needs for good performance of assigned responsibilities and duties.

In a practical sense, approaching different motivation theories must differentiate between three paradigms that are based on:

- I. Needs
- II. Processes
- III. Behaviors.

Even though motivation, based on the definition, is a personal phenomenon, in an organization it represents a systemic problem that must be addressed and modified based on the structure of the organization, its objectives and real achievements. Certain authors suggest first analyzing the entire system in which members of the organization work, and then looking at the impact motivation and behavior of individuals produce on work efficiency (Maslow,1970, Kanfner,Heggstad,1997). They believe the system itself comprises three following groups of variable parameters that affect motivation in an organization:

1. Individual characteristics (interests, positions and needs a person brings to the organization. Given that prior to arriving into an organization people differ based on their individual characteristic, they clearly harbor different or possibly similar motives. That is why same motivation does not produce the same effect with everyone!)

2. Job characteristics (tasks and job qualities employees consider satisfactory, further resulting in greater responsibility and work motivation),
3. Work situation qualities (factors in the work environment that stimulate productivity. A particularly important aspect is the system for evaluation and reward managers implement, along with the reached level of interest the organization shows for its employees).

A particular aspect in the systemic approach to motivation is modification of employees' behavior that includes a set of various techniques managers can use to generate individual behavior that would be adequate for assumed work tasks or set objectives. The most common methods or techniques managers can use to timely and positively change the behavior of their subordinates include:

- Positive reinforcement or support,
- Learning by avoiding negative consequences,
- Absence of reinforcement or support,
- Punishment.

Managing work motivation is one of the most important aspects of work of every manager, especially manager who cares about human resources in an organization. A global economy and proliferation of new technologies, informatization with a precise control of the entire work process and various forms of inter-organizational business networks in consolidating capital and prestige in the market have imposed the importance of motivation at the level of the organization and its members (Kanfner, Heggstad, 1997). Hence, managing work motivation may be conducted on a macro (focused on the organization) or micro level (focused on the individual).

**A.** Measures and activities that may be undertaken to manage motivation on the macro level include:

- Researching relationships in the organization
- System development
- Analysis of regulatory procedures and rules
- Motivation factors incentives
- Support for factors concerning "business hygiene"
- Improving communication
- Improving participation in decision-making

**B.** Measures and activities that may be undertaken to manage motivation on the micro level include:

- Legalizing personal needs
- Creating opportunities for development
- Influencing individual efficiency
- Positive reinforcement in the workplace
- Reward
- Continuity of success

- Type of reward
- Advancement
- Improvement
- Culture within an organization
- Cooperation and communication
- Expected task performance
- Feedback
- Leadership
- Realistic estimate
- Self-confidence and faith
- Sense of personality

## ***CONFLICT AND MANAGING CONFLICT***

Conflict in an organization represents a disagreement between two or more members, groups or teams because they have to share insufficient resources or work activities, or have different statuses, objectives, positions or perceptions. Modern approach to conflict suggests that conflict is inevitable, and in many aspect even useful for successfully and efficiently resolving certain situations and issues. Even though literature differently interprets the mere essence of a conflict given the approach and the method of its resolution (conflict of interest or values, disagreement with general objectives, low level of interpersonal relations, influence of demotivation factors, dysfunctional tendencies in outward or inward organizational development, etc.), it is evidently one and the same process. It can have both positive and negative qualities that must be diagnosed in time and the negative impact on the entire organization or work of individual teams or individuals in the organization prevented.

It is very important to distinguish early on between conflict and competition, since the two phenomena are often jointly presented (Stoner, Wankel, 1986). Competition is created when group's or team's objectives are not equal and harmonized, and when groups or teams cannot interfere or influence each other. If a window for interfering with or influencing work between groups and/or teams arises, the conflict ensues. As opposed to competition, cooperation and conflict do coexist, as the opposite of cooperation is not conflict but absence of cooperation. Based on the definition, cooperation is a process in which two or more groups/teams work together to jointly achieve common objectives. Based on the aforesaid, a common denominator in a modern understanding of conflict is that conflict is far more functional and positive in an organization than it is directly destructive, and therefore human resource managers and managers in general must timely recognize conflict and manage it by minimizing its detrimental effects and accentuating useful aspects the conflict may produce (Rahim, 1985). Experienced and skilled manager must be able to not only identify conflict but also the conflict phase.

Conflict process has 6 following phases:

- Potential conflict
- Emerging conflict
- Identified conflict
- Personal conflict
- Conflict episode
- Conflict consequences

Even though the spectrum of conflicts is very diverse in terms of the adopted resolution approach, emergence aspects, relations within an organization, team structure and personal traits, one of the educationally most explanatory conflict classifications is the following (Mićović et al., 1983):

- Conflicts based on the source and cause (include subjectively induced conflicts due to poor interpersonal relations, negative personality structures, opposing attitudes, opinions and interests, and those objectively determined due to various organizational, technological or economic problems),
- Conflicts based on actors and levels (there are three types of conflicts based on actors: within oneself, between individuals, and between groups/teams, whereas based on levels we can differentiate between five possible types of conflicts: within oneself, between individuals, between individuals and groups/teams, between groups/teams within an organization, and between organizations),
- Conflicts based on onset phases (include potential, emerging and identified conflicts),
- Conflicts based on work and management levels (include vertical, between various work and management levels within an organization, and horizontal emerging between individuals or groups working within the same organizational level),
- Conflicts based on its character (include destructive, due to emotional intolerance or disagreement with work objectives and work methods, and constructive emerging due to aspirations to increase individual creative capacities).

Before we proceed with explaining the conflict management procedure, it is important to learn about potential conflict prevention activities within an organization. Human resource manager must permanently monitor and insist on the importance of human potentials, value objectives and needs of members of an organization, work on risk minimization, create a climate of understanding and respect, support informal groups in their strive to resolve problems, support the culture of self regulation in relation to the culture regulated by authority, influence the division of responsibilities according to levels, encourage innovations and practicality and be active in harmonizing new strategic interventions with structures and processes in an organization. Since conflict and the entire collaborative process significantly influence the functioning of an organization, it is necessary to recognize models, procedures and methods for managing conflicts.

World Health Organization has suggested the following measures and activities the manager must undertake in managing conflict situations (WHO/EURO, 1981):

- Pay particular attention to individuals or groups that are “troublemakers”
- Work intensively on improving communication
- Precisely define “superior objectives”
- Examine the nature of mutual dependence
- Accept and take the risk for proposed changes
- Show authority and “power” when needed
- Limit the activity of opposing sides
- Work on building mutual confidence
- Work on joint acceptance of satisfaction and motivation
- Work on creating empathy towards the opposing side.

Modern management refers to three main outcomes in resolving conflicts with three outcome options, namely when both sides either win or lose, or when one side wins and the other loses. Pragmatic approach in managing conflict involves support for both cooperation and rivalry within the same process as they are not mutually exclusive. One of the current approaches in managing conflict presumes precise positive traits that must be adequately stimulated. Managers and human resource managers nowadays have at their disposal three most important methods for managing conflict, namely:

- I. Conflict stimulation
- II. Conflict minimization, and
- III. Conflict resolution.

Managers should stimulate and control conflict in instances in which it is evident that conflict may be useful for organizational development or teamwork efficiency. Stimulating methods include:

- Bringing people from the outside,
- Supply,
- Organizational restructuring,
- Rivalry support,
- Appointing appropriate managers.

Application of the conflict minimization method is far more present than conflict stimulation, as it reduces antagonism created by conflict. This method is mostly employed in situations in which the conflict has already gained its full intensity as a destructive and disharmonic force for the organization.

Conflict resolution method should be applied once conflict reaches a phase in which any further postponing may produce serious consequences for the organization. For that purpose four methodological forms are applied (Muller, 2009):

- Changes in the organizational structure (targeted restructuring of an organization, changes in sections of the main organizational matrix, with different links, adequate increase in responsibility where required and new more efficient groups/teams in the organization).

- Authoritarian problem overpowering (situation in which the problem is not resolved but overpowered by forcing the losing party to accept the position of a higher authority or higher force).
- Compromise (situation in which managers try to convince opposing sides to ‘sacrifice’ some of their positions or requests in order to allow themselves to ‘live’ with their problem even though they have not resolved it completely).
- Joint problem resolution (method for resolving intergroup conflicts with three possible problem resolution options: consensus, confrontation or acceptance of a higher, superior objective. It is important to note that conflict between groups leads to a greater cohesion within a group, whereas acceptance of a joint, higher goal creates greater cohesion between groups).

## ***REPRESENTATION AND INTERPRETATION OF RESEARCH RESULTS***

Research measures a wider set of elements comprising motivation and conflict in order to study the structure and relations between those elements with employees in education, by employing the so-called “factor analysis”. The research included a sample of 247 respondents working in high schools. Respondents were presented with two groups of questions. The first set of questions included questions concerning work motivation, whereas the other set of questions were directed toward conflict. Respondents were within each question provided with answers, each carrying a certain number of points ranging from 1 (as the least significant) to 5 (as the most significant). Respondents within each question assigned values from 1 to 5 to provided answers based on which we gathered results further presented in this study:

*Table 1: Overview of main characteristics of respondents*

Characteristics		N	%
Gender	Female	149	60.32
	Male	98	39.68
	Total	247	100
Education	High School	23	9.31
	Associate Degree	47	19.03
	University Degree	167	67.62
	Masters Degree	7	2.83
	PhD	3	1.21
	Total	247	100
Work type	Administrative staff	22	8.91
	Teachers	47	19.03
	Professors	151	61.13
	Pedagogues and	7	2.83

	psychologists		
	Lawyers and economists	14	5.67
	Science workers	6	2.43
	Total	247	100

### ***GROUPS IN THE MOTIVATION FACTORS SAMPLE***

First question “Motivation for professional orientation” explains the largest number of the total variance, where “motivation at work” is defined by the following elements:



*Figure 1: Motivation for selected professional orientation*

Analysis of obtained results represented in Figure 1 indicates that personal income is a priority in selecting a professional orientation. The second most important factor is personal development, i.e. intention to realize professional desires of employees. Opportunities for professional advancement at work: individual is motivated to professionally educate and train only if he/she is convinced that such behavior will realize personal priority objectives regarding professional advancement, and consequently an adequate salary. Personal development in correlation with personal salary leads to the next specific factor, namely “success at work” or participation in the latest work advancement developments in a selected business activity.

Second question, “What demotivates you the most at work” is defined by the following elements:

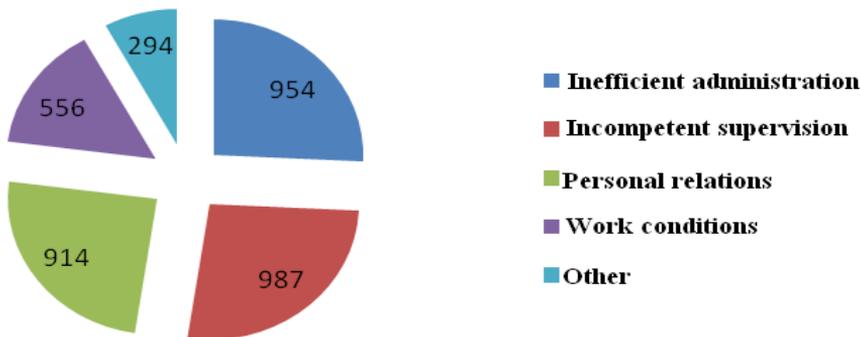


Figure 2: Demotivation factors in the workplace

Selected element that influences demotivation of employees the most is incompetent supervision, clearly pointing to the organizational management or the organizational process within the organization. Inefficient control leads to poor results, and therefore demotivates employees.

A third question refers to variables directly defined by the following motivation factors:

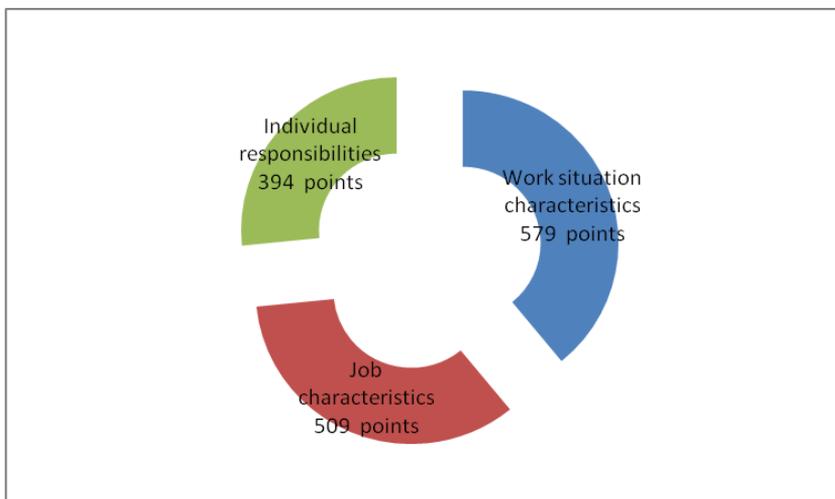


Figure 3: Factors influencing motivation the most

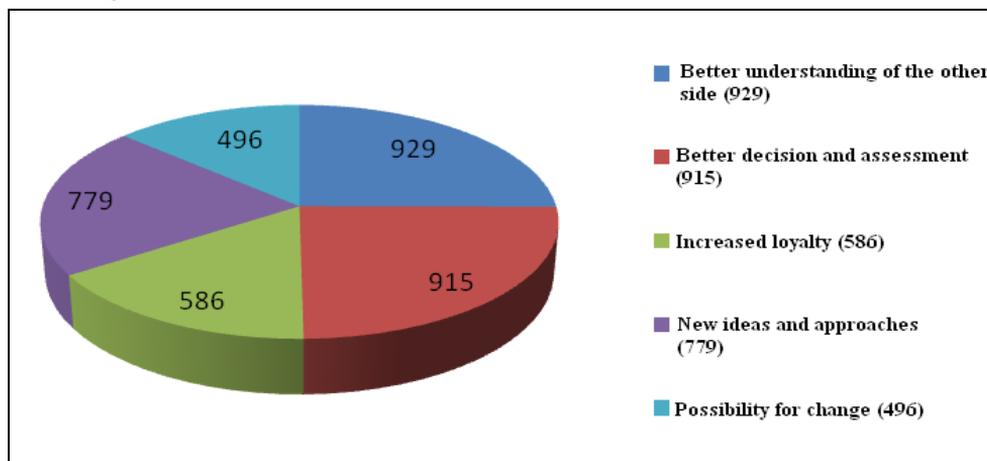
The first most important variable defining the third motivation factor at work is the “work situation characteristics”, whereas the second is “job characteristics” indicating the significance of attitudes towards opportunities for and levels in accomplishing work tasks in terms of their development, mutual disharmony, partiality, lack of organization and formalism in regards to the opportunities, expectations and social significance.

Conducted analyses show specific interdependence between work and motivation in all organizational systems. The analysis also shows that work motivation, namely positive and negative effects thereof, must be considered from psychological, economic, sociological and other aspects, in other words, with an interdisciplinary approach.

Scientific studies confirm that motivation is an unavoidable work and development factor playing a significant part in encouraging and satisfying diverse employees' needs. Timely insight in multiplicity of human needs and motivational impulses ensures grounds for designing and creating suitable motivational strategies that will allow all employees to search and use available options. Changes in the work content may further encourage and speed up introduction of new work methods and techniques, directly and positively influencing a range of human abilities and creativity.

### ***WORK CONFLICT SAMPLE GROUPS***

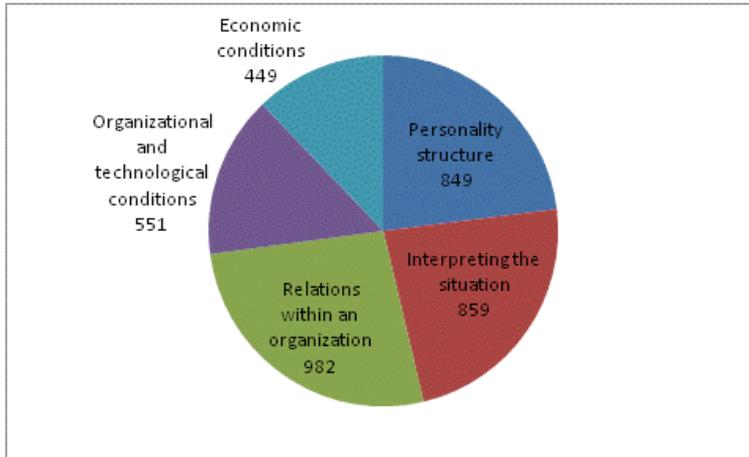
The first factor is a portion of the total “work conflict” variance defined by the following elements:



*Figure 4: The most significant positive effects of work conflict*

The first response in a sample was “better understanding of the other side”, indicating a need to work on building mutual trust and creating empathy towards the other side. The second answer was “better decision and assessment” indicating a need to improve communication and joint acceptance of satisfaction and motives. The third answer was “new ideas and approaches”, in other words, creative possibilities of opposing sides or individuals as support for innovative processes. The fifth answer was “possibility for change” indicating a desire for change through different types of connections, adequate increase in accountability and new efficient teams in the organization.

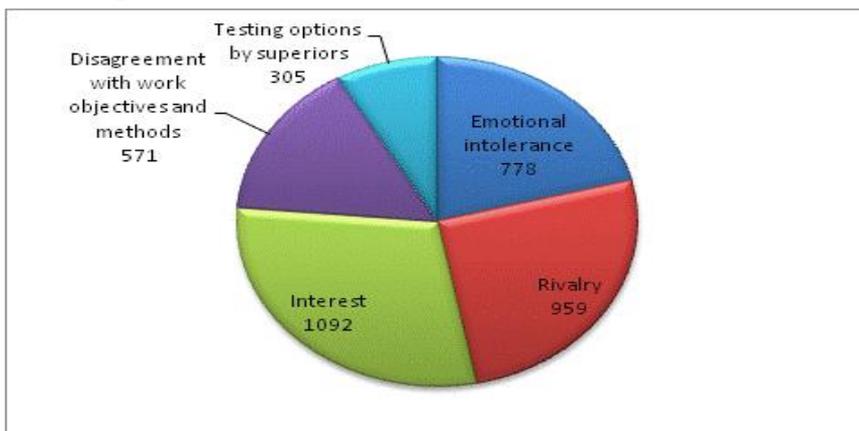
The second factor is defined by the following elements (Figure 5):



*Figure 5: Causes of conflict*

The first answer in the sample was “relations within an organization”, indicating a need for joint efforts in resolving issues, considering that conflict between groups and individuals leads to a greater cohesion within an organization either by accepting joint objectives through a consensus and confrontation or by accepting greater and superior objectives. The second most commonly provided answer was “interpreting the situation”, whereas the third most commonly provided answer was “personality structure”, indicating the significance of situation and individual determinants of a personality (conscience, independence, interests, values, needs, academic level, intelligence, etc.). There are also other personality determinants such as: creativity, moral values, social status, training, prestige, etc.

Variables presented in Figure 6 define the third factor:



*Figure 6: Created conflicts by character*

The most commonly given answer concerning the third factor was “interest” as a consequence of different goals, different statuses, positions, etc. The second most commonly given answer was “rivalry” containing vertical conflicts (conflicts between various job and management levels within an organization) and horizontal conflicts (between individuals and groups within the same level in an organization). The third most commonly provided answer was “emotional intolerance” including either destructive conflicts due to emotional intolerance or disagreement with goals and/or work methods, or constructive conflicts emerging in an attempt to increase certain creative capacities.

Prescribed scope has limited our study of these complex issues. Respondents were able to select their priorities between three motivation factors and three conflict factors in a work environment. All respondents provided answers to given questions (previous ranking of answers) regardless of their group affiliation, age, gender, employment tenure and education. The study found that there are differences in ranking answers based on said categories, just as there are certain correlations between said motivation and conflict factors in the work environment and their influence on the business culture.

## ***CONCLUSIONS***

- We investigated different influences using a sample comprising 247 education centers’ employees regarding positive and negative motivation factors and two conflict categories: real professional differences and power struggles and personality issues.
- The objective of this research was to establish the relationship between organizational culture and conflict management styles together with motivation approaches in the workplaces.
- Approaching conflicts with a positive attitude is the best way to make the most of it and emerge at the end of the tunnel with more creative solutions.
- Business culture does influence motivational practices in terms of whether the culture is task-orientated or person-orientated.
- Future studies on organizational and business culture must focus on a greater number of variables, in order to learn about, understand, explain and foresee professional and individual participation of groups and individuals in business processes and realization of business results of any organization or organizational unit.
- Studying these complex issue requires complex theoretical, empirical and interdisciplinary research, which in addition to motives and conflicts must include professional capabilities, psycho-social personality traits, employees’ attitudes towards work and profession, and in particular, attitudes towards acquiring knowledge and skills.

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# **THE TRANSFORMATION OF TRADITIONAL ORGANIZATIONS TOWARDS A MODERN APPROACH BASED ON QUALITY MANAGEMENT AND EMPLOYEE MOTIVATION**

*Marina Gasic, MSc*<sup>29</sup>

## **ABSTRACT**

*Companies must seek to optimize their business rather due o increasing competition. Profitability is the biggest reason why companies do business, and thus develop new approaches and ways to make operations more efficient.*

*Modern business is different from traditional in several aspects. First, employees are better informed, with better systematically education. Physical work is replaced by the intellectual and service sector dominates the production. Apart from this, there are also changes in the business that are very fast acting, and thus decisions are made at the time the problem occured.*

*The task of recruiting and retaining quality people in every organization is a part of human resource management. Appropriate human resources are the individuals in the organization who contribute largely achieving the objectives of the management system.*

*The leaders of modern organization are significantly different from those of traditional, because today's economic situation often leads to layoffs to reduce labor costs in order to improve decision-making processes, whereby to be more effective and efficient with the aim of improving the overall quality of the organization's business. It is in these new situations we distinguish new styles of management such as transformational leadership, training, „superleadership“, servant leadership and entrepreneurial leadership. Those who stand out are leadership styles that allow the inclusions of employees to demonstrate their abilities.*

*One of the main tasks of a manager is to fully understand the process of motivation to better influence the behaviour of followers and thus make it more consistent implementation of the organization's objectives.*

*Motivating subordinates is implemented with various strategies such as managerial communication, then the theory of x-y theory, design work place, behavioural change, Likert management systems, in-kind and cash incentives.*

**Key words:** *Leadership Style, Employee Motivation, Human Resource Management, Intellectual Capital, The Competitiveness of Enterprises*

**JEL Classification:** *B50, M54*

**UDK:** *005.591.4 005.32:331.101.3 005.336.4 005.336.3*

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## ***INTRODUCTION***

Knowledge is becoming crucial, and thanks to globalization and the development of technology innovation has become key to global competition. Flexible workers are becoming a central factor in business and thus encourage the achievement of competitive advantages. The unification of the world into one system makes globalization that is actually achieved by constant information and technological progress. Thus enables the transition from a traditional economy to the "New" economy, which is also called "knowledge economy". Classic resources of production are land, labor and capital, but in today's modern world, the main resource is knowledge. The only thing that could be recognized through people is their knowledge and the most important is that it can be constantly renewed.

Employed invest their knowledge in the company in which they work, so the employees pay should not be considered a cost, all the benefits that are focused on employees should be considered an investment. Human resources are very important backbone of management and governance, as well as a mechanism of forming effective, accountable, transparent and quality of public administration. Management flexibility creates new demands of human resources.

About mergers and acquisitions of companies is written for many years, as well as their activities where there are numerous studies. Within society there is divided opinion on the effectiveness of acquisitions, taking into account the fact that the performance of the company after the takeover is affected by many factors, that opens up space for scientific contribution in identifying the impact of the style of management to successfully manage change in firms that are taken over.

Today, this modern world is ruled by knowledge and technology, education, expertise and innovation of employees, and the elements which are crucial to master change and competitive advantage for organizations, and societies as a whole. Training and development of employees is in constantly growing, so there is an investment in the skills of employees, regardless of whether they are on the macroeconomic or microeconomic level.

Unfortunately the Republic of Croatia and its organizations are not particularly aware of the level and quality of education, which is actually a key to success. Specifically, in Croatia there are no similar studies specifically based on the microeconomic level.

From the earliest beginnings of the existence, man was forced to learn, develop and prosper. Hence the definition of how human learning actually is preparing to meet their needs. The history also came to the distribution of work and work organization, and contrast study also belongs to some kind of preparation for life in a society.

In the twentieth century, industry and later tourism and transport have experienced unimaginable development and progress. There have also been major changes within the community as well as the economy. When it came to the oil crisis in the early seventies, it comes to question the environment that become

unstable. The reason for this is the so-called completion of so-called Cold War and the disintegration of the socialist and communist social system that major problems are due to a market economy and market relations. In contrast, East Asian states provide great economic progress, regardless of the crisis that has engulfed the late nineties. Globalization is increasingly becoming the rule in the society and economy and slowly affects all parts of the world. Some economic activity in some parts of the world were created in the 21st century, and some are still in the developmental process, and therefore there is a crisis of certain professions, while some propulsive branches are enable to progressively develop.

The progress of the economy and economic relations is reflected in the struggle for consumer's preference and service users themselves. Many international organizations are in the process of closing, while others manage to turn their attention to other activities. Due to such situations there is a clear line between rich and poor.

Information technology experienced the largest and fastest development. It is important to notice that the time from discovery to using specific applications is reduced, while the process of obsolescence of certain knowledge accelerates, which corroborates the fact that knowledge knows obsolete before another generation of students or student ends in their education.

Technical education of employees in production and development institutions must follow changes in the environment in order to be competitive. Social changes in recent times require more general education, so the general social and technological progress must use it. It was concluded that education has become the rule in all sectors of production, but in the economy as well as in science.

Many authors, like (Vujić, 2004) repeatedly warned us that a major factor in successful organizations is to adapt to change, as well as their monitoring in the environment. The continuous process is an ongoing training and education.

In the world there is a major problem for graduates who allegedly do not have enough knowledge and skills to work. Therefore, many countries are trying to incorporate mechanisms for rapid adaptation process in their education systems, reviewing the major changes in the environment. These school systems are joined by numerous representatives of chambers of commerce as well as scientific institutions so the programs become more contemporary.

Science, engineering and technology are in great progress and require a quality education. Accordingly, there is a development of organization that has its own interests, and individuals with their needs and desires. Thus, interests are opposed, and the success of the organization comes aligning the interests of the one and the other.

Interests of the organization and the individual one are completely different and can lead to conflicts. It is necessary to satisfy the interests of the organization as well as the interests of the individual, whom sometimes is not easy to achieve, but we must weigh the effort of education and training of employees. Knowledge is part of the organizational structure that is increasingly gaining in importance and affects all aspects of society. Education is not only the area of human resource professionals and managers, but the whole enterprise, which covers all employees.

It is very important to recognize motivation as a means of managing human resources, also recognizing the important when choosing a motivator that will in the course of this work be the target. In addition to human capabilities and knowledge there is increasing weight to the interests of individuals and their motivation. Unfortunately, today's managers forget that in front of each machine still stand a man, and his knowledge and skills they possess.

Quality management, good team spirit, meaningful planning and good organization, in a familiar environment, encourages and rewards knowledge and skills, thus achieving the desired business objectives in the interest of the company and its employees.

According to Maslow theory, by Abraham Maslow (1943) Vujić (2004) says that every man is trying to satisfy five basic needs - physiological needs for love and security, social needs, the need for respect and power and the need for self-fulfillment. All needs are psychological in character part the first, which business linked is primarily related to money.

There are many theories, like the theory of scientific management and the theory of achievement, they try to explain the nature of motivation and especially help explain the behavior of individuals in specific situations. There are also a number of motivational techniques that are available to managers.

In the entrepreneurial society individual staff as well as their motivation and specialization and promotion become part of the development program of integrated enterprise quality. The most productive firms become one that fully includes the premise of employees in their work. Firms has differ two different types of strategies that must be closely linked with the way of competition in the market, and by the development, engagement, guiding and motivating and controlling internal resorce. Compensation strategy should be integrated with the business strategy, formulated and to enable the achievement of long term objectives of the business policy and human resources policy.

## ***MOTIVATION, ITS THEORY AND MEASUREMENT OF MOTIVATION***

In the process of introducing into work it is necessary to inform applicants that the volume of his work relates to the structure of the organizational unit, to point out the role that the unit has in the overall enterprise. It is very important to create a sense of importance, because it will be because of that candidate socialize in the company. On top of the charts is to develop strong motives, to describe the goals of behavior.

Motivation may ultimately be viewed as a series, which consists of a need to feel, and needs lead to the goals to which we aspire, which eventually leads to satisfaction or dissatisfaction, depending on the performed action.

The motivation is affected by many factors, which can be divided into three groups

1. Individual characteristics
2. Characteristics of work
3. The characteristics of the company.

Individual characteristics are those that describe the needs, interests and character of the individual. Some are in turn driven by money, some with work security; some are looking for adrenaline, so forth. Characteristics of individuals almost always have to be in the form of companies to encourage employees who contribute to the achievement of company objectives.

Job characteristics describe a job where unanimity is essential, team-mindedness, and above all the responsibility. It is necessary to harmonize the relationship between individual characteristics and job characteristics.

Characteristics of companies are simply all the elements that contribute to the efficiency of the company, or company rules, personnel policies, a well-established management and process rewarding. They are designed to attract new and retain current employees.

In the modern system of business, knowledge and application of the foregoing represents an exceptional way to direct the individual and thus successfully predict individual and organizational goals.

Motivation precedes motif that represents the inner psychological and emotional boost for a particular activity. One can look back at a few parties; it may be of material or psychological character.

Defining motif come to the idea that motivation is defined as the collective notion of human behavior where it involves a lot of interconnected and interacting factors transforming into a motivational system.

Motivational system is a system of employed measures, advancement opportunities and training, achieving compliance and more.

The motivation for the work is the totality of the various methods and procedures for finding, maintenance and growth of the activities of labor. It represents the activity to encourage success at work.

The person who is responsible for making motivational system must be prepared to anticipate the interests and reactions of employees, because, of course, they are all of the different nature. Therefore, the motivational elements affect different on each person.

We distinguish several incentives for work, most notably are content and process theories of motivation.

The content theories (Vujić, 2004) include the theory of scientific management, followed by interpersonal relationships, then known Maslow's theory (Vujić, 2004) of needs, a theory of two factors and three stage hierarchy theories and the theory of achievement.

The theory of scientific management, by author Frederick Winslow Taylor reduces the human motivation to one motive, and that is paid. It occurs at a time when the earnings of employees were so low that they were concerned with existential needs.

The theory of interpersonal relationships, by author George Elton Mayo describes the relations within the group and the relationships between employees and managers of the company.

Hierarchy of needs theory or Maslow's theory is one of the most researched and most prominent theory as the author points out that motivation is a process that never ends. It warns that greater emphasis should be placed on continuous employee development. It is based on the assumption on the complexity of the human personality and its needs that are hierarchically structured.

The theory of two factors, the author Frederick Herzberg described as job satisfaction as an intrinsic factor, and job dissatisfaction as extrinsic factors. Intrinsic factors to motivators are achievement and recognition for a job well done. Extrinsic factors are caused by interpersonal relationships, financial or material incentives, work environment and more.

Theory of three stage hierarchy is also known as the "erg" and is based on Maslow theory. According to Aldelfereru there are existential needs, the needs of the connection, and the demands of growth and development. Existential needs are basic physiological and material needs; the needs of connectivity are needs of social character. The needs of growth and development describe the initial needs of individuals who use and develop their potentials where lower needs need to be saling, in order to execute multiple purposes.

The theory achievements of Mc Clelland and Atkins (Vujić,2004) highlight strong desire of employees for achievement and success. It is based on individual assessment of probabilities.

Further studies of individuals, groups and entire system of an organization are finding new strategies and principles of scoring, stimulation of workers. The process theories talk about it. It is such rules mostly are applied in procedural theory.

Process theory defines how a man motivates and how he makes each decision in certain situations (Vujić, 2004). Therefore, we distinguish between the theory of "path-goal", "VIE" theory, Fishbein model since 1975 (Vujić, 2004), the theory of commitment, fairness and expectations.

The theory of "path-goal" describes the path worker chooses in order to meet his personal goals. He will conduct them in a way that he ordered his vision of leading the line for their own advantage.

"VIE" theory was given by Victor Vroom in 1964 (Vujić, 2004) as a theory of valence, instrumentality and expectations. Valencia is assessment of the achievements of a particular goal. Instrumentality estimates that the employee may, for example to achieve a higher salary. Expectation is the attitude with which the individual can achieve his goal.

Fishbein model describes how some people can not make certain decisions without the opinion of others that are very important in their lives.

The theory of commitment by Patricie Smith and C. J. Cranny since 1968 (Vujić, 2004) is described as a model of what the ultimate effect of employees does not only depend on the amount of wages, but also on the amount of satisfaction level. Sometimes the only effect acting on his personal commitment.

The theory of justice J. Stacy Adams since 1963 (Vujić, 2004) evaluates the relationships between profit and investment. It is unfair if two people are taken for comparison, and are not really equal.

The theory of expectations by Edwards since 1954 (Vujić, 2004) is the driving force of a man with multiple goals should be and will always choose the one goal that makes the most impact.

Measuring motivation should be done at least once a year, because this is a very complex and demanding job. In the process of measuring motivation to work the problem arises because individuals are not aware of their behavior, and given that, they are unaware of their motives that initiate their behavior. When implementing the measures of motivation it is especially important to pay attention to the shape, weight and tone of the questions, if it is through conversation

Satisfaction at work is an individual's mental attitude towards work environment.

Various studies (Marušić, 2001, p. 264) have led to a ranking list of motives which is led by wages, then advancement, is the work interesting, working conditions. Most interesting in the above ranking is that wage-led, and in last place as the motive is knowledge. The problem in Croatian organization is because there is no built system of evaluation of human capital and promotion of staff.

Manager in order to predict the behavior of employees must know something about its goals and methods in order to know what to do to achieve those goals.

## ***INNOVATION KNOWLEDGE AND ACHIEVEMENTS OF EMPLOYEES***

Innovating knowledge of employees is contributing to their independence and greater business excellence. New knowledge takes time before it goes into technology and application, and it can not acquire and limited to the school. Knowledge is life-long and very important because it changes the person and makes it more capable for different and more effective action.

The modern economy is constantly renewed, it's advancing due to the large investment, but that investment can not exceed those investments relating to knowledge. The European Union has proposed to allocate at least 6% of the gross national (Vujić, 2004) income of all member countries for education. Investing in knowledge should be seen as an investment in existing and future business.

The effectiveness of economic and other activities are increasingly dependent on the general state of science and the level of development of technology, especially in manufacturing. Science is not just learning or gaining knowledge, but also the educational activities of people. Technology becomes the sum of knowledge.

Employer somehow becomes an educational institution, and the manager professor of his fellow colleagues.

In Croatia, the labour law even prescribe obligations to the employer, it is obliged to comply with the conditions of work and business, to provide employee training, but there is also a law in reverse (Vujić, 2004).

The policy consisted of principles, criteria and specific requirements is an integral part of the business and development policy of the company.

We distinguish between formal, unformal and informal education. Formal refers to the classical education through regular educational system and its institutions. Informal education is reflected in the guild associations and is available to all citizens through the Internet and other communication flows individuals which are more accessible than teachers or mentors.

Performance management of employees is an important part of the job of management of human capital because it contributes to improving satisfaction of staff and business enterprises. Without effective feedback between managers and employees that process will be resulted in poor business success or a failure.

Throughout the year, employees are monitored and measured their working ability in the form of an unformal conversation or in more elaborate form lasting several days, which includes a variety of procedures. Such a process, depending on the results of the assessment, contributes to increased wages, then a higher level of hierarchical work, various benefits and personal development career.

Personal career combines individual and social interests as individuals and organizations actually become partners. It reflects the ability, interest and motivation of the individual through its activation during education and work. Professional development includes a period from sixth year of human life until retirement. Career progressively advancing depending on the status, remuneration and responsibilities.

## ***QUALITY MANAGEMENT AND THE REMUNERATION OF EMPLOYEES***

Management has multiple functions, most prominently is the conduct. The key competitive advantage is the ability to lead, leadership. Leadership is a very important element of business success of the company. Leadership is a process in which an individual influences a group or organization in achieving a common aim.

The functions of leadership are setting goals, then the motivation of others to achieve these objectives, management processes during the achievement of goals, the achievement of unity of effort, innovation knowledge, and adaptability of groups to local and global changes.

The difference between leaders and managers is that leaders have to take a vision, people and business excellence, and strive to keep together a group of people leading them in the right direction while managers are preoccupied with efficiency. Knowledge, temperament and other capabilities of leaders are important elements in the process of leadership.

Rational leaders listen subordinates, it participate in decision-making, and is accessible and tries to solve all the problems in its domain. Often this style is called socially sensitive. The leader structure and assigned tasks, highlights expectations that are expected of employees, as well as terms which subordinates must abide by.

Further research is drawing a line between autocratic and democratic leadership style. Autocratic style is based on a decision by one person that has completely unlimited power. In this style of management employees have no right to participate in decision-making, but subordinates are only notified of changes. This style allows for fast decision making, no employee view, and thus the leader increases its power. Contrary to this style of democratic leadership style, where employees are involved in the decision making process. Sometimes leaders held meetings on a particular topic, where employees share their opinions and base that counted the votes.

Author Renesis Likert in the 1970s (Vujić, 2004) developed four models of management systems: authoritative-exploitation, authoritative-benevolent, consultative and participatory democracy. Authoritative-exploitation consists in the fact that employees have no motivation, no communication in the organization's work, but only receive decisions from the top. Accountability is centralized at the top of the organizational hierarchy. Authoritative-benevolent system is described as approachable style of leadership where there is still some kind of reward system, as well as the communication and teamwork that is on a deeper level than the previous system. In addition, the authority is not only at the top, but it is distributed to the secondary level. In consultation system employees are involved in decision-making, communication is developed in all directions, there is developed teamwork as well as the system of motivation and responsibility extends throughout the entire organizational structure. Participatory democratic system is a leadership style in which the complete trust is in employees hands. In addition, we recognized a laissez-faire style of leadership where the leader does not behave like the leader. Actually they provide complete freedom to employees who are trying to achieve the goals set by managers. I can say that laissez-faire leadership style stands out as the most successful when managers collaborate with doctors, engineers and other professionals.

Reward system is located inside the motivation of workers, but also the system itself can cause unwanted behavior of workers. Reinforcement theory defines the access to the worker who has earned the award, and to repeat the same behavior in

the future, whereas expectancy theory emphasizes the expected rewards. In such cases, we distinguish between external and internal motivation where external depends on the rewards and inner stems from the very nature of work. From this context, it can be concluded that it is not always the rule that money is the only way to motivate employees.

Award program for results and operations in various companies is based on the criteria for calculating the bonus. Total bonus fund is determined for business year and consists of the sum of individual bonus amount for each employee. The criteria for calculating bonuses are systematized for each employee depending on workplace in organizational structure and the structure of the competence of the organization. Bonus performance is defined for each employee and contracted by annex contract for the current business year. The amount of possible realization is determined in advance by the rank and structure of competence.

Linkage between success criteria with the annual business plan is based on a monthly basis. Business rebalancing plan is associated with the share of the total prize fund. Standards are associated with monthly operating results to a practical way eliminating the problem about pre paid bonus that was not made. Organizations typically set limits bonus payments ranking between minimum and maximum realization of the plan, to the prize fund was stable and thus not be subject to constant revisions.

The criteria are related to the indices of gross accounts of individual companies and are connected to the system of calculation of wages. This system is suited for lower-ranked jobs with the criteria for a larger share of customer managers.

The sum of the individual criteria for each employee created a set of key elements of successful performance. The purpose is to select the criteria for the calculation of the annual bonus and the amount of shares in a percentage. The level of competence is different, and so is a measure of success, so as the amount of realized bonus. Employee accomplishing the tasks in a satisfactory manner has provided a constant bonus for months. But, for example, the Commercial Manager in addition to the task achievement of sales growth and profit must provide accounts receivable and purchase high-quality resources. As to his level of assessment is less, but consequently the work is judged on a stricter manner.

The annual bonus is provided for payment at the end of the business year and is a good mechanism for development workers. The organization benefits from a quality and efficient operation in terms of increasing the volume of business results, while the owner is assigned with a motivated and committed to the work employees, which, moreover, reward themselves with operating results. With this procedure it is achieved its main task, to transform the business environment in a modern system. Realized are the investments in the most important resource of a business organization, which are people.

## ***CONCLUSION***

In modern society, knowledge is a key factor in achieving competitive advantage. Employee knowledge and skills are the basic resource of organizational success, and continuing education and development have become a basic need. Organizations in the Republic of Croatia, unfortunately not sufficiently improve the knowledge and skills of their employees to meet the requirements of new technologies, increase their productivity and become more competitive. Hence there is a need for significant investment of Croatian organizations in the education and development of their employees, not only in order to be successful in the domestic market, but also to achieve competitive advantage in a growing and integrated European and world markets.

Productive forces such as land, labor and material capital that in an industrial society were the main elements of competitiveness in the modern information society is increasingly replaced by intellectual capital, and human resources. To help organizations become competitive is not so more essential to have the latest equipment, but people who are capable at all levels and who are willing to constantly improve their knowledge. Rapid changes in the business environment had a significant impact on changes in business philosophy and turning the man to knowledge. Education and training is no longer a privilege of only managers, but have to be implemented at all levels of the organization. Employees have become the most important resource of the organization, and their satisfaction is placed in the first place. Labour productivity and business performance mainly depends on the knowledge and motivation of staff. Many authors consider that the motivation should be the sole task of human resources management as motivated staff provides their full potential.

Education and training, and motivating employees is one of the most important forms of management and human resources development, and the transformation of human capital as the biggest investment of each company. People represent potential which is valid for a maximum, because by innovation knowledge and skills also with motivation is necessary to improve staff and convert them into equity by which the organization achieves competitive advantage.

Giving autonomy to employees relating to their work performance is something to deal with the psychological and managerial research. It may surprise you how much this case giving autonomy really powerful and how can help only if used correctly. Let's look in the mirror and think about what we would require to accomplish a good deal with customers every day.

People have to have a reason that will make them happy when they wake up in the morning and the reason it should not be the only one that applies to wages. It is not enough motivation. As a good employer it is necessary to allow employees to know exactly why they do their job and the best methods to get the job well done. It makes the difference between an employer who cares and one that does not care about people in its own company.

Flexibility plays an important role, not one that is obtained when the job is complete, but one that allows employees to do the job in the way they think is best. It is necessary to involve employees in the whole process of doing business so that they felt the importance of the work itself. Employees must have a good excuse why they go early in the morning for work, and if they are motivated on this issue means that they are well explained about the work and if there is a fair worksharing for the job. Payment only for quality work is not enough, because the quality work done will be difficult to become a reality if employees do not get the impression that something about them depends. It is that freedom that employees receive, and the employer it gives them because it gives them the importance they deserve and the space they need to be creative and the more the better.

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## ***ENABLING EMOTIONAL INTELLIGENCE: EXPLORING THE SOURCE OF MOTIVATION***

*Vaibhav Birwatkar, PhD<sup>30</sup>*

### ***ABSTRACT***

*To optimize organizational performance and ensure their long term competitiveness and sustainability, organizations need to be able to fuel their employees to work at or near their peak level. It is difficult to understand what motivates people without assessing what people need and want from their work. Motivation is commitment and obligation to perform tasks without discouragement or despair in face of failures and as well optimism regarding the future. Decades of interest in better understanding the determinants of and the processes though which employees decide to extend varying levels of work effort has resulted in a proliferation of work motivation theories into the determinants of work related behaviours. Emotions are a significant determinant of an employee's judgement about referents, rewards, and equity. Emotional intelligence is emerging paradigm discussed and researched widely in many organizations to improve businesses and employee performance. It can help an employee to identify his/her emotion and deal with it in a more effective manner. Once employees understand their subtle emotions, they can break the circle of causality and are motivated by the opportunity to develop their skills or capabilities.*

***Key words:*** *Emotional Intelligence, Motivation, Emotional Management, Empathy, Interpersonal Skills*

***JEL Classification:*** *J28*

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## ***INTRODUCTION***

The major concern of man has been work which has been a cogent and potent feature of both the old and modern societies. Work plays an important role in the daily lives of a person, in that it allows individuals to support themselves and others. It also takes a considerable part of the overall time at man's disposal during his life time, and the economic benefits accruable to him become a major index of his standard of living.

Attitude is the single most important factor that directly translates into the level of success achieved in many situations. It impacts success because it influences perspectives, interpretations, decision-making, actions, and results. Workplace emotions and attitudes are receiving a lot more attention these days in many other organizations. That is because emotions and attitudes can make a huge difference in individual behaviour and success, as well as in the organization's performance and productivity. Over the past decade, the field of organizational behaviour has experienced a sea change in thinking about workplace emotions. It has been said that people join organizations but leave their supervisors. It is a problem of relationships which is one of those core motivators.

Successful employees present an attitude that reflects positivity, competence, self-confidence, and a genuine intent to tap their full potential. The emotional drives and behavioral tendencies that feelings motivate are part of emotional intelligence. Emotional intelligence is the set of personal characteristics that have an impact on the way we feel, behave, relate to others, and handle job responsibilities. Emotional intelligence strengths help employees in remaining optimistic about their work challenges and in maintaining a high level of work ethic. Factors such as courage, consideration, and sociability are some other outputs of good emotional intelligence. In today's challenging world where uncertainties and cutthroat competition are virtually indistinguishable phrases, motivation is key to success. Motivation keeps employees interested and drives them to focus their efforts and take actions that help them attain their targets and taste success. Absence of the right attitude, lack of good emotional intelligence, and a low level of motivation could make them incompatible with others, lose direction, feel dissatisfied with their career choices and jobs, underperform in their roles, lose self confidence, and sub-optimally handle stress.

To be effective, today's leaders have to connect with people on a personal level and understand what drives their people. Emotionally intelligent leaders are attuned to their people. They see their people's strengths and weaknesses clearly, so they can foster that essential sense of competence. They become aware of how their words and actions support each employee's autonomy, competence and relatedness and either build or flatten relationships.

Emotional intelligence is the primary driver in leader effectiveness because leadership is about using influence and building effective relationships, which are largely emotional tasks. Leaders who put emotional intelligence into action are able to foster genuine collaboration. This fuels stronger interpersonal connection, motivating people through relatedness.

## ***EMOTIONAL INTELLIGENCE***

Emotional intelligence is defined as "the capacity to deal effectively with one's own and others' emotions", and encompasses a range of personal, emotional and social skills that help a person to cope with environmental demands and pressures. Emotional intelligence and understanding the role of emotions with regards to behaviour, performance, and development and maintenance of relationships is a new and emerging area.

It is an important factor in determining a person's ability to succeed in life and will influence their psychological wellbeing. Emotional intelligence provides an individual with an understanding of their emotional skills, and therefore a better understanding and awareness of how to use emotions effectively.

Our thoughts influence our emotions, and in turn our emotions influence our behaviour and actions. Therefore, given that leadership largely involves personal interaction and people management, it is essential that leaders possess the skills to access their thoughts and emotions, and to display sufficient emotional intelligence. People with better emotional intelligence typically have more success in personal and interpersonal interaction compared with people who have less effective ways of dealing with emotions.

The emotional intelligence is a subject that attempts to describe and explain the emotions status, feelings and human capabilities ( Zadeh, 2007). The emotional intelligence has been defined as the ability to comprehend and understand the emotions as to appraise thoughts and dispositions and adapting hem in such a way that results in the emotional and rational elevation and growth (Goleman, 1995). The concept of the emotional intelligence has given a new profound depth to the human intelligence. This is the tactical capability intelligence (personal performance) while the cognitive intelligence is the strategic ability (long term ability). The emotional intelligence allows for the prediction for the achievement, because it shows how a person immediately applies his knowledge for achievement. The emotional intelligence is a form of the social intelligence that is efficiently a suitable predictor with respect to the specific areas such as professional and educational performance. In other words, the emotional intelligence is the ability to control one's own feelings and emotions as well as the others' (Bar-on, 2000).

## ***TWO EMOTIONAL INTELLIGENCE MODELS (THE ABILITY VS MIXED MODEL)***

There are two predominant models of emotional intelligence: the Ability Model (Mayer, Salovey, 1997; 2002) and Mixed or Trait-based Model (Bar-On, 1997; Goleman, 1995). The ability model is represented by Mayer and Salovey who view emotional intelligence as an actual domain of intelligence composed of specific emotional and mental abilities (Mayer, Salovey, 1997). Ability emotional intelligence requires the use of maximum performance tests with correct and incorrect responses and pertains primarily to the realm of cognitive ability, which is accordingly most appropriately measured by performance tests (Petrides, Furnham, 2000). The latter, mixed or trait-based model, takes a narrow approach to emotional intelligence combining emotional abilities with elements of personality, motivation, and social skill (Bar-on, 1997, Goleman, 1998). This type of emotional intelligence pertains to the realm of personality which can be assessed by self-report questionnaire (Petrides, Furnham, 2000).

Mayer and Salovey's (1997) emotional intelligence model encompasses four interrelated abilities: perceiving, using, understanding and managing emotions. Each of the four abilities is discussed below.

- Perception of Emotion is the ability to perceive emotions in oneself and others as well as in objects, art, stories, music, and other stimuli. It entails identifying information conveyed by facial expressions, tone of voice, gestures, body posture, colour and other cues.
- Emotional Facilitation is the ability to generate, use, and feel emotion as necessary to communicate feelings or employ them in other cognitive processes. This entails the capacity to associate mental images and emotions. It also includes knowing how emotions influence cognitive processes such as deductive reasoning, problem solving, creativity and communication.
- Understanding Emotion is the ability to understand emotional information, to understand how emotions combine and progress through relationship transitions, and to appreciate such emotional meanings.
- Managing Emotion is the ability to be open to feelings, and to modulate them in oneself and others so as to promote personal understanding and growth.

The mixed model of emotional intelligence, represented by the work of Goleman and colleagues (Goleman, 1998; Boyatzis et al., 2000), includes emotional abilities, but also a number of elements that are best described as personality dimensions, as well as some aspects that may have little to do with emotions or personality (e.g., recognising the need for change; challenging the status quo, choosing team members based on expertise). The most recent version of the Goleman mixed model measures 20 competencies which can be organized into four dimensions: Self-Awareness, Self-Management, Social Awareness, and Social Skill. According to Goleman (1998), these emotional intelligence abilities are considered independent (each contributes to job

performance); interdependent (each draws to some extent on certain others with strong interactions); hierarchical (the emotional intelligence capabilities build upon one another); necessary, but not sufficient (having an emotional intelligence does not guarantee that the competencies will be demonstrated); and generic (different jobs make different competence demands). Each of the four emotional intelligence dimensions is discussed below:

- **Self-Awareness** concerns knowing one's internal states, preferences, resources, and intuitions. Self-awareness involves emotional awareness, which is deemed as the fundamental core ability of emotional intelligence, and ability to know one's strength and limits and self-confidence.
- **Self-Management** refers to managing ones' internal states, impulses, and resources. The self-management cluster contains six competencies, including self-control, being trustworthy, conscientious, adaptable, taking initiative, and having a drive to achieve.
- **Social Awareness** refers to how people handle relationships and awareness of others' feelings, needs, and concerns. It involves empathy, a service orientation toward customers or clients, political awareness and understanding others as well as ability to cultivate opportunities through different kinds of people.
- **Social Skills** concerns the skill or adeptness at inducing desirable responses in others, including general communication ability, ability to influence others, manage conflict, inspire others via a vision, recognize and catalyze change, collaborate with others, and promote teamwork.

### ***WHY EMOTIONAL INTELLIGENCE?***

In recent years, widespread attention has been given to the concept of emotional intelligence. Much of this can be attributed to the popular book *Emotional Intelligence* written by Goleman (1995). In this book, Goleman made strong claims about the contribution of emotional intelligence makes to individuals' success and work performance. He identified IQ as contributing 20 percent towards life success and intimated that the remaining 80 percent of life success may be attributable to emotional intelligence. Bar-On et al.,(2000) conducted a study examining the impact of emotional intelligence on occupational performance, and the results indicated that the ability of emotional intelligence on identify occupational potential accounts for approximately four times (25 percent) more variance than IQ (6 percent) when compared with Wagner's extensive meta-analysis of emotional intelligence (Wagner, 1997). In addition, Stein and Book (2000) in their book entitled *The EQ Edge*, which draws on research across 30 professional and managerial career fields, revealed that anywhere from 47 percent to 56 percent of work/life success is the result of emotional intelligence, with the range being related to job type. Although there is not a consensus amongst researchers as to the extent to which emotional intelligence predicts one's

performance, these studies have revealed that emotional intelligence is a strong predictor, even more powerful than IQ, in determining one's success and performance (Abraham, 2000; Ashforth, Humphrey, 1995; Ashkanasy, Daus, 2002; Goleman, 1995, 1998).

Martin (2004) noted that people are sometimes successful not because of their knowledge of the tasks, but due to their ability to manage people socially and emotionally by using charismatic personalities in their communications. This is embodied in the emotional intelligence concept as "the ability to effectively reason about emotions and use emotions to aid cognitive processes and decision making" (Mayer et al., 2000). It reflects the ability to understand and manage emotions and their interrelations with cognition both in the self and in others to enhance effective functioning. Martin (2004) suggested that people with high levels of emotional intelligence have a natural aptitude for emotional perception and can utilize this to move people to respond positively to them. Mount (2006) conducted a study to examine the relationship between IQ and emotional intelligence in five roles in an international petroleum industry, and the results revealed that emotional intelligence competencies, such as self-confidence, empathy and teamwork, act as catalysts that enable the cognitive intelligence competencies and the individual's skills and knowledge (expertise) to achieve international business successes.

In other words, the emotional intelligence competencies created an environment that allowed the other competencies to be maximized, thereby giving them traction for performance. Most importantly, emotional intelligence is thought to be highly malleable and can be developed through appropriate learning interventions, life experience and is amenable to training (Goleman, 1995; Mayer, Caruso, 1999; Jaeger, 2003, Lopes et al., 2006). This statement is supported in the research conducted by Sala (2002) in developing a programme to increase emotional intelligence at work. The results showed an improvement in emotional intelligence of individuals who had participated in an emotional intelligence training programme compared to those who had not.

## ***MOTIVATION OF EMPLOYEE***

Increasing motivation, commitment and engagement levels are key organizational aspects nowadays. The development of compensation policies has an important role in motivating workforce to deliver high levels of performance, discretionary effort and contribution. The process of motivation usually starts with someone recognizing an unsatisfied need. Then a goal is established to be reached and that way to satisfy the need. Rewards and incentives can be established for people to better accomplish the given goal. The social context will also affect the motivation level. This context consists of organizational values and culture but it also includes leaderships and management as well as the influence of the group or team in which a person works. Motivation can be intrinsic or extrinsic. Intrinsic motivation can be described as the process of motivation by work itself in so far as it satisfies the personal needs of the

employee. Intrinsic motivation is self-generated and it is thought that people seek for a job they think will most satisfy their needs. The factors affecting intrinsic motivation include for example responsibility, freedom to act, courage to use and develop persons own skills, interesting tasks and opportunities for advancement. Extrinsic motivation is the amount of effort other people give to the person to motivate them. Extrinsic motivation is for example the rewards management provide such as pay rise, praise or promotion. Extrinsic motivators are efficient but the influence doesn't last long. Intrinsic motivators tend to have a longer effect as they are inherent and not imposed from outside. As the needs of individuals differ a lot, it is important to concentrate carefully on the attachment of goals and incentives given when goals are accomplished. Motivation theories help to understand different motivators. Motivation theories have been examined for decades. These theories can be implemented to the company's human resource policies to get the best out of the employees.

### ***EMOTIONAL INTELLIGENCE AND EMPLOYEE MOTIVATION***

Emotional intelligence can contribute to the achievement of a person. For example, reflected with the salaries, salary increases with the increase of the position of the company. Emotional intelligence allows a person to build positive relationships at work, work well in teams, and build social capital (Yao, 2009). Motivation often depends on the support, advice, and other resources that available. Emotional intelligence also can contribute to the motivation of a person to enable someone to set their emotions in order to cope with stress and perform well under pressure, and it also can help someone to adapt with organizational change.

Thus, organization is a social system in which members always interact with each other and also with the external members. The interaction with the external member is referring to the interaction between customers, suppliers and others. These interactions are usually needs the great of emotional that can form the basis of human behavior. The employee that has a high level of emotional intelligence can clearly feel the emotions of colleagues and managers and accurate understanding of the meaning of other behaviors, until they can make the accurate evaluation about their working role that expected by others, and then performs adaptive behaviors. Therefore, they are more harmonious and more quickly integrated into in organization, and achieve higher performance.

In conclusion, there are many researches that have shown a positive relationship between emotional intelligence and motivation. Therefore, this study was conducted to propose a theoretical framework highlighting the link between emotional intelligence and motivation.

## ***THE THEORETICAL FRAMEWORK***

The sample was delimited to managers from various manufacturing as well as service sectors including equal representation from domestic as well as MNC companies. The study was further delimited to managers of only Mumbai corporate sector. The population consists of all the managers of the various industries in the Mumbai corporate sector. This includes managers of both domestic as well as MNC companies.

The sample of the study comprised of 780 top management level managers from manufacturing and service companies of the Indian corporate sector. A total of 52 companies were selected as the final sampling unit. Out of these 52 companies, 26 companies were of manufacturing type and 26 companies were belonging to the service sector. Out of the 26 companies of manufacturing 13 companies were domestic and rest 13 companies were MNC's and from each company 15 managers were selected.

Emotional intelligence levels and competencies will be assessed through a pre-designed Questionnaire. The areas covered by this questionnaire can be briefly summarized as follows:

- The first part was related to finding the awareness level regarding emotional intelligence as well as its related competencies.
- The second part consisted of a 5 point rating scale of 20 questions related to the four clusters of emotional intelligence namely self-awareness, self management, social awareness and social skills.
- The Part 3 consists of a 5 point rating scale consisting of questions related to leadership whether managers used emotional intelligence to enhance their leadership skills.
- The Part 4 consists of a 4 point rating scale consisting of questions related multiple constituents and how far the managers recognize emotions of multiple constituents and attend them in designing organization functions.

A Two (2) hour workshop on emotional intelligence was conducted in each company and the data was collected and analyzed quantitatively for each objective. In the present study both Descriptive Analysis as well as Inferential Analysis were used. The data was analyzed in terms of frequency and percentage. Mean and SD were computed and 't' Test and ANOVA were used as part of inferential data analysis.

Awareness level of emotional intelligence amongst managers

- Informed Awareness - Unprompted awareness

The study proved that that nearly all managers of both Manufacturing as well as Service did not know as they were not able to name the component with no prompting.

- Prompted Awareness – Manufacturing – Service comparison

*Table 1: Prompted awareness - Manufacturing – Service comparison*

	<b>Manufacturing</b>	<b>Service</b>
Emotional Self Awareness	4%	5%
Accurate Self Assessment	2%	2%
Self Confidence	10%	9%
Self Control	8%	7%
Trustworthiness	6%	6%
Conscientiousness	3%	3%
Adaptability	5%	6%
Achievement Orientation	3%	3%
Initiative	7%	6%
Empathy	3%	5%
Organizational Awareness	5%	4%
Service Orientation	3%	3%
Developing Others	6%	5%
Leadership	8%	8%
Influence	4%	4%
Communication	8%	7%
Change Catalyst	2%	2%
Conflict management	3%	4%
Building Bonds	3%	4%
Team work & Collaboration	8%	8%
<b>Total</b>	<b>100%</b>	<b>100%</b>

The levels of prompted awareness varied considerably by the specific sub-competency concerned. In particular, awareness among the sample of self-confidence competency was the most widespread in both manufacturing and service sector of the 20 sub-competencies covered, and awareness of accurate self-assessment and change catalyst was least widespread.

*Table 2: Emotional intelligence of Managers in Manufacturing and Service sector (both Domestic and MNC)*

	<b>Manufacturing N=26 companies 390 managers</b>		<b>Service N=26 companies 390 managers</b>		<b>'t' value</b>	<b>0.01</b>	<b>0.5</b>
	<b>Mean</b>	<b>SD</b>	<b>Mean</b>	<b>SD</b>			
Self Awareness	8.93	1.6	8.78	1.69	1.26	NS	NS
Self Management	16.16	2.9	16.04	2.91	0.58	NS	NS
Social Awareness	8.12	2.52	8.21	2.09	0.54	NS	NS
Social Skills	22.84	4.6	22.57	4.96	0.79	NS	NS
Total EI	56.05	8.78	55.6	8.62	0.72	NS	NS

*Table 3: Leadership skills – Managers in Manufacturing and Service sector (both Domestic and MNC)*

	<b>Manufacturing N=26 companies 390 managers</b>		<b>Service N=26 companies 390 managers</b>		<b>'t' value</b>	<b>0.01</b>	<b>0.5</b>
	<b>Mean</b>	<b>SD</b>	<b>Mean</b>	<b>SD</b>			
Leadership skills	13.57	4.18	13.94	3.51	1.33	NS	NS

*Table 4: Multiple Constituents – Emotional intelligence of Managers in Manufacturing and Service sector (both Domestic and MNC)*

	<b>Manufacturing N= 26 companies (390 managers)</b>		<b>Service N= 26 companies (390 managers)</b>		<b>'t' value</b>	<b>.01</b>	<b>.05</b>
	<b>MEAN</b>	<b>SD</b>	<b>MEAN</b>	<b>SD</b>			
Employees	13.66	2.40	14.03	1.78	2.49	NS	S
Customers	10.78	1.76	10.72	1.67	0.50	NS	NS
Investors	7.97	1.68	8.12	1.52	1.30	NS	NS
Competitors	7.66	2.69	7.55	1.89	0.66	NS	NS
Total	40.07	6.52	40.42	5.31	0.83	NS	NS

*Table 5: Experience wise comparison using ANOVA*

		<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Self-Awareness	Between Groups	2.269	2	1.135	.412	.662
	Within Groups	2077.362	755	2.751		
	Total	2079.631	757			
Self-Management	Between Groups	14.249	2	7.124	.846	.430
	Within Groups	6359.515	755	8.423		
	Total	6373.764	757			
Social Awareness	Between Groups	5.039	2	2.519	.464	.629
	Within Groups	4100.412	755	5.431		
	Total	4105.451	757			
Social Skills	Between Groups	192.953	2	96.477	4.213	.015
	Within Groups	17290.251	755	22.901		
	Total	17483.204	757			
Total EI	Between Groups	345.733	2	172.866	2.279	.103
	Within Groups	57279.634	755	75.867		
	Total	57625.367	757			

*Table 6: Education wise comparison using ANOVA*

		<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Self-Awareness	Between Groups	20.594	2	10.297	3.776	.023
	Within Groups	2059.037	755	2.727		
	Total	2079.631	757			
Self-Management	Between Groups	32.498	2	16.249	1.935	.145
	Within Groups	6341.266	755	8.399		
	Total	6373.764	757			
Social Awareness	Between Groups	25.142	2	12.571	2.326	.098
	Within Groups	4080.309	755	5.404		
	Total	4105.451	757			
Social Skills	Between Groups	597.716	2	298.858	13.363	.000
	Within Groups	16885.489	755	22.365		
	Total	17483.204	757			
Total EI	Between Groups	1472.253	2	736.127	9.898	.000
	Within Groups	56153.113	755	74.375		
	Total	57625.367	757			

*Table 7: Age wise comparison using ANOVA*

		<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Self-Awareness	Between Groups	10.358	3	3.453	1.258	.288
	Within Groups	2069.272	754	2.744		
	Total	2079.631	757			
Self-Management	Between Groups	93.319	3	31.106	3.734	.011
	Within Groups	6280.445	754	8.330		
	Total	6373.764	757			
Social Awareness	Between Groups	3.766	3	1.255	.231	.875
	Within Groups	4101.685	754	5.440		
	Total	4105.451	757			
Social Skills	Between Groups	191.358	3	63.786	2.781	.040
	Within Groups	17291.847	754	22.933		
	Total	17483.204	757			
Total EI	Between Groups	680.263	3	226.754	3.002	.030
	Within Groups	56945.103	754	75.524		
	Total	57625.367	757			

Table 8: Gender wise comparison

	Gender	N	Mean	Std. Deviation	Std. Error Mean	't' value	.05	.01
Self-Awareness	Male	594	8.89	1.640	.067	0.424	NS	NS
	Female	164	8.70	1.717	.134			
Self-Management	Male	594	16.10	2.993	.123	0.141	NS	NS
	Female	164	16.02	2.550	.199			
Social Awareness	Male	594	8.18	2.128	.087	0.249	NS	NS
	Female	164	8.04	2.949	.230			
Social Skills	Male	594	22.82	4.902	.201	0.907	NS	NS
	Female	164	22.15	4.416	.345			
Total EI	Male	594	55.98	8.939	.367	1.090	NS	NS
	Female	164	54.90	7.868	.614			

## ***FINDINGS***

Amongst the sample a strong correlation was found overall and between each of the four emotional intelligence abilities (self-awareness; self-management; social-awareness; and social skills) and leadership skills, emotions of multiple constituents were recognized in designing organization policies.

In essence what the study revealed was that most of the managers in the manufacturing sector and in the service sector not very well informed about the concept of emotional intelligence indicating the lack of awareness regarding emotional intelligence. Managers in the service sector were more informed regarding the concept of emotional intelligence in comparison to manufacturing sector. The managers of both manufacturing as well as service were not able to name the components of emotional intelligence without prompting. Since scores were mostly below average, efforts to improve emotional intelligence among managers has to be implemented. Managers were fairly aware of the emotional intelligence however they are not capable of expressing or describing the term emotional intelligence in a verbalized way or be unable to even know that they are using it as they use. The reason behind this could be that managers are not skilled at expressing themselves and their beliefs or opinions.

The second objective in the present study concerned the measurement of managers emotional intelligence level for both manufacturing as well as service sector including domestic and MNC company managers. Emotional intelligence concerns the degree to which you are able to repair negative moods and emotions,

and maintain beneficial positive moods and emotions both within yourself and others at work. Proficiency in this area is typically reflected in congenial dispositions such as genuineness, warmth, optimism and charisma. The results indicate mostly an average emotional intelligence among managers. Emotional intelligence levels for managers of both manufacturing as well as service companies did not show much difference with most of the managers in the manufacturing as well as service sector showing to have average level of emotional intelligence. Self awareness, self management, social skills and social management all were in the average category. It may be that managers in both types of organizations possess similar skills that prepare them for their managership positions. That is, perhaps the manager's share similar experiences overall and those experiences result in similar levels of emotional intelligence.

The overall leadership skills for manufacturing sector as well as service sector (both domestic as well as MNC) was found to be moderate with most managers in the average range closely followed by high range. Differences in emotional intelligence scores among managers by type of organization showed no significant differences. Scores indicated that the managers of these organizations were average, indicating adequate emotional capacity. It may be that managers in these companies of both the sectors possess similar skills that prepare them for their managership positions. That is, perhaps the manager's share similar experiences overall and those experiences result in similar levels of emotional intelligence.

Managers were far below the satisfactory range as far as considering emotions of multiple constituents in framing organization policies was the concern. To be adept at an emotional competence like customer service or management of other multiple constituents requires an underlying ability in emotional intelligence fundamentals, specifically, social awareness and relationship management. However, emotional competencies are learned abilities: having social awareness or skill at managing relationship does not guarantee that one has mastered the additional learning required to handle a customer adeptly or to resolve a conflict. A person be highly empathic yet poor at handling customers if he or she has not learned competence in customer service. Although emotional intelligence determines the potential for learning the practical skills that underlie the four emotional intelligence clusters, the emotional competence shows how much of that potential one has realized by learning and mastering skills and translating intelligence into on-the-job capabilities.

For self-awareness, self-management, social awareness and total emotional intelligence there was no significant difference in the mean scores of managers having different number of years of experience. However for social skills, the difference was significant. Low emotional intelligence scores in terms of social skills can be attributed to problems with interpersonal relationships as well as difficulty changing or adapting. As the number of years of service progress, the tendency to become adjustment in particular mould becomes intense with the result that one tries to shun any external changes which might prove to be a hurdle in routine way of working to which he is accustomed.

As far as self-awareness, self-management and social awareness is there is no significant difference in the mean scores of managers having different educational qualification. For both social skills as well as total emotional intelligence there exists a difference in the mean scores of managers with different educational qualification. Improving managers' emotional intelligence would involve education and specific job-related training. Managers should also be encouraged to enhance their skills through continuous self-learning.

As far as self-awareness, social skills, social awareness and total emotional intelligence are concerned there is no significant difference in the mean scores of managers belonging to different age groups. One possible explanation could be that emotional intelligence is not a function of age and with the advancing years it does not get strengthened. Emotions are individual and their expression and manifestation depend upon individual's profile. Managers belonging to different age groups may not remarkably differ in their emotional intelligence competencies. Emotions can be trained probably with experience and exposure.

There is no significant difference in the mean scores of emotional intelligence gender wise with respect to self-awareness, self-management, social awareness, social skills as well as total emotional intelligence. The findings indicate that women score somewhat higher on measures of emotional intelligence than men. Extensive reviews of the data on leadership and gender indicate that women leaders are devalued in comparison to their male counterparts, but especially when women employ a stereotypical male leadership style, namely an autocratic as opposed to democratic, style. If emotional intelligence plays a role in effective leadership, and if women, as a group, are higher in emotional intelligence than are men, then we need to realize that women possess a critical leadership skill.

## ***RELEVANCE***

In so far as the management of social behavior involves the management of emotions (Hochschild, 1983), emotional intelligence has the potential to be a strong predictor of performance. Hence many organizational researchers have recently called for more focus on the role of emotions at work.

As the competition heats up and the pace of change is getting faster and the world more complex, we cannot continue doing business as usual. We need a new approach that transcends linear thinking and goes across barriers. As organizations downsize conflicts arise and undue stress is placed on every person within the organization. Extra pressure from increased workloads and financial stress, coupled with intra-individual conflict has created the need for and understanding and regulation of emotions in the workplace. Emotion detection is particularly prevalent at critical periods for instance during appraisals, promotions or retrenchment. However, since emotional processes can work faster than the mind, it takes a power stronger than the mind to bend perception, override emotional circuitry, and provide us with intuitive feeling instead. It takes the power of the

heart. The senior and middle level managers' behavior and treatment of their people determine turnover and retention. They interact daily with individuals who have distinct needs, wants, and expectations. They significantly influence the attitudes, performance, and satisfaction of employees within their department and of other departments.

As organizations begin to understand and implement emotional intelligence training they can reestablish the sense of a secure caring and people first atmosphere in their organization. This reestablishment is a key element in meeting the fundamental need described by Maslow's Hierarchy, of security and sense of belonging. Emotional intelligence is a simple yet effective route to establishing this sense in an organization. Furthermore, establishing an emotional intelligence organization now will ready an organization for the future influx and prepare them to become a streamlined and more effective organization.

### ***IMPLICATIONS OF THE STUDY***

The implications of this study for organizations include a more socially interconnected, motivated, emotionally healthy workforce, the retention of talent in Mumbai in the global economy, and increased revenue. A practical implication of a manager recognizing and developing improved emotional skills, that is, exercising emotional leadership, is improved individual performance with inherent benefits, including improved health and well-being, status in the organization and financial reward.

Organizations may use the results of this study to design training activities to enhance particular components of emotional intelligence. If these professionals know the emotional intelligence levels of their managers, they can design programmes around specific emotional intelligence components. Knowing the emotional intelligence levels of managers in different types of organizations would help identify areas for further managerial development.

Furthermore, this study revealed that managers in all of the organizations studied were average or low in their emotional intelligence scores. If a managerial program aspires to train managers with exceptional emotional intelligence – like skills, then this study is of value because it illustrates the need for emotional intelligence training among all organizations.

Results of this study may also be used by organizations for human resource development practices and assigning the work profile. If managers are aware of their strengths and weaknesses in relation to emotional intelligence subcomponents, then they may be persuaded to participate in managerial development programs that help them strengthen areas of weakness. Managers may also use the results of this study to further their understanding of how to enhance their emotional intelligence in relation to managerial and organizational activities.

Activities that promote active involvement and a sense of commitment will develop a sense of dependability and collaboration among the membership.

The implication of this study is that by using their own emotional competencies managers can encourage subordinates to enhance their problem solving strategy. The perception of subordinates of their supervisors' use of these skills may have compound positive impact on the subordinates' problem solving strategy of managing conflict and job performance. Therefore, the challenge for a contemporary organization is to enhance the emotional intelligence of their managers. Improving managers' emotional intelligence would involve education and specific job-related training. Managers should also be encouraged to enhance their skills through continuous self-learning. Organizations should provide appropriate reinforcements for learning and improving employees' essential emotional competencies needed for specific jobs. Education and training may be of limited value when it comes to improving supervisors' emotional intelligence. Organizations may have to adapt the policy of recruiting managers with vision and charisma who are likely to be high on emotional intelligence.

## ***VALUE***

The value of this research resides in the directness of the approach, the insight gained in the experience of managers going through processes of self-management and regulation. This research provides analysis on the emotional skills of managers and perceptions of senior executives and managers on the influence and importance of emotional intelligence for organization effectiveness and individual performance.

The research points to the need for organizations in Mumbai to establish emotional intelligence at the forefront of their employee value proposition and focuses the need for training in emotional intelligence if companies are to compete successfully in the global economy.

## **CONCLUSION**

The idea of emotional intelligence, and the findings of this research which supports it, indicates that organizations which select managers on the basis of IQ and other "traditional" measures will not develop the talent and capabilities which will deliver their future success. It is clear that managers with high levels of emotional intelligence have greater career success, foster stronger personal relations, have more effective managership skills, and are healthier than those with low emotional intelligence. Further, they are able to monitor and evaluate others' feelings empathize with others and excel in interpersonal skills. It is recommended that organizations seek out managers with high emotional intelligence and seek ways to enhance the EQ of current managers. Because this component of managerial success can be developed, it is also suggested that firms develop programs that enhance the EQ of their managers. This will enable them to motivate themselves and their subordinates and to work in more creative, more fulfilled, and more enthusiastic ways.

Results of this study may also be used by organizations for human resource development practices and assigning the work profile. If managers are aware of their strengths and weaknesses in relation to emotional intelligence subcomponents, then they may be persuaded to participate in management development programs that help them strengthen areas of weakness. Managers may also use the results of this study to further their understanding of how to enhance their emotional intelligence in relation to managership and organizational activities. Activities that promote active involvement and a sense of commitment will develop a sense of dependability and collaboration among the membership.

An important area of future research concerns carefully designing and evaluating the effects of intervention on supervisory emotional intelligence in enhancing positive conflict management styles and effectiveness. Additional research in this field could be conducted in an attempt to correlate managerial practices and organizational climate with concepts of emotional intelligence.

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# **THE MORAL VALUES OF BUSINESS IN VIRTUAL ORGANIZATIONS**

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## **ABSTRACT**

*The context of stakeholder theory specifies the aim of business in a complex way, taking into account the need to attach importance to the interests of all stakeholders in an optimal way. Thus defined the framework of business leaves room for evaluation in terms of ethical standards. The beginning of this evaluation is the determination of corporate social responsibility. That fact brings researchers in the position to separate economic and moral values of the business. Our focus is on moral values. The aim of this paper is to point out the specific articulation of moral values of business within the virtual organization. First, we'll point out which are the basic moral values of business in general, and then we'll try to determine how they seem in the framework that is defined by the parameters of the virtual organization. The theme that emerges as central in this context is the value of trust and its place in traditional and virtual business concept.*

**Key words:** *Social Responsibility, Moral Values, Virtual Organizations, Trust, Confidence*

**JEL Classification:** *Z19*

**UDK:** *005.71-021.131:174*

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## ***INTRODUCTION***

The times we live in set up the requirement to consider the finality of every experience in which we participate as an imperative. So the research of such a case is dominantly turned into the functional analysis. If there is something we do, if we act in a certain way, we sense his actions and proceedings largely founded on purpose or reason. If you deal with what in ancient times was considered the crown of our building knowledge, knowledge for knowledge, you can easily be declared a futile man. In this paper we will try to find the purpose of our business practices, looking back at the foundation of business practices that comes from the area of moral values. This will, hopefully and at least partially, be enough for avoiding the label of futility. First, let us consider the relationship between the action, purpose and value, the notions that we have already used to announce the topic.

Let's try to find a place in human nature which belongs to the activity of setting purposes. The will is the power to set purposes. The action is the subject of ethical analysis. That action is intended, and a presumption of intent is the freedom of the actor to choose stages on his path. Striving to reach the set purpose is the feature of the action so conceived. In other words, the decision of reaching the end is mortgaged in the action. When it comes to values, things are different. Namely, if we have successfully attained the aim, our action may be declared as valuable from the standpoint of value that we call success. If so, the actor feels pleasure and happiness. But such an action is not automatically assessed as valuable in the moral sense, that is, from the standpoint of moral right. There are at least two reasons for this. First, the successful realization of the objective can be fully or partially beyond the power of the actors, so the result is not a matter of their responsibility. Then, it is possible that the very thing that makes the action positively marked from the success standpoint, to classify the same action as morally wrong (Babić, 2007). In terms of axiology the items that define the actions are not the same if we look from the success as a value standpoint as if we look from the moral values point of view.

We pointed out that the subsets of successful and morally right actions do not match, because the values that determine these subsets are not constituted on the basis of identical characteristics. Their overlapping is accidental, as far as we are concerned for the characteristics that constitute these values. Let us concern now to the moral values. What is it that defines an action as morally right? The answer to this question is different for philosophers whose teachings represent different ethical theories. Our response arises from deontological ethical theory. We believe that utilitarianism, as the strongest rival option, is a form of rationality that does not provide strict ethical arguments. The main reason for that becomes from the very value field, because utilitarianism defines ethical values through values of utility, pleasure and happiness, and we have already seen that they are completely different values and they do not form the basis for the moral evaluation of the action. In Kant's ethical theory is morally worth action is the action that has been

done from motives of duty, or out of respect for the moral law. So, if something is morally right, it is because it is done in accordance with the express intention of respecting moral standard, and that standard is the moral law. Kant so clearly points out that the fulfillment of duties is made in the form of serious desires, not by the indirect causes of success (Kant, 1975, pp. 330). In other words, the question is not whether we are happy, which occupied a prominent place in the utilitarian estimates, but whether we are worthy of happiness, as Kant holds.

After these short basic settings, it is clear that we are interested in the nature of standard for moral right action, when it comes to business practices. So, on the source of Kant's ethical preferences, we wonder if we are worthy of happiness in business? In particular, we are concerned by the values that are particularly important if we ask the same question about virtual teams.

## ***CONCEPTIONS OF THE NATURE OF BUSINESS***

What are the characteristics of the business practices area? What complicates the simple application of ethical standards is precisely what defines business practices. If the goal of business practices is achieving success as measured by economic parameters, it is difficult to apply the standard of moral right to something that is defined using the value of success, because we have found that substantial heterogeneity parameters constitute these values. It is therefore important to address in the goals that determine the nature of the business more carefully. On this basis it will be possible to determine the scope for ethical analysis, and thanks to this we will be able to realize the importance that belongs to ethics in business.

There are two basic views about the nature of the business, as seen through the way in which we define its goal. The first point of view is the traditional *stockholder* (or shareholder) *theory*, while the second one is the *stakeholder theory*. These theories are confronted primarily in the way they envisage the aim and tasks of the business subject, ie. In the way they consider the social responsibility. The traditional approach, whose founder is an American economist and Nobel laureate Milton Friedman, argues that the sole purpose and obligations consist in profit maximization. And that defines the corporate social responsibility too. Stakeholder theory, advocated by Edward Freeman points out that the direct social responsibilities of the company can't be reduced to the profit maximization, but to the obligations concerning social responsibility. Which interest groups and whose interests should be taken into account? Who are the stakeholders? Stakeholders are all those who affect the company's operations, or those in which the business of the company affects. There are several ways to clearly determine who are stakeholders that should be taken into account. Frequently, economic theorists referred to primary (directly involved in business) and secondary stakeholders. In more detailed list we can found shareholders (owners), managers, employees, consumers (customers), suppliers, creditors, competitors, local communities, government,

environment, international community and humanity. Each interest group has its own aim: shareholders want capital (money for his independent values), the managers want to succeed against the competition, employees want cash and promotion, consumers want cheaper and better products, etc. Since resources are limited and there are many preferences, the optimal result involves scarcity and we have a range of unmet interest. In this conflict of interest situation it is not possible to find a solution that can make everyone be happy. It is crucial that one gain and others lose. The manager can't remain innocent, because the manager is the one who decides whose interest to sacrifice, and whether that sacrifice was "worth it." The manager does not bring his money into the business, and his freedom of decision making is less than the freedom of capitalists, and he deserves his freedom by his successful enterprise. This does not diminish the complexity of his position, and daily efforts in making decisions. Sometimes the sacrifice of interest, which is attached to someone who seems to be far away from business in question, turns out to be much more expensive for the company's image. So, it turns out that the long run fact is important moment in the decision making.

What are the limitations of managerial decisions? In the framework of the classical theory, the manager is required to make decisions that will lead to the maximization of profit, while respecting the legal restrictions and general rules of the game (derived from the basic guidelines of business practices and values of the society). This is often referred to as the principle of moral minimum mandatory for the business world, because it should, equally as the law and business practices, set limits to decisions. The moral minimum in business practice determines the prohibition of harming others. Does this mean that companies have a duty to prevent harm and are they in the position not to do good? The answer to this question would require that we thoroughly expound the problem of perfect and imperfect duties, as well as the concepts of positive and negative responsibility, which is not the part of our ambition in this paper.

According to the proponents of the theory of interest groups, the task of the manager when making a decision is to take into account (and to give them weight to the extent they estimate is necessary and appropriate) all the conflicting interests of different stakeholders and to respect them, in proportion to their importance. The regulation, which is present in the business world is legal (external coercion, often reactive character), derived from the internal code of the company, the normal behavior and business culture. What would it actually mean, depends on "company policy", the people who make decisions and those people who are affected by such decisions. Discussion about the stakeholders is connected with the ethical analysis of the duties of managers. Do they have a fiduciary duty to shareholders, or they have a duty of equal respect for the interests of all stakeholders?

What is the ethical aspect of the dispute over the determination of business purposes? We have found that it does matter whether we're in the business on the ground of only material interests that require the sacrifice of something that is not recognized as valuable, or our position is the one that allows us to determine values that business should affirm, even because that is the way to make some effect on success of business practices. Business ethics should perceive the target business

more realistically, in order to have a chance to success in this area. We'll call for the words of Peter Drucker, who claims that handy epigram of satisfied and happy employee who is also efficient, shows only half the truth, because "the company does not have a task to produce happiness, but to produce and sell shoes" (Drucker, 1961, pp. 313). Thus, the world of business is clearly defined with values that are instrumental. In that area the measures of the success are efficiency, money, knowledge of opportunities and knowledge, if unfailingly manages to find its way to the application, ie. cashing. And it would be the best that monetize is "monetize", ie. not to be at the level of cash, but on the level of capital. On the other hand, ethical norms are focused on our actions, and we, as people whose conduct is partly manifested in the business, follow their dictates. We should apply these standards to the successful and the less successful actions, and these standards are not defined in terms of instrumentality. But, it is not possible to act on business alone, in the sense that the field of business has absolutely nothing to do with morality that is incorporated in us (as well as in business, and society in general) and with, more or less expressed, awareness of it. Sphere of morality does not match with the sphere of success in business. But the sphere of morality in the context of successful operations of business is determines business subject through the dimension of its social responsibility. Socially responsible corporations have a greater chance of long-term good business image, and that is certainly something that significantly affects the performance of the corporation.

The real determination of the business aim as well as the determination of the factual situation when it comes to responsible business, can use the results of relevant researches. At this point our attention should focus only on one of them, which monitors the impact of compliance with ethical standards and principles of CSR on corporate governance in Serbia. Research has shown (Pržulj, Radovanovic) that Serbian managers believe that companies have a responsibility to their stakeholders, and that moral behavior and business success go hand in hand. Immoral behavior in business is considered unjustified. However, business practice in Serbia currently testifies that the actual situation is not in accordance with these views. If the practice is the only criterion, then the request for ethical and responsible conduct would rest without its base.

## ***BUSINESS AND MORAL VALUES OF BUSINESS PRACTICES***

From the standpoint of business values, it looks like the manager within the classical theory has the task of fighting for one value- profit, and that he is accountable only to the owner (shareholders). According to stakeholder theory of values, the profit is one value among others (in addition to personal, legal, moral, civilized, cultural). The decision about the dominant theoretical conception is the decision about the acceptance of the sole economic value or the holistic horizon of values, where the economic value is only one among others. If we include the long life moment into consideration, making profit as the primary objective that defines

business, requires that we take into account the values that are not strictly economic. Thus, the struggle for social responsibility is at the same time the struggle to build a successful corporation. If so, traditional and stakeholder theory meet at some point (Beauchamp, Bowie, 2004, pp. 49).

*Ethical business* means morally right business. Good business can be determined according to the functional analysis of good, which has been in use since ancient times. As this analysis assumes that the quality *good* is attributed on the base of the use of things, its role and its intended purpose, *good business* means business that is successful, which brings profit. Within the stakeholder theory, which determines the purpose of business by relying on the concept of corporate social responsibility, business success, by definition, involves respect for the moral standards. Is the successful business at the same time morally right business, and what is the nature of this connection? Ethical behavior in business, in a situation where the moral and successful requests are inconsistent, has a price, but, as we have seen, brings profit. Here the aspect of the situation in which to get to the goal involves the elimination of unethical competition cross our mind. But it is necessary to have knowledge about the tendencies of competition behavior (problems of game theory and strategic behavior) if we want to make that happen. We should consider how in this case the hierarchy of interests look like in decision-making, and whether the costs (care for the environment, employees and the like) which turns out the dictate of morally right are greater than the profit it is about to bring.

Thus, we have good reasons to believe that the basic ethical value of business is trust. If the value of trust defines the functioning of business frame, it's easier to understand how does the quest for respecting the moral integrity of the business participants fit into the broader evaluative picture that shapes the bases of business practices.

Without trust there is no agreement or contract. The value of confidence can be attributed to the expression of the moral integrity of the actors, and the respect for these values at the same time makes room for professional integrity. Observing the cruel capitalism through the prism of trust as a basic value might seem utopian. This is justified if we are concerned only with bare facts about business practice. The basis of business ethics can only be stable and meaningful if it is defined in the way that affirms values that we claimed to be the basic ones. Also, we believe that trust as a basic ethical value of business can provide the performance and profitability of the business. It would be good to address the arguments that support that thesis, and to show how the idea of ethical business contributes the affirmation of business values that have nothing to do with ethics. Such an argument would follow instructive observation of Kenneth Arrow:

"If we look closely, we'll discover that a large part of the vitality of economic life depends on a certain limiting degree of commitment to ethics. Completely selfish behavior of individuals is totally incompatible with any regulated economic life. Almost without exception there is an element of trust and reliability. A lot of work is done on the basis of verbal guarantees" (Arrow, 1963, pp. 314).

If we need to do the job on the basis of a verbal guarantee that anything else does not ensure, we can't skip the evaluation of the reliability of the other side. It is important to explain what it means reliability. In business our expectations of other stakeholders are related to the expectation of their reliability (trustworthiness), ie. their actions should be such that we can trust them. To specify, they should not cheat, ie. should not lie, should fulfill promises and respect contracts. That requires that we should really believe them, and that is our faith (trust) to other participants. But some authors, such as Ed Soule, distinguish between reliability as confidence and reliability as trust, holding that only the reliability as confidence has inductive origin that means that it stems from previous experience that confirmed positive behavior. And that is why the basic activities in the work place require just the reliability as trust, for which there is no precise inductive support. Just because of the risk that is part of this kind of reliability, as there are no guarantees, we emphasize the need for it; its necessity for the sake of functioning and most basic business transactions is used instead of the guarantee, we do not have.

We see that the relationship of trust is formed in a complex game of interdependence, whose duration is uncertain. That fact prevents withdrawal of strategic moves from one side in favor of purely personal promotion. Without trust there is no reciprocity. If one of the parties in this relation is worse or weaker, you never know if the other party will interact in the way to abuse the weakness, if there is recognition of the fact that trust is not complete. Bearing in mind that it is almost impossible to do business if the business moves are drawn only within precise guarantees, it is irrational to claim that cheating in business is a natural thing. Albert Carr (Carr, 1968, pp. 145-148) is famous just for that position, but he mistakenly placed contradiction of the business world, arguing that the game of poker, which mostly resembles the business practices, requires not to trust other players and to ignore requirements of the friendship.

## ***WHAT ARE VIRTUAL ORGANIZATIONS?***

There have been many attempts to define a virtual organization. As an illustration, we will give two definitions: „To the outside observer, it will appear almost edgeless, with permeable and continuously changing interfaces between company, supplier, and customers. From inside the firm the view will be no less amorphous, with traditional offices, departments, and operating divisions constantly reforming according to need. Job responsibilities will regularly shift, as will lines of authority- even the very definition of employee will change, as some customers and suppliers begin to spend more time in the company than will some of the firm's own workers” (Davidow, Malone, 1992, pp.5-6) or „virtual enterprising is a process through which companies team their capabilities, building upon their ability to define and redefine multiple cross- functional team as needed. These teams may include not only members of the company, but also people from vendor or customer companies“ (Savage, 1996, p.231). Without exaggeration, we

can say that the concept of virtual organization follows and represents the development of business skills. If we follow the definition that the authors such as Mowshowitza (Mowshowitz, 2002) have suggested, we will notice that lots of features are specified but they all are around the basic idea: the virtual organization is a term used to encompass the capacity of management to meet, again and again, permanently changing demands of business. Initially, the virtual organization is supposed to signify that a corporation has a greater capacity than is actually manifested in a given time. So this concept originated by analogy with the concept of virtual computer memory (Mowshowitz, 2002, pp.xiv). However, the term virtual organization is very flexible and includes many forms of business practices today. Many organizations do not realize that they are in fact a true example of a virtual organization.

Due to the complexity of the definition of virtual organization and the scope of literature with this topic, we have chosen to consider the characteristics of the virtual organization using the example of virtual project teams, for the needs of this particular study. The reason is based on the simple fact that the virtual project teams are one of the most modern editions of virtual organizations (the text from the following paragraph till \* is modified according to the source Majstorović et al., 2013, pp. 54-71).

Virtual project teams are teams that have appeared as a result of new demands caused by the globalization of business. They consist of groups of people who achieve cooperation almost exclusively via computer and communication networks in order to get the common goal they have. Face-to-face communication is an exception.

In order to highlight the degree of change, we compare the virtual team with traditional one. In the traditional business environment, employees physically depend upon each other. These are people who share office space. Their communication is manifold in formal and also informal levels. Their manager is a man who knows a lot about employees and maybe even about their families. He is monitoring their work and interaction every day. He invites them to individual counseling if needed, and makes efforts to improve their motivation. Manager includes the new-comer to the collective by considering his qualifications, as well as examining his ability of fitting into the existing team. This concept, according to a growing number of virtual teams, dies. New web technologies (LAN, WAN, Internet) radically altered the appearance of the project team. What has not changed is the fact that members of the team are also working on a common goal, and that there are resources that are necessary to achieve this goal. Everything else is different. The teams bring together people who live in different countries. It happens that there are people from 26 countries in a team of 35 people (Schneider Electric), and this is just one example. Their office is our planet, as well as information they possess are limited only by achievements of web technology. So, these people do not meet in offices, nor are they able to lead informal discussions. In the traditional model, moving to another place because of business requirements was a major problem. It isn't easy to leave family and friends, and to put aside relationship with people at work. Virtual Team was set up as a team of experts in a particular field, not in a specific country. People in the labor market have become available and are able to offer their skills to a wider market. The concept of a virtual team saves the cost

of frequent travel for business meetings, and at the same reduces the effort that travel brings to people (fatigue, sickness, frequent adaptation due to climate changes). Lot of money must be invested in improving the informational infrastructure that is supported by the new technologies. The team members and their managers do not meet at the same desk in the office, but in front of the web camera, sitting at home in front of the computer, participating in web conference.

Now, let us mention one important feature of virtual teams, and that is cross-culturalism. The request for gathering the most competent people, typical for the virtual team, erased geographical and cultural borders. Geographic dispersion of the team resulted in a cross-cultural nature of the team. Cross-culturalism is demanding brand new conditions.

Cross-cultural aspect became an academic and scientific challenge in 1937. Then Peter Murdock (Murdock, 1940) led a project organized at the Yale University with the aim to draw attention to specific sociological and anthropological problems that this phenomenon entails. Today, in the context of the business problem, specific features that multiculturalism brings seek an equal effort from researchers. On the one hand, it is necessary to preserve and if possible enhance focus all team members toward a common goal. On the other hand, it is important to note the differences that could lead to weakening of pursuit of an end. It is necessary to know which the differences and to what extent are threatening the functioning of the team and develop an appropriate treatment for these differences. It is important to take into account the fact that the funds that can be used are limited, because the dominant or exclusive communication model is virtual communication.

What does the aim of managing the cross-cultural virtual team imply? At the beginning it is necessary, as with any team, to make a team. This means transforming a group of individuals into a coherent team, able to create a plan of action that meets certain tasks defined by that plan. This is achieved through teamwork orientation, which becomes integrally connective tissue of the group. Creating a team is crucial task. After that, performance management and team development are two other tasks (Hunsaker, 2008).

If you gather experts and agree to specific geographically dispersed company, we have to deal with the requirement to minimize the importance of cultural differences in order to have successful and effective team. To minimize does not mean to eliminate cultural differences, because that could harm the integrity of individual and lock creativity. We should not forget that cross-culturalism makes coming to creativity and innovation easier. To make this actually happen, it is necessary to provide an atmosphere that will encourage these values.

It seems that the position of manager of virtual team is extremely delicate. He needs to mitigate the cultural specificities of the team members, in order to make them achieve appropriate level. On the other hand he needs to keep them at the right level and also to encourage those constructive among them. He has to find the principle of limiting cultural freedom that is legitimate from the interest of the company point of view. This principle shouldn't harm the moral and business

integrity of team members. Inventing this principle is a remarkable effort, which will lead managers to the position of the multidimensional challenges, requiring substantial ethical weighing. This manager has a much more complex task than managers in traditional team. Hence his qualifications have to be different.

There are many challenges for managing the cross-cultural virtual team. Virtual team manager's role looks like the role of manager of traditional team, but only in some respects. It could be argued that their roles share the same formal frame. This frame is defined by the prescription of responsibility for their choices and through connection of the realization of these decisions and the expected effects. That, in long term conditions, must be interpreted as beneficial. Within this frame, there are different settings. The work of the virtual team is determined by virtual settings. The most prominent challenge in this specific set is the value share challenge, with the problem of trust as its main subject.

### ***MORAL VALUES OF VIRTUAL ORGANIZATIONS***

As we have already stated, the crucial condition for making a successful team is trust. Trust is a value that limits many business practices and makes ethical norms and principles useful for business. Management theorists have discovered trust as an important ingredient for competitive success. They needed trust because lack of trust raises transactional costs and complicates collaborative efforts. It is easier to have trust as an assumption in business relationships, because without it everything would be impossibly complicated and expensive. For example, think about the role of contracts in everyday business, and how often we use them. Without trust as an assumption, contracts would be endlessly long, spelling out every possible contingency and defining every conceivable obligation (Fukuyama, 1995, pp. 152).

Some authors name five main disadvantages to a virtual team as: lack of physical interaction, loss of face to face synergies, lack of trust, greater concern with predictability and reliability and lack of social interaction (Cascio, Shurzgalio, 2003). In our opinion the problem of trust, which is closely related to specific treatment of predictability and reliability, is the basic value problem for virtual teams. The issue of trust is increasingly complex in a virtual environment, though trust is important condition for the success of any team. Furthermore, this problem is much more visible in the virtual cross cultural team setting, than in the traditional one. There are many reasons for this claim, and the first one is concerned with the way we build trust among each other.

How does phenomenology of coming-to-trust look like? According to one model (Zaccaro, Bader, 2003) there are three stages of trust. The first stage is the trust that economists hold to be calculative: there is a good reason for each side to trust the other. In the new team this stage of trust is recognized as the benefit of working together. The problem for virtual settings is that there are no guarantees of future contact, so the calculus, as the base of trust, can't work. If the only reason for trustworthy is "because it pays" when we move the possible transaction, we do

not have the reason that leads to action any more. Trust must rely on the more solid ground, and maybe that ground can be reached on further stages. \*

We may address the problem of trust in various ways. Trust is recognized as an important issue in organizational psychology, management, public administration, organizational communication, education (Bachmann, Zaheer, 2006, pp.15). The authors agree on the view that the focus of the management literature of the 1990s is topic of virtual organization and confidence. As an example, we refer to the observations that amount to Jones and Bowie (Jones, Bowie, 1998, pp. 273-292). The authors talk about the economic and social reasons due to which the trust is recognized as a value that underlies the success of the virtual organization. Significantly, their observations concern the paradoxes of virtual corporations (ibid. 273). In fact, it is clear that coming to an agreement in a short period of time and in terms framed by standard specificity of virtual organizations may not be possible if we don't have mutual trust and strong bonds of cooperation that connect participants of business transactions. The relationship of trust that we talk about is the trust that no contract can guarantee. Indeed, the situation in which are stakeholders in the business situations of which we speak looks like the situation in which are people in so called natural position, before the occurrence of the state. Their confidence in the political entity that has yet to occur recalls the confidence of businessmen. There is no contract that guarantees that the government will fulfill its promise and ensure people the security of life and property. Nevertheless, people still give up the part of their freedom in exchange for security services. This is one of many explanations of the origin of the state. According to that we can interpret the state as a protective agency. However, although this theory about the origin of the state is commonly called the social contract theory, there is no contract, because the state can only provide the contract. If you want to find a contract that is basically in the name of the famous theory, the most appropriate concept would be determined by a psychological contract. This agreement has its basis in the will of individuals on both sides, when it comes to business transactions, too. When it comes to the analogy of the political sphere, the state guarantees the validity of the contract, and the emergence of the state enables trust. Such confidence is essential in the business we're talking about. Jones and Bowie argue precisely the thesis that only such, they call it the *moral concept of trust*, which is ethically-based and which does not have the usual guarantor, can enable business success.

This is a very strong notion of trust, and thus there is a demanding condition posed to virtual organizations. Ethically-based trust, hard-core trust, as otherwise we call is a *conditio sine qua non* for the success of virtual organization. One justification for this claim is found in Norman Bowie's arguments. Bowie's moral treatment of trust provides the answer to our normative ethical orientation of Kantian type. Bearing in mind our core ethical beliefs, Bowie's arguments are very interesting to us. He argues that the definition of the capacity of the negligence of trust as inappropriate maxims that express the neglect of trust can't be practically universalised. Drawing on observations of Kosgaard, he emphasized that there actually is a pragmatic contradiction, which occurs whenever the success of

achieving a goal depends on the exception to the application of certain practices. Thus, a false promise is a pragmatic contradiction, because the success of such a promise in reaching the specific goal (money), depends on the fact that most of the promises we do not use in that way. This means that a false promise is not promising paradigm, on the contrary, it is an exception, and can lead to target only accompanied with the background assumption that it is the exception to the standard cases of promising. This way Bowie's argument fits into standard of practical universalization- the maxim of a false promise passes the test of logical, but not of practical universalization. And practical universalization is the paradigmatic ethical test, which detects the moral right. Finally, we can conclude that if the Bowie's argument of ethical grounding of trust is valid, it would have important implications to the way we comprehend the notion of trust. Trust is not only a descriptive term, but essentially a normative concept. Thus, the requirement for trust in business can't be excluded by the fact of numerous scandals, as they miss the nature of the real requirement.

Virtual organizations are very specific. So, people whose conduct would be otherwise in accordance with the ideal of education and the aim of moral autonomy would be the best to engage in virtual organizations. That is partly because the fact that only autonomous personality can successfully take part in the organization that incorporates laissez-faire style. The main feature of such a style is high level of individual freedom. Virtual organizations are much alike such model of leadership, and that is why management has a coordinating role unlike its role in the classical styles of guidance.

## ***CONCLUSION***

We offered factual and normative arguments to demonstrate the essential importance of the existence of trust in business practices. To ignore the trust means not to understand the purpose of business, because without trust this purpose generally is not achievable. As we have focused on the trust that does not an inductive origin, so-called hard-core trust, it is clear that we don't have strong or any guarantees for that kind of trust. The insistence on the affirmation of the trust value within the overall business environment goes hand in hand with the insistence on giving priority to moral reasons (which is an essential feature of moral integrity) at the individual level, when speaking of participants in the business activity. And that is a significant task for business ethics.

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# **ORGANIZATIONAL DIAGNOSIS AND MANAGEMENT OF CHANGE IN ORGANIZATIONAL CULTURE OF BANK INSTITUTION**

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*Snezhana Ilieva, PhD<sup>34</sup>*

## **ABSTRACT**

*The identification and comparison of the current state of an organizational culture and the desired future state allow the planning and implementation of subsequent interventions in the ways an organization functions. This article aims to present the results of a study of organizational culture in a bank institution and to outline the main areas in which the necessity of future organizational change is proved. A profile of this organizational culture is established, which represents it as a purposeful, clearly structured, and highly market-oriented one. The good relations, cooperation, and willingness to disclose innovation and development are highly appreciated. Stability and continuity between current and desired organizational culture are established with emphasis on the need of strengthening the orientation of the external environment, on one hand, and on the other, on the need of autonomy and independence of the employees in the working process and also on the importance of good relationships and traditions. The results of the study of the preferred future organizational culture in the banking sector can be obtained in process of change management and in determining the domains where an intervention is needed to achieve an organizational change purposes. They can be combined in the following sectors: providing more independence and flexibility, and improvement of the inter-bank communication channels.*

**Key words:** *Organizational Culture, Organizational Change Management, Types of Organizational Culture, Bank Sector*

**JEL Classification:** *L20, M14*

**UDK:** *005.32:336.71*

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## ***INTRODUCTION***

Bank sector is one of the most dynamically developing and strongly competitive sectors in which mergers and acquisitions are often applied. This requires of its management not only to manage the process of continuous changes implementation in service quality and to resist the pressure of the competitors, but also to know how to build and maintain an organizational culture which is congruent to the requirements of the external environment, and, in the same time, reflects the specifics of the particular bank and gives it an uniqueness.

Culture is broadly defined as a “system of basic assumptions, beliefs and values found, identified, developed and taught by a group in the process of dealing with its problems of external adaptation and internal integration, and adopted as valid by all members of the organization for the correct way to perceive and solve problems” (Schein, 1992).

In order to make a successful change in the organization it is necessary the totality of intentional and goal orientated actions to be precisely planned on the base of organizational diagnosis of the recent state of the organization, which results in developing of strategies for accomplishing the change and applying the relevant approaches, interventions and organizational practices. The main goals of the organizational change include increasing of the organizational ability to adapt to the external environment and to integrate the changes that were done, which reflects in change of the organizational culture and behaviour of the employees, i.e. organizational change should achieve simultaneously adaptation to the market environment and internal integration, on one hand, and shared values and patterns of behaviour, on the other.

Exactly because of this, the success of organizational changes can be evaluated by the dimensions of organizational culture which not only differs one organization from the others in the same sector, but also ensures sustainable development and effectiveness. The organizational culture has many functions which prove its significance for the development of one organization. The most important among these functions are the adaptation function or adjustment to the changes in organizational environment and context, and the integration function which is focused on the processes within the organization (Schein, 1985). The role of the integration function shows itself in the influence of the organizational culture on team effectiveness, and on the commitment and identification with the organization as well as in the coordination and communication between different structural sections which ensures internal organizational stability regardless of the crises that occur outside the organization (Ilieva, 2006 b).

According to S. Robbins, there are six major forces that promote organizational change: the changing characteristics of the workforce, technology, economic shocks, changing social trends, the "new" world politics and changing characteristics of competition (Robbins, 1983). All these destabilizing forces affect

organizations because they put them in a new situation, which imposes new internal and external conditions of existence. For this reason, organizations must continually adapt to the environment and this is only possible if there are changes in the culture of the organization according to the context requirements.

Achieving these two main organizational culture's functions - external adaptation and internal integration (Schein, 1992) can be found in bringing to four main types of organizational culture, which are subject of research in the competitive model of organizational values (Quinn, 1988). This model provides a possibility to compare the main types of organizational culture and to assess their influence according to the dominant value orientation in every one of them. The four types differentiate between themselves according to two main value orientations - orientation towards internal and external environment, and orientation towards flexibility and independence in actions, and towards stability and control (Cameron, Quinn, 1999).

The values inherent for the organizational culture of clan type include traditions, loyalty, interpersonal relationships, team work, and accepting the organization as bigger family. The manager is expected to be a father figure, mentor, and facilitator of the processes, whereas the organizational strategic goals are human resources development achieving high degree of attachment and labour moral. The orientation in the adhocracy type of culture is towards external environment and the strategic goals and values comprise dynamism, growth, innovations and creativity. The successful management requires the managers to be innovators and entrepreneurs, and to be ready to take risks. The hierarchy type of culture stands on the processes within the organization and the stability, order, clear rules and procedures have priority. The managers' role is to coordinate and organize the implementation of the work and the interaction between the employees. The market type of organizational culture supposes searching for competitive advantages and, in the case of administration, recognizing the external environment and the requirements of the citizens. Motivation for achievement and determination are the preconditions for effective leader's style in market organizational culture (Cameron, Quinn, 1999). Organizational culture contains characteristics of every type of culture, but the dominance of one particular orientation defines its specifics and differentiates it from the rest organizations (Meschi, Roger, 1994).

Organizational diagnosis incorporates the assessment of the current level of functioning in order to plan an appropriate future intervention and change. Organizational diagnosis process requires collecting information about the problems and their origin and the existing organizational difficulties, exploring the possible solutions and ways of organizational improvement and choosing the appropriate organizational interventions.

Organizational diagnosis could be viewed as a comparison between the current and desired organizational state (Beckhard, Harris, 1987), as a process of data collection for discrepancy between the ideal and current behaviour manner (Blake, Mouton, 1989) or as a means for outlining the differences between the organizational situation now and the situation that ought to be (Weisbord, 1985). Main goal in the organizational process analysis is to disclose the forces and causes

led to the current situation in the organization, and to define ways and tendencies toward achieving a new desired organizational state. Organizational diagnosis's main purpose is data collection about the current "picture" of the organization, which would serve as a basis for short-term and long-term changes and improvements in its functioning (Ilieva, 2006 a).

The goal of this survey is to measure and to establish the recent organizational culture and the desired future culture in the chosen, representative for the sector bank, by defining the dominant type of organizational culture and, on this basis, to diagnose the spheres where future optimization and organizational change should be made. Congruence is expected to exist between the perceived and the desired future organizational culture (stability), as well as to be observed clearly dominant type of organizational culture, focused on market success.

## ***RESEARCH METHOD AND SAMPLE***

To measure the recent organizational culture and the desired future one, K. Cameron and S. Freeman's model of competitive values is applied which gives an opportunity to define well each type of organizational cultures (Meschi, Roger, 1994). The questionnaire is based on the theory of competitive values and it shows appropriate psychometric qualities (Cronbach's alpha,  $\alpha = 0,731$ , current state; Cronbach's alpha,  $\alpha = 0,813$ , future desired state) (Ilieva, 2006 b). It contains 16 questions which measure four types of organizational culture - clan, hierarchy, adhocracy, and market cultures. Questions are divided equally in four scales and are evaluated by a 5 point Likert scale.

The questionnaire was given to the respondents to fill it twice. The first evaluation is relative to the way they perceive the recent state of the organizational culture, whereas the second evaluation is relative to their personal perception and concept of the desired future state of the organization. In this way, comparing the results we can diagnose the employees' perception of the organizational culture dimensions and its strengths and weaknesses. Thus, spheres of discrepancy between the real and the desired organizational culture in the Bank could show up and preconditions for future structuring of effective plan for organizational change could be created as well as what is necessary to maintain and to improve in organizational culture.

For conducting an organizational diagnosis we used the R. Preziosi questionnaire, based on the six-component model of Marvin Weisbord (Weisbord, 1985; Hamid, 2011), which contains the following components: goals, structure, relationships, rewards, support, leadership. This model is based on the systematic approach and it is aimed to analyse the interrelationships between the particular variables that affect the ways the organization is managed. Preziosi had added to these spheres another one – change that measures the attitudes and resistance to change. The questionnaire shows good psychometric properties (Cronbach's alpha,  $\alpha = 0,926$ ) and is composed of 35 items, divided by 5 in 7 subscales (Preziosi, 1995).

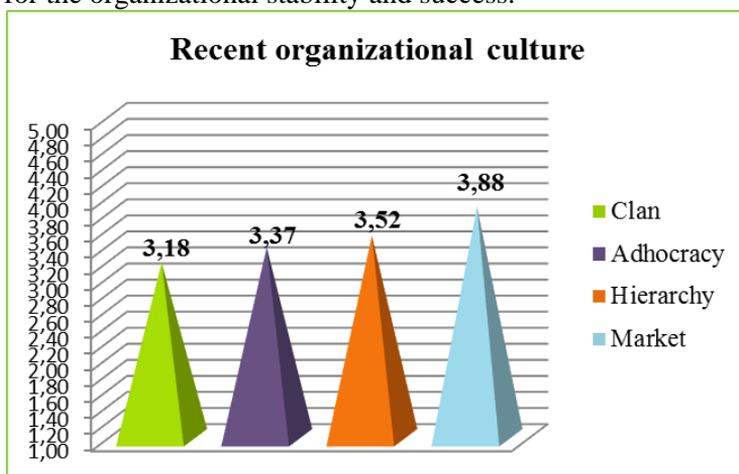
## ***SAMPLE***

The data were collected in international bank institution which has more than 17 years of history on the Bulgarian financial market. This bank has Central Office where more than 250 employees work, and financial centres throughout Bulgaria where the employees are approximately 400. The respondents that took part in the survey are 70 specialists who work in functional, business and risk departments. They were randomly chosen and 90% of them work in the Central Office. 44 of the respondents are women which is 62, 9% of the sample and respectively 26 are men, which is 37, 1% of all the respondents.

## ***RESULTS AND DISCUSSION***

### ***RECENT STATE OF THE ORGANIZATIONAL CULTURE***

The expectation that one dominant type of organizational culture has been established was justified to a certain extent, but results show that the Bank's organizational culture is a balanced combination of the 4 types of organizational culture (Figure 1). The employees define the organizational culture as market-orientated ( $\bar{X} = 3,88$ ,  $SD = 0,5$ ) and that has given a reason to define the following characteristics of the Bank organizational culture which are: orientation towards stability and control, on one hand, and orientation towards external environment and result achievements, on the other. The manager is perceived as responsible to reach the organizational goals and tasks which is extremely important for the organizational stability and success.



*Figure 1: Organizational culture types*

There is a statistical significant difference between the employees who work in the Central Office and in the Financial Centres ( $T = -2,081$ ,  $p = 0,041$  ( $p \leq 0,05$ )). Those who work in the Bank branches/Financial Centres evaluate the organizational culture as market orientated ( $\bar{X} = 4,37$ ) much more than their colleagues from the Central Office ( $\bar{X} = 3,84$ ). The difference comes from the job specifics of the employees in the Financial Centres – every day they meet clients, work with the Bank trade products and make direct efforts and actions toward goals achievement.

The results indicate for peculiarities of the organizational culture of the current bank and meanwhile the culture types can be defined as typical and representative for the whole banking sector. Being mainly market-orientated culture, it emphasises innovation, dynamics and development (adhocracy type), notices the requirements of the work and specific job procedures (hierarchy type) and meanwhile appreciates the unity, loyalty, ethics, traditions and good relations. The competitive advantage is based on stability of organization achieved by combining the orientation towards external environment which can be seen in the higher values of the market type of organizational culture with the orientation towards keeping the internal rules, order and hierarchy which are typical characteristics for the hierarchy culture. Flexibility towards external environment can be achieved through the adhocracy type of culture which increases the innovativeness and develop organizational ability for adaptation and maintains its competitiveness.

### ***DESIRED FUTURE ORGANIZATIONAL CULTURE STATE (COMPARATIVE ANALYSIS)***

The results about future desired culture state show employees' preferences that the characteristics of all types of organizational culture be expressed more strongly, except the characteristics of hierarchy type of culture which respondents would like to decrease a little or to keep them in the recent state (Figure 2).

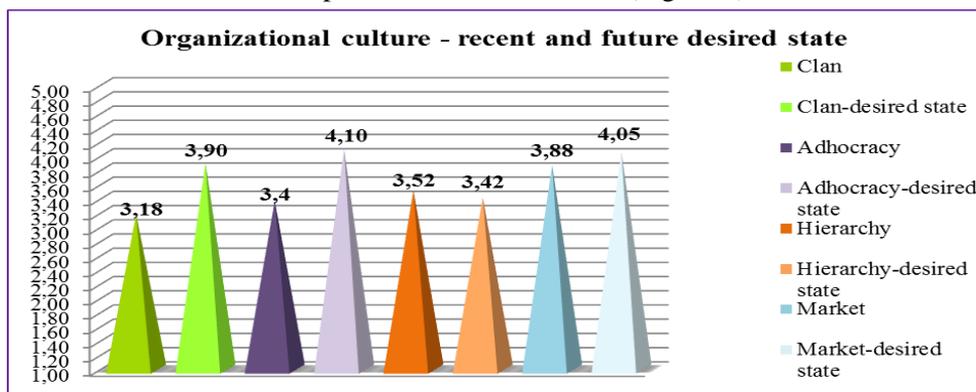


Figure 2: Comparison between recent and future desired state of organizational culture types

The biggest differences are observed between the clan and the adhocracy types of organizational culture. This result indicates that employees have preferences to increase the flexibility and autonomy, which the organization allows them in the recent moment and, in the same time; they have readiness for innovations (adhocracy organizational culture). The change towards creating an organizational culture which contains characteristics inherent for the clan type is also pronounced (recent state:  $\bar{X} = 3,18$ ; desired future state  $\bar{X} = 3,90$ ;  $SD = 0,67$ ). Employees would like to develop further the good relations and teamwork they have with their colleagues and are ready to commit and involve stronger in the organization activities.

Comparison of the profiles of the recent and future desired culture gives a chance to bring out tendencies in the practices of support and improvement, which should be taken into consideration in the future bank management actions toward leading in changes in the strategy, structure and human resources management (Figure 3).

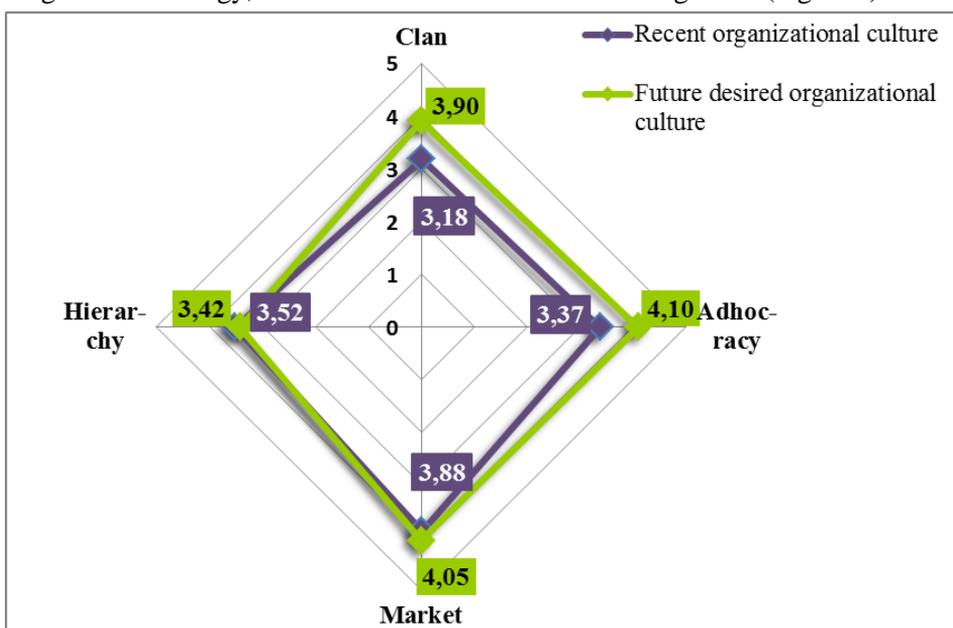


Figure 3: Recent and future desired organizational culture's profiles

The tendency for agreement in sustaining the market and hierarchic types of culture is kept, but obvious preferences for change and improvement of clan and adhocracy types of cultures are also demonstrated. To summarize the established differences, it could be concluded that the desired image of the future Bank's organizational culture is based on the already existing recent orientation towards stability and control, but at the same time organizational culture is expected to be much more open to and orientated towards the external environment, which will give the employees more freedom, independence/autonomy and flexibility in the working process and will put higher the importance of good relations and traditions which give a sense of social and organizational support and loyalty.

## ORGANIZATIONAL DIAGNOSIS

The analysis of the results of the conducted organizational diagnosis provide comprehensive picture of the way in which the Bank operates and give additional information about needed changes (Figure 4).



Figure 4.: Values of organizational functioning components

The surveyed employees evaluate positively the relationships they have in the organization with their colleagues ( $\bar{X} = 3,84$ ;  $SD = 0,55$ ) which give them a sense of support and security, and allow them to show good job performance. Important components to sustain this atmosphere are the relationships with the line manager, which are good for 87,2% of all the respondents. A confirmation for those results is the fact that employees and their teams are supported by the line managers through new ideas and advice, that help them in the successful performance (support mechanisms:  $\bar{X} = 3,63$ ;  $SD = 0,54$ ). Overall, they have been satisfied with the information they received about their tasks, but do not highly appreciate the mechanisms for assuming obligations. With regard to possible future changes, surveyed employees, albeit moderately, find out a potential in the banking institution ( $\bar{X} = 3,35$ ;  $SD = 0,46$ ). According to them, when new strategies and implementation procedures are introduced, the organization does not have a strong resistance, but it does not actively support the innovation. Respondents have a positive attitude towards change, confirming the results obtained from the study of current and future organizational culture.

With regard to the structure ( $\bar{X} = 3,65$ ;  $SD = 0,54$ ), according to employees, the existing division of labour is dependent more on the achievement of the

organizational goals and is not assessed as very flexible. The top rated organizational functioning component is leadership ( $\bar{X} = 3, 87$ ;  $SD = 0, 46$ ). With respect to the development and success of the bank, employees attribute great importance to the initiated rules and the management approaches, and appreciate the efforts of the entire leadership to achieve the goals.

Employees clearly understand the goals and priorities of the organization (goals:  $\bar{X} = 3, 87$ ;  $SD = 0, 47$ ), they are aware of their personal goals, which largely correspond to group goals. The lowest rated organizational component is the rewards they receive (rewards:  $\bar{X} = 3, 12$ ;  $SD = 0, 68$ ) and they do not perceive the options for personal and professional growth, available to them, as viable. According to them, the proportion of the efforts they make, the job they do, and the rewards they receive is satisfactory, but they are not quite convinced how equitable the payment levels of all the subordinates are.

## **CONCLUSIONS**

The data allow establishing an organizational culture's profile which can be considered as representative for the banking sector. The studied organizational culture is strongly orientated toward goals achievement and results, and toward market stability. It is clearly structured, and focused on following, and keeping the rules and procedures, which create stability and order inside the organization. In this regard, good relations, friendly support, and cooperation are highly appreciated in the organization, and the readiness and willingness for innovation and development are revealed.

This tendency strengthens even more in the employees' notion of the desired future image of the organizational culture. It shows that there is congruence between the recent organizational culture and the desired one, by demonstrating the stability of organizational values in the future. Bank's leading competitive advantages expressed in stability and control, on one hand, and in achieving results, on the other, are kept and require purposeful managerial actions of maintenance and development. Employees would work even harder in order to fulfil the business goals and they would not change anything in the division of labour, subordination and management style which they highly appreciate. But besides that, employees' preferences about the future organizational culture's profile contain a desire for more flexibility and action independence which would stimulate them to develop their initiative and innovativeness, and to identify themselves with the organization and with the teams they work in, by developing higher level of unity, loyalty and commitment.

A long-term organizational change planning could be built on the basis of the survey and diagnosis, which would be focused on increasing employees' job satisfaction without being necessarily related to changes in the reward system. The results from the survey on the desired future organizational culture could be

considered as a starting point for the areas which need intervention for fulfilment of the desired state, and the following ways and approaches for organizational culture improvement and change could be designed.

The implementation of more independence and flexibility for employees could be made by applying of the following techniques of organizational change: group decision making and team development; giving opportunities for personal planning and organizing the delegated tasks; rotations and in-the-job trainings. Improvement in the interrelations within the bank and creation of a higher identification, loyalty and commitment could be developed by elaborating common projects and tasks, which enlarge the collaboration between teams and organizational units, improve inter-bank communication channels and help to prevent and manage conflicts.

It could be concluded that the main organizational culture's characteristics of the bank researched provide its competitive advantage and meanwhile reflect the tendencies and requirements toward the organizational culture, which is inherent for the banking sector as a whole. These tendencies are the following: balance between the main values orientations, with focus on the external environment and a simultaneous combination between flexibility and stability. Maintenance of the organizational culture and its change in order to ensure wider initiative and innovativeness, on one side, and internal integration, loyalty and commitment, on the other, would create preconditions for more successful functioning and development, and would help to plan and manage actions towards stabilizing its market position and towards creating new competitive advantage.

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## **STAFF MANAGMENT AND EVALUATING THE STAFF EFFICACY**

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### **ABSTRACT**

*Every modern corporation where people are a secondary factor carries a high risk of unfavorable results of work, which leads to inconsistency in the development of the productive forces. Managing modern organizations must be based on the human resources, which allow them to their activities, awareness and enthusiasm to develop and improve work processes and relationships. People are leaders and economic development factors, which determine the development of the productive forces and production relations and the fundamental creators of expanded reproduction and its organization. Of the great importance for personal management is the performance of staff at all levels of management and leadership. In human resources researches there is an area that deals with evaluating the effectiveness of staff, although the practice confirms that this field is not yet been sufficiently examined. The aim of this paper is to establish a balance in the flow of human resources development and material resources and the satisfaction of the principle of "adequate human resources for the proper technology." It's not possibly always to measure the results of staff by using the available instruments, but it can be set a system of evaluation of their performance. Evaluating of staff performance represents characteristics, behaviors and analyzes the results of their work. The value of such evaluations is reflected in the comparative review of individual results and to provide opportunities for the most capable to take the key places in company with an intention to achieve optimum results based on available resources.*

**Key words:** *Management, Staff, Resources, Efficiency*

**JEL Classification:** *L21*

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## ***INTRODUCTION***

Management comprises a number of interrelated functions that are present in all organizations and at all organizational levels. One of the major problems facing modern management is how best to use the resources of the company in a rapidly changing and turbulent environment. The optimal combination of available resources and their best use is one of the most difficult problems faced by the management at the beginning of the XXI century. In order to solve these problems there is no single management practice, which would be universally applicable to all kinds and types of business.

Personnel management as part of operational management lately attaches great importance. Since man is the only living factor in the organization, there is no universal pattern of work and dealing with people who would guarantee the success of the company. Task functions of human resource management in the enterprise relates to: filing and maintaining jobs in the organizational structure, education, development and training of employees. Since people, as individuals, have to be organized in work teams, i.e. groups, this means that the organization depends on interaction and coordination among people to accomplish their goals (Stojanović et al., 2013, p.78) Management system in a broader sense includes research human resources, recruitment, employee development, their fees and salaries, promotion at work, health care and life of employees, relationships with employees and unions. Only selection can not guarantee success of that company, if it is not accompanied by action of continuous improvement, education and training, and retention of quality staff. At a time when the knowledge of employees to expand and multiply at short period of time, the success and survival of any enterprise is caused by continuous development and training of employees. Only those companies that are able to recruit, develop, promote and retain their employees will be able to achieve its planned objectives and survive on the market. Companies must continually search for quality personnel, in order to achieve the planned objectives. The main objective of human resource management in any company is to place the right people in the right jobs. (Jovanović et al.,2007) The economy of the XXI century management personnel is facing new challenges of the business environment. Requires new ways of thinking and acting, new policies and practices, new technology and new business needs. Today, enterprises are subject to organizational change, change management and the role of employees. (Farkaš, 2008) Construction of management function is not complete yet and it must necessarily be developed in accordance with enterprise development and social relations. Otherwise, he threatens her risk of bed development and stagnation. In connection with the development of business, it's necessary to build a profile of leading personnel (Stefanović, 1996).

## ***ENTERPRISE DEVELOPMENT AND HUMAN CAPITAL***

The organization is also the product of human intention to create 'perfect' structure/system that would provide maximum benefits/profits/gains with minimum costs. Support and cooperation is an important aspect of enterprise development (Stojanović et al., 2013, p.76).

The properties of these enterprises are change, innovation, openness and trust. If we look at the company, the starting point should be a system of enterprise value, because companies that are focused on the development are based on values. The main values that are the key element and directed the development of the company are: quality, knowledge, skills, competencies, expertise, knowledge sharing and innovation. Successful utilization of the expertise of employees is main quality performance of companies, which is why personal competence plays an important role in the value of the company. This means that the company must nurture an appropriate long-term philosophy focused on the development. The philosophy of the company development must have the place it deserves, and this leads to the improvement of individual employees and at the same time contributing to the achievement of the strategic goals of the company. Orientation on development policy will inevitably lead to individual success of each manager. Just based on the introduction of new techniques and the improvement of the productive forces leads to an increase in the social productivity of labor, one of the factors playing a society.

Development planning is a specific form of leadership and decision-making basis, leads to the fact that the creative role of the main lever of leadership in policy development. For this policy are crucial these moments: (Stefanović, 1996)

- Provide support to all staff
- The selection of objectives
- Alignment of interests
- Financing strategy and
- Constant activity in the implementation of (consistency).

In the long-term development policy must come to the fore especially economic interests and principles. Economic interests consist in increasing profits, achieving full employment capacity and human resources, increase labor productivity and, in this regard, earnings, and also in economic stabilization and job security companies. One must not forget the increase in the educational level of staff and strengthening the position of enterprises in the market mechanism. Economic development principles require that each plan must be realistic, achievable and consistent.

It should be noted that the long-term development policy has a broader meaning than it does in practice. She includes many elements of development, such as increasing production and productivity, long-term contractual obligations, market expansion and export, but also its contents are rationalization,

specialization, integration processes and self-organization, reconstruction, replacement, expansion and new production. The width gives each company to enter into the general mechanism of economic development. Optimal investment in material and human resources make effective business results and promotion of human work. Important role in that process are a long-term policy development and personnel policies designed to interrelations and reconciliation. The main driving forces of production are the staff with its knowledge and experience in the function of carriers and employees, and the organizers and the steering wheel. Adequate staffs with continuous systematic training are equally important as the introduction of new technologies. Technical progress and adequate staff profiling are two essential conditions for the development of the productive forces. Human resources and means of production are indivisible unity in initiating economic development. Funding alone can not achieve results without man nor can man perform productive activities without the means to work. They are the two essential elements and indivisible factors of production and the productive forces (Pelević, 2004). Human capital is the accumulation of investments in people. Education is the most important type of human capital. Like all types of capital, education is a waste of resources in a given period in order to increase productivity in the future. Unlike investments in other types of capital, investment in education is related to a particular person and it is a bond that makes the human capital. Not surprising that workers with more human capital on average earn more than those with less human capital. For example, people with a university degree in Europe and North America earn almost three times more than workers who have earned a high school education. The big difference is even greater in less developed countries where the supply of educated workers is limited. From the perspective of supply and demand, it is easy to determine why education increases wages. Companies are willing to pay more for highly educated workers because such workers have higher marginal products. Workers are willing to bear the cost of acquiring education only if such efforts are paying off (Mankiw, Taylor, 2000, p.58). According to the analysis of the labor market, employers and leaders want employees to continuously modernize and further develop their skills and to communicate effectively and work independently. In the publication, "Why the sphere of business worry about education?" it was concluded that the new economy require individuals who possess a wide rang of high-level skills and competencies such as critical thinking, problem solving, teamwork and decision making skills (Maksimović, 2006). The world today is a sophisticated and multifaceted. People need to have a high level of skills to act, respond, learn and react to various changes. The success of every profession and every individual will largely depend on his ability to think, learn, adapt and communicate. In these conditions, a special place for technology in the future it will continue to be the main power in the workplace, community and individual lives. For all individuals, especially those who belong to the sphere of management, it is necessary to understand how to use the tools of technology (Maksimović, 2006, p.37). These tools are: computers, networking, and other technologies, audio, video and other media and multimedia tools. These tools enable people to effectively monetize their work and daily life and to set of tasks

such as electronic commerce, multimedia programs, presentation, preparation and processing of database research, networking and communication with others. Given these estimates of analysts and theorists, the question in the academic world is how to develop or even better refine the appropriate skills and student's knowledge in higher education institutions. If we talk about management studies, business and administration (because these areas are often linked) it receives alarming significance and requires special involvement of higher education institutions and those who manage them or implement programs (Ostojić, Damjanović, 2013, p.519). Consequence of the specific human capital relative to physical is that there is a material embodiment of human capital. Therefore it can not be possible to establish an effective lien against such capital. This makes it difficult to finance investment in human capital, particularly education financing. Because the capital market does not provide the socially desirable offer of debt to finance investment in human capital. Those who invest in human capital, and education, is not able to internalize the overall yields of these investments, so there is a difference between private and social rates of return.

There are significant implications for the behavior of companies in terms of capital investments of its own employees, and education of the labor force employed in the company. The company acts so that equates the present value of future returns engaged workforce and the present value of the cost of investment in human capital. The greater the share of investment in the workforce, the less fluctuation, since workers will remain in the company, seeking to appropriate the returns as long as such investments in equity. Practice has shown that the standard accounting categories are not reported in full production potential available to a company. Existing accounting categories of fixed assets or equity does not include fund of human capital that have employees in the company, thus effectively disposes of that company (Pelević, 2004).

### ***SUCCESS RATE AND APTITUDE***

The process of production and management are increasingly dependent on the role and importance of human resources. Staff is in the process of reproduction occurring as drivers and factors of economic development and a factor of development of the productive forces and production relations. So far, the staff was neglected ("minor factor"), which adversely reflect on their personality and performance, especially in creativity. This led to a series of contradictions and inconsistencies in the development of the productive forces, and had come to the question of the redefinition of leadership in our conditions.

One of the basic requirements for access to assessing the success of any staff profiles is that, to meet the main principle of the operation: "adequate staff for the proper technology", it means every man to "own" the right place. This principle reaches its appropriateness thereby ensuring the success of the enterprise, and individual satisfaction. The worker can achieve optimal results only on jobs and the

next workplace where the best come to the fore of his abilities. He will be happier if you achieve success in the workplace that suits his skills and abilities, more than assigned to the position of the status and out of range of his abilities and not achieve the expected results.

Our economy is measured and assessed part of the work and come up with undesired phenomenon that staff are allocated to jobs that require higher skills than theirs, because it brings higher status and greater profits. Accordingly, the first phase of evaluation of personnel in all companies and institutions related to the fact, whether they are adequately distributed in the work process. This will justify the "cost" only if they have been systematized jobs and established measure of success in work and the criteria for it.

The result of the work can not be measured by precision instruments, but it can introduce a system of evaluating personnel and evaluating their effectiveness. Performance appraisal system of staff is important from the standpoint of optimization success. That system is very suitable for the proper progression of staff and their change from responsible places.

Evaluating performance of staff is evaluating the properties and behavior of staff, measurement and analysis of the results of their work. Assessment process consists of several stages: assessment of personality, assessment activities, as well as the analysis and evaluation of the success of an individual. Each category of personnel requires special methods of assessment, their adaptation conditions, the complexity of the tasks and functions and social relationships. Previous methods have a universal character, a certain element method are subject to change, given the nature and purpose of performance evaluation of staff (Stefanović, 1996).

The success of the work includes motivation, creativity, and performance evaluation. The motivation for the work is the biggest problem in the field of human resources management. An important reason for the purposes of designing work motivation is the need to understand the mechanisms of behavior as a basis for building motivation. One of the tasks of a manager becomes successful management of human resources and building motivation. The problem of long-term retention of high quality staff and employee motivation is a constant creative input and includes two basic questions:

1. How to measure the performance of and contribution to the people and
2. How to reward their work?

For the first question are related to the problem of criteria and methods for measuring and assessing the work contribution, and success in one or more dimensions (quality, quantity, innovation, etc...), and the second question elaboration best remuneration policy and its implementation of a range of instruments. The company must start from the objectives to address the issue of how to achieve these goals and to measure their performance. Managers design tasks in jobs that are in line with organizational goals employ people with the necessary skills, then train, motivate and reward. These are the basic aspects of staffing that allow successful operation, and evaluation of the work is used primarily for monitoring the implementation of the objectives to develop corporate

strategy. One of the most popular and most widely used control method as successful managers and staff management by objectives. The advantage of this method is that the managers and staff familiar with the objectives to be carried out. Creativity that carries the individual comes to the fore in a particular climate and enterprise value to the social environment. The task of management is to recognize the creative individual in the company and provide the conditions in which they will be his ability to play. The success of the work of the permanent care of the entities and personnel management. An important role in that, have the motivation, creativity and evaluating success (Ostojic, Damnjanovic, 2013, p.522).

### ***THE METHODOLOGY OF EVALUATION OF PERSONNEL***

The success of the staff, especially managers assessed in different ways and by different methods, which are conditioned by the general terms and conditions in society. In relation to "the object" of assessment, there are three levels of managers. Each level requires specific methods, given the complexity of the functions, powers and responsibilities. There are three methods of evaluation for system performance evaluation of staff.: first, the assessment made by others managers (board, commission, researcher on the basis of specific methods - tests, reminders, surveys and results); Second, the assessment given by the head manager thru methods "control shares"; Third, evaluations are conducted by team (appropriate manager to other managers and authorities, as well as the research team) using the "Chart of leadership." Methods for assessing the success of managers are: (Stefanović, 1996)

- Method of ranking
- Scales courts method
- Free choice of method claims
- Method of forced choice statements
- Method of critical vessels
- Content analysis method biography (dynamic score last time in preparation for a new feature),
- Method of continuous "control their own actions"
- Method "chart management"
- TAM - method (evaluation capabilities, performance and features)

The above methods are based on the familiar grounds and used objective criteria and standards with the help of mathematical and statistical indicators, which means that instead of bureaucratic - administrative assessment managers, it's used impartial assessment of the appropriate people, comparing the obtained value with the valuation requirements of the respective functions. Correlation between these two levels of parameters, is the condition that someone can be a candidate for appointment or reappointment to the position from which he will manage.

There are two basic criteria for evaluating managers: relative score value and performance evaluations, which restrict the choice of the appropriate method. The procedure of the evaluation requires certain principles, systematic, and contains a number of elements, such as the purpose and program evaluation; draft scheme assessment; choice timeline evaluation; rules of evaluation and accuracy assessment. The choice of method depends on the evaluation criteria and elements of the assessment, but also on the specific conditions and the appropriateness of that action.

Method of ranking in the evaluation of managers consists in ranking the group of managers to total abilities and quality from best to worst. It is suitable for the assessment of workers and managers to lower organizational units for comparison. Scale vessels, containing the bad side, which are reflected in the lack of precision in grading. The method of free choice of the claims made in the selection of those statements that best characterize a particular function, and the person who is performing. Assess the behavior, performance, and accountability of the head, in order to choose the positive and negative sides of the person. Claims are converted into points on a given system, which provides numerical expressions and measurement. Thus, the assessment can be compared with the heads of other companies. This method is suitable for assessing the performance leading staff, particularly because of the possibility of quantification. Methods such as mandatory choice statements and critical cases are of more recent date. They are complex and time consuming, and did not show confirm proper value. The first time the long-term preparation (selecting several groups claim to good and bad), and in the second, it takes longer to wait for the critical cases that characterize the evaluated person. Method of analyzing resumes suitable in the appointment of managers as gaining insight into the overall operation. To do this, collect all the data about the person, since it is necessary for the success of the sum of all the characteristics and behavior in different situations. The most important criteria are achieved efficient economic outcomes, and the quality and level interpersonal relations in those business units where the specific manager acted. It's important to see business results and attitude towards co-workers, agencies, and organizations. Data are obtained by objective methods, surveys and direct conversation. The method of "control shares" is a method of self-assessment. The aim is to achieve stability, balance and efficiency of the organization, and the adaptation of his own work. It has its own self-assessment of creativity in setting up the organization of work in the production and social frameworks and way that it is optimal, consistent and appropriate given situation, in order to allow maximum efficiency of operations. This method is the self-awareness and monitoring of the situation and the organization of work. It can serve others (board) as the ability to control the current work. Figure leadership is the latest method of assessing the success of managers. It covers all stages of company development: creating the concept and construction of the organizational structure, training executives, setting up the organization and its implementation, measuring the efficiency and rationality of organizational change. Prior to the evaluation of the success of the program makes enterprise development this is of particular importance, because the assessment has a complex personality of leaders in all stages, from concept to results. Given that specifies the powers and responsibilities through the program, and trained personnel for the proper function of the company, it is possible to monitor the contribution of each manager. Who it fails, or is the weakest link in the chain must be replaced. The work is organized in teams, evaluate the team, a determined individual

responsibility. Phase of the program include: seminars, team building, integration of various teams by profession and status, setting organizational goals, achievement of goals and overcoming "resistance to change" and stabilize the organizational structure. This method provides tangible results in business, education leaders, strengthening the company and the opportunity for realistic performance evaluation of managers. TAM - method is complex and multidimensional, as it allows the right image for the promotion of staff. Managers are the "driving force", their impact and effect felt throughout the company, not only in his country. That is why it's important to be so significant the role of manager evaluates by certain principles, which will allow a delegate certain roles. This will be the most successful seen by the following principles for evaluating managers (Stefanović, 1996)

- Management functions are evaluated by a separate system, because they are fundamentally different from other functions in each company,
- It is necessary to choose the elements for assessment (knowledge, quality, experience, competence, responsibility, influence),
- Establish measurement of functional duties and responsibilities,
- Each element to give proper meaning of the wide variety of facilities and activities and
- Score to tie the components and the complexity of the corresponding function, because it is the foundation of every grade behavior and understanding tasks.

Choice of elements in evaluating is the question of principle in achieving the purposes of evaluation. With the evaluation of results, and evaluating the subject property managers such as properties important for successfully solving tasks, refer to the members of the collective, general personality traits and moral properties. It would be difficult to enumerate all unbundled properties that are related to personality characteristics and functions, because it's always should keep in mind that the selection and ranking depend on the specifics of individual functions. Generally speaking, it seems that the following features of the profile manager are the most important: (Stefanović, 1996)

- Ability to apply knowledge
- Persistence for understanding and resolving complex problems
- Sense of organization
- Sense of rationalization
- Talent for coordination and cooperation
- Courage to take responsibility and
- A realistic assessment of their own capabilities.

Each selected attribute for evaluating the weighted and weighted results are added, which allows the comparison score between the evaluated individual people, according to the relative satisfaction requires certain functions. Evaluating the success of managers must contain the principles of professionalism, application method, building assessment system, impartiality, transparency of results and achievement of program objectives rater. The procedure is performed through the evaluation of evidence, analysis, synthesis and control.

## ***ELEMENTS FOR EVALUATION***

The ability of managers is evaluated by how he mastered the strategy and tactics of business policies in the market economy. In other words, how he was able to organize the business and what results have been achieved in the company. Assessment skills and performance of employees in a company subject to scientific investigation. This task is the evaluation of management actions in terms of market relations and the study of the level of control in certain collectives.

Evaluates the effectiveness of achieving the basic functions of the company by managers with special powers and responsibilities such as planning, organizing, delegating, coordinating and controlling. The evaluations are the result of specific solutions that perform complex functions of any business executive in our conditions, within a complex range of problems, since the managers management as a profession deserves to be treated with different aspects: economic, technological, organizational - human, psychological, sociological, legal, social, medical and even.

The function of leadership consists in balancing the available resources to achieve the objectives, where it is necessary to coordinate the multitude of specialties. Expertise is absolutely necessary, but more in the form of gaining knowledge for their application, given that the manager must be able to organize, control and fit. He has his creative imagination to have a vision of a new mechanism for the creation and implementation of new business policies. A man can be trained for that through the teaching or educate at schools for managers. Achieve such a manager profile, with some personal predispositions, can and must be achieved through learning.

Training and education for managerial function must be understood as an ongoing process, since many of the functions have a dynamic character, and that in the conditions of market economy must not stagnate. The function of the management body should be creative, and less operational. It is intended for the role of policy and organization, and operational tasks necessary to delegate to its assistants. Business executive coordinator who by delegating, directing and controlling realize the responsibility that can not be fully delegated. This role manager can be achieved by mastering and applying the three essential functions of the company: long-term policy development, personnel policies and deliberate scientific organization of labor. It necessary to set up the thesis that concentration on these three basic functions leads to the development and optimization of interpersonal relations.

It's not about the managerial staff with only these three functions, that is, they only keep to themselves, but to the predominant activity in this regard focus to these essential functions for the success of the business. Actually manager delegate functions to the appropriate partners and service to professional elaborate ideas and concepts. Delegate tasks to the experts, which means to execute them cheaper, more professional, faster and more efficiently. Today managerial personnel asked not to be "scrapbook", but experts - the organizers.

## ***GRADING SYSTEM STAFF***

The study of human nature occupied the experts in different times and spaces. When the pre 2.5 millennia asked Confucius what is wisdom, he said that wisdom is "knowledge of mankind." With the help of scientific knowledge, now can be assessing and evaluating personnel to predict the level of achievement in the career of the individual and the degree of its success at work.

An evaluation of actor in work processes is an expert job, but it also means the democratization of interactions between staff of different structure and position. The purpose of the evaluation, the possibility of the most able to take key positions in the system of promotion, in order to achieve optimum results from available resources. Rating capabilities and performance of staff enables the promotion of staff in relation to the vertical, horizontal, diagonal and spatial mobility.

In parallel with the needs arise resistance evaluation for various reasons, such as: the inertia of the organization which makes a change, "freeze" status positions, the vested interests of certain power, neglect of public work, promotion without criteria. The transition of an economy dominated by innovation at all stages, and in the personnel policy. Forms of cooperation in work processes as an important factor in efficiency means joint effort of skilled individuals in an effort to achieve collective goals. This principle demands and evaluating capacity and performance of personnel, especially management.

The practice is said to be appointed by the head manager by ability. And when it comes to optimal staffing solutions, the ability to be increased through education for the position of leadership. Successful cooperation in the work is role and tasks of managers, embodied in their actions and behavior, of which the most characteristic as follows (Stefanović, 1996):

- treat the workers as individuals
- learn workers' about their rights, duties, and obligations
- give appropriate recognition to employees
- Promptly inform workers about the events and the set changes
- Optimal use the ability of workers
- Motivate employees to work and education and stimulate results
- A balance of common interest
- Provide a creative atmosphere and mutual trust

Good management is achieves that gives the best possible results with the corresponding structure of workers. Given that the results obtained by all the staff, they are the core responsibilities of managers for the success of the business which makes homogeneous power to companies. Any demands from the outside can not successfully change the lack within the company, but it can own forces. The grading system of staff displays the following elements of staff character:

- Type of ability (primary mental abilities and organizational skills)
- Character traits (primary traits of temperament and primary traits)
- The ethical virtues of personality (ethical principles and moral habits of behavior interpersonal relations).

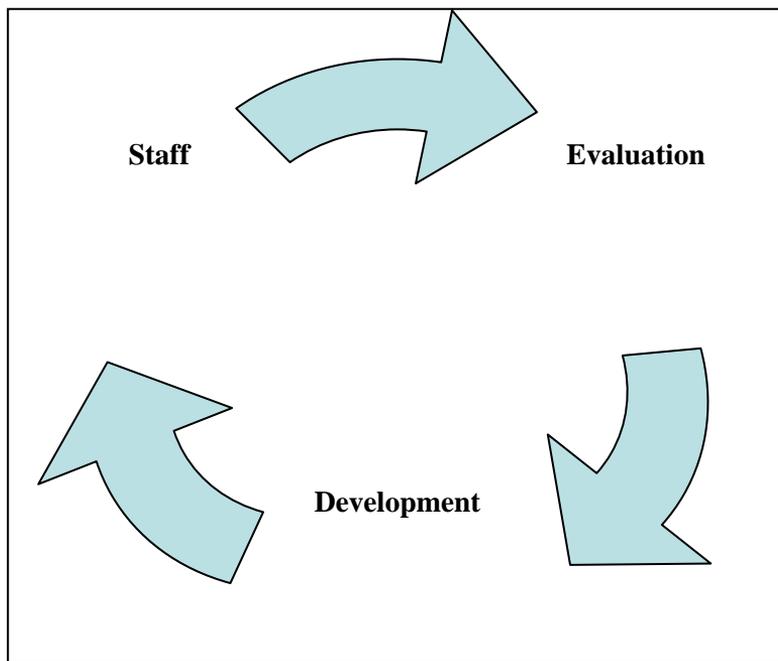


Figure 1: Contained method of feedback

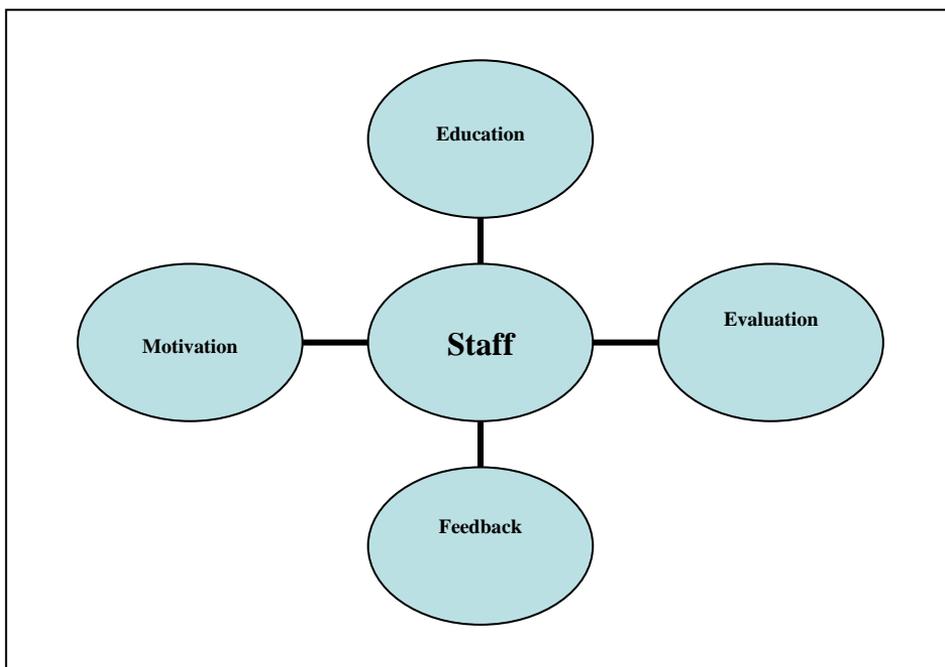


Figure 2: The basic elements of staff development

## ***THE IMPACT OF QUALITY MANAGEMENT IN THE EVALUATION OF STAFF***

To order to evaluation of each worker could have its full effect, as one of the main mechanisms to comprehensive results lies in the quality training and multi-system management. To make managers aware of how and what parameters should be evaluated primarily employees is essential to the training of the managers at the highest level possible, which will include all modern trends in business. The knowledgeable staff is a blend of theory and practice, the best and the real, the possible and necessary. One of the part of this paper shows how managers should be trained to had from employees the highest degree of respect, credibility, loyalty and motivation, but also themselves to have sufficient knowledge to evaluate the other. In the early stages of the emergence of corporate society, it was thought that the manager should be an 'iron fist' of the companies, where there can be no compromise and deviation from the standards and quality that are set before them, and that one mistake can lead to loss of job. An important part of the appraisal process involves recording incidents and behaviors that is out of the ordinary. These are referred to as "critical incidents" and "significant behaviors"(Max, Bacal, 2011). However, at the present time, these phenomena must be eradicated, because companies need to recognize the dearth of quality manpower which is on the market, a particular need to focus on staff who are in their own ranks and recognizing them as future potential managers or persons whose knowledge and dedication can help increase company profits.

At the present time, when the recession practically 'destroys' human resources managers within the company played a major role in the recognition of the problem and the need to find a way to highlight the personnel policy as a capital for quality business, but also with the continuous control and evaluation to reach a clear success indicators or potential downtime.

Modern managers are all aware of the importance of skills working with people and is of crucial importance since their following capabilities:

- to select, train and empower employees,
- to shape and lead group meetings of all kinds,
- to manage all sorts of conflicts between powerful individuals and groups,
- to influence and negotiate on an equal basis
- to integrate the efforts of people of different professional specialties.
- to implement best options to evaluate the work of employees and then send a clear feedback

So the managers can assess the work of their employees, it is crucial their level of knowledge, in which leading next abilites:

- Humane
- Technical and
- Conceptual,

because their unification, the manager becomes highly competent person who can evaluate in a full form perform of existing staff.

## ***KEY PARAMETERS OF EVALUATION***

Assessment of job performance is a process that measures the contribution of employees in achieving the goals at a time. If such an assessment is not done properly can damage relationships, in contrast, accurate assessment can encourage employees to better realization of the goals and set tasks in front of them. Today, in addition to higher-level managers and associates and colleagues all over the process of assessing performance, and includes self-assessment, which should contribute to a single dose of reality with the employee (McCourt,2003).

Control should not defend anyone. On the contrary, everyone should be content, for it provides better results. Also responsible leaders should not omit the control for the alleged trust they have in their co-workers, and thus to make a big mistake.

The trust should not become a naivety or even abuse, but there needs to be both, and the control should not be exaggerated, as there would be no resistance to the employees.

Excessive control may cause adverse effects. (McCourt,2003) For a good and successful control required many assumptions and the best control system will fail if not set good plans, norms and organizations to function.

Regular employee evaluation helps remind workers what is expected of them in the workplace, and provides employers with information to use when making employment decisions, such as promotions, pay raises, and layoffs. In a traditional employee evaluation, the manager or supervisor writes and presents the employee's contributions and shortcomings to the employee. The manager and employee then discuss improvements. Some organizations ask the employee to write self-evaluation before the meeting. The performance evaluation process in organizations is ongoing - every day - as the manager or supervisor observes and coaches each employee's performance. In many organizations with a formal employee evaluation process, employees are ranked and rated in comparison to other employees. Depending on the employer's practices employee evaluation can frustrate and demoralize employees. All previous mentioned elements of evaluation alone can not provide a complete picture of the performance of employees. Combining all the available parameters can contribute to a clearer and comprehensive picture, as an individual as well as all sectors of the company. Key synergies in the evaluation of employees, as well as improving individual and group performance are:

- Improving the training and education of employees
- Improved work plan
- direct conversation
- Clear and unambiguous way that assesses the performance of work
- Establishing feedback

Without quality training and development of workers, managers will not be able to ask for high grades of employees, because they will have sufficient knowledge to perform a given operation, which will in most cases lead to negative results in the performance evaluation. Therefore it can be concluded that neither the planned work process will not be correlated with expected if employees do not have a sufficient level of competency, so that is one of the key elements in corporate success today, the fact that the adopted plans must constantly revise and harmonize with the current market needs in order to achieve long-term competitiveness. Every action must have a reaction, which is the directing relationship between the manager - employee, because through communication can greatly enhance the effect of a real transfer of information to the employee. Through directing conversation, should be transferred expectations, deadlines and parameters of success that will continue to measure through a clearly defined form of evaluation. As the final phase of this part should be presented feedback to all employees' on the current state of work, level of success, segments where there is a deadlock and how they expect it to be resolved in the future. The joint action of these items leads to the best possible results in the understanding of the tasks and removes errors.

### ***METHODS TO IMPROVE THE PERFORMANCE OF STAFF***

Whether it is about the results of the performance of employees, the question of wages or of implementation of the new evaluation plan employees, there are several elements that have been identified as essential in improving the above mentioned elements of functioning and decision-making. Through this approach to employees, managers, unless they come to clear results of performance evaluation, they also improve their ability to interact with employees. Control of results relates to the quality, quantity and value of output of certain processes of the organization (products, services and decisions) (Petković, Đokić, 2012),

In the case of today's modern corporate world, the following approaches should be taken into account as a key to developing perception among workers about the importance of evaluation as a process of improving the performance, not as a repressive methods which included a penalty for errors. That is why the interaction is very important for the improvement of the performance of each individual. Primarily be addressed to the following parameters:

- The employee should never hear about positive performance or performance in need of improvement for the first time at formal performance discussion meeting, unless it is new information or insight. Effective managers discuss both positive performance and areas for improvement regularly, even daily or weekly. Aim to make the contents of the performance review discussion a re-emphasis of critical points.
- No matter what are the components of performance review process, the first step is goal setting. It is imperative that the employee knows exactly what is expected of his or her performance. Managers periodic discussions about

performance need to focus on these significant portions of the employee's job. Manager need to document this job plan: goals and expectations in a job plan or job expectations format, or in employer's format. Without a written agreement and a shared picture of the employee's goals, success for the employee is unlikely.

- During preparation and goal setting, manager needs to make how he will evaluate the employee's performance clear. It's important to describe exactly what he is looking for from the employee and exactly how will evaluate the performance. Manager need to discuss with the employee its role in the evaluation process. The employee needs to understand that if he does what is expected, he will be considered a performing employee.
- If managers company uses a form that manager fill out in advance of the meeting, it's good to give the performance review to the employee in advance of the meeting. This allows the employee to digest the contents prior to her discussion of the details with manager. This simple gesture can remove a lot of the emotion and drama from the performance review meeting.
- Preparation is an important part for the discussion with the employee. It's not good to go into a performance review without preparation, because in opposite performance reviews might fail. It can be missed key opportunities for feedback and improvement and the employee will not feel encouraged about his successes.
- When manager meet with the employee, it's important to spend time on the positive aspects of his or her performance. In most cases, the discussion of the positive components of the employee's performance should take up more time than that of the negative components. The employee will find this rewarding and motivating. But, is necessary to mention the areas that need improvement either. Especially for an underperforming employee, manager needs to speak directly and not to mince words. If he is not direct, the employee will not understand the seriousness of the performance situation.
- The spirit in which manager approach conversation will make a difference in whether it is effective. If manager's intention is genuinely to help the employee improve, and he have a positive relationship with the employee, the conversation is easier and more effective. The employee has to trust that he want to help him improve his performance. He needs to hear him say that he have confidence in his ability to improve. This helps him believe that he has the ability and the support necessary to improve.
- Conversation is the key word that should define a performance review meeting. If manager doing all of the talking or the meeting becomes a lecture, the performance review is less effective. The employee will feel as if he was yelled at and treated unjustly. This is not the way how manager wants employees feeling as they leave their performance review. Manager want an employee who is motivated and excited about his ability to continue to grow, develop, and contribute. Aim for performance review meetings in which the employee talks more than half of the time.

This kind of approach is very complex and requires a lot of effort by managers, as well as some time as he could in the right way to master these methods. Such an approach to the evaluation of performance improves relations of the manager and employees, improving work within the organization, raises communications manager-employee at a higher level, which will have a positive effect on customers, as well as relations within the working community.

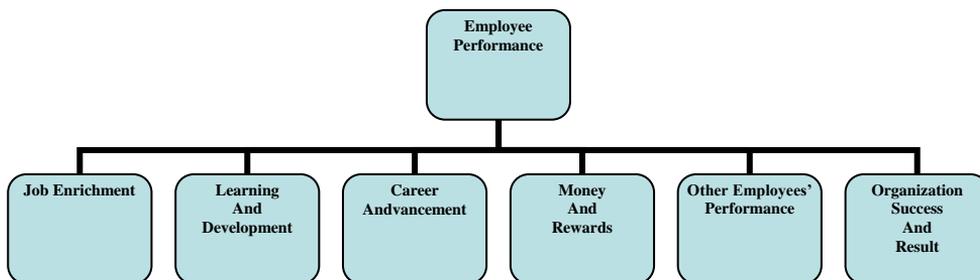
### ***LINKING EMPLOYEE PERFORMANCE TO RESULTS***

If an organization wants to improve the performance of its employees, it must think in terms of everyday communication with employees. To talk about the new tasks, plans, terms, ideas, purpose. This segment of corporate cultures is important because in this way remind employees that are stored in a serious system which largely depends on the quality of their work. Why is it important? Because in this way the effect of employees associated with the resulting company.

It is important to emphasize the employees that when they give their reports on time and express their views on improving the business, it immediately gives a time limit within which the management will have to respond. It reduce time for the adoption of certain plans. Another thing that should be encouraged among employees is to attend meetings where they will be senior managers and will then have the opportunity to interact express their particular opinions and ideas. Also, by participating in some project employees will have the opportunity to become familiar with the company's strategy.

The main reason this results-based approach works is because manager is able to explain the value of positive performance from different perspectives. Manager can talk about results that are important to employees and results that are important to the organization. Manager is also able to use multiple reasons to explain why something is important or why something is not important. So if employees react negatively to one result (ie impact another employee), manager can use a different result (ie impact customer service) to illustrate his performance conversation. That means manager do not have to say, "Do it because it's your job."

Correlation between quality of work of staff with company success is one of the most important design feature to the evaluation of the performance of the individual. At the individual level, you can link employee performance to desirable outcomes such as greater autonomy, less stress, reduced workloads, or increased visibility. On a broader level, employee performance can be linked to organization mission, goals office, customer service, or team performance. These require employees to look at the larger impact of their performance results. Connection between the employee's work is in many aspects relates to a given overall evaluation. If an employee manage to link at all levels that are listed in the table, then we can talk about the greatest possible work performance of the individual with the group (company).



*Figure 3: Primary tasks linked to employee success*

Evaluation and assessment of performance of the individual or sector brings with it a number of methods and approaches. Access to link employees and the performance of enterprises, primarily given the importance of each individual to be in an organized system of work, his contribution to evaluate, assess, and always improving. Consequently gets a sense of belonging to an employee and his desire to continue to provide its full contribution to the companies development and market competitiveness. Direct access to the employees, who are not only applies to the written word, or by filling out the form of reports, but direct interpersonal communication, employees are given the opportunity to be a listener and proposer and critic. That's why the conclusion should be that it is best to evaluate performance of the individual comes through quality training and development, direct contact and linking or creating an unambiguous sense of belonging to the company.

## **CONCLUSION**

The new role of managers is to improve the process of developing enterprise flowed better. Modern division of labor shows a shift from the classical model of employment in enterprises. Companies can analyze their field activities and expand to new business and so open up the need for new skills. Techniques for assessing the competence and efficiency of the staff have a clear advantage when it comes to decisions in employment and to obtain staff with the highest qualifications that should be introduced into the business, and also play an important role in the selection of programs for training and development. Accurate assessment of expertise has proven to be a very useful tool in the formulation of plans for business development and management careers.

The new employment processes used various tests and assessments. Potential staff must be able to create good working relationships with clients and colleagues, and exhibit a high level of motivation and ambition in their work. Staff require a high level of knowledge in its profession and the excellent skills of communication and cooperation.

Without quality staff and business can not be well done. The main question in this equation is the improvement of techniques and skills that lead to increased ratings and long-term competitiveness of the company. System of training and education, evaluation, flexibility in policy decisions and implementation of modern business trends lead to the highest possible results.

The aim of this study was to demonstrate the importance of education at all levels in the company, the importance of planning management, the establishment of methods of evaluation of performance, his individual and collective approach and the methods by which the employee is the best way tie for the success of the company and thereby increase their level of motivation and commitment, all with the aim of providing quality services that are in accordance with the wishes and needs of consumers and market.

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# **EMPLOYEE PERFORMANCE AND DEVELOPMENT: ALCOHOL AND ITS EFFECT ON ORGANISATIONAL PERFORMANCE**

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## **INTRODUCTION**

*It has indeed been recognised at least since the 1940s that alcohol is a 'problem' in the workplace although it may seem surprising that serious efforts to cope with the 'problem' were initiated as recently as the late 1980s (Pratt, Tucker, 1989). Pratt and Tucker add that, as was with the case of alcohol as problem on the roads, it took about a half a century from the first official recognition of the problem until the Criminal Justice Act of 1925 when prevention became reasonably effective. However, the case of alcohol use or misuse in the workplace is not a straightforward issue, as this paper will identify. In the case of the workplace, the main problem areas that are seen to be of concern as a result of alcohol use or misuse are identified as alcohol-related accidents, reduced work performance and loss of working time.*

*The need to focus the study of this paper on the workplace is based on an understanding that work, and for that matter the workplace, offers a setting and an opportunity where one might conveniently scrutinize some of the most important factors shaping the lives of individuals. Therefore, based on the aims of this paper, emphasis will be particularly placed on multinational companies (MNC) (Interviews for this study were carried out with individuals from MNCs based in the East Midlands, United Kingdom) to address the overall aims of this study.*

**Key words:** *Employee, Work, Organizational Performance, Alcoholism*

**JEL Classification:** *I12, J24*

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## ***INTRODUCTION***

### ***ALCOHOL AND EMPLOYMENT***

Alcohol misuse in the workplace has long been perceived as being associated with accidents, inefficiency and absenteeism (Gill, 1994). In response to these claims, a considerable amount of literature has been produced and these relate to drinking habits and alcohol-related problems amongst workers in different settings and to initiatives designed to curb, prevent or respond to alcohol misuse in employment. According to Newman and Sell (1992), the initial problem related to alcohol misuse in the workplace is finding a realistic definition for the term 'misuse'. Even the widely accepted medical definition which characterises it as a long-term disease creates much controversy. It is added that the conflict over the diverse views on the definition of alcohol misuse or abuse will not be resolved soon. Banta, Tennant (1989) made two observations on the issue. Firstly, while there is a debate over whether alcoholism is an illness and what causes it, most definitions agree that it is a condition of dependency on alcohol. Secondly, alcohol is, of course, a drug and suggestions have been made that efforts employed in addressing alcohol misuse in the workplace should be similar to that of drug misuse.

Newman, Sell (1992) add that the causes of alcohol misuse, especially in employment, are as elusive as a true definition. Steele (1988) suggests that potential causes range from social influences to organisational pressures and Ames (1987) argues that the workplace can strongly promote alcohol misuse if the employees feel alienated and if manager adopt a permissive and ambiguous attitude toward alcohol. It is clear that most studies relating to alcohol use and the workplace have intended to prove alcohol's detrimental influence on the workplace and has thus 'criminalised' the act of consuming alcohol in any form or amount.

Further emphasis on the susceptibility of the workplace to alcohol misuse among employees is drawn by Newman, Sells (1992) who refer to the notion that drinking on the job usually evokes some form of major sanctions. It is further stressed that many companies are hesitant to specify policies beyond on-site consumption or condition on arrival at work. Most organisations (including some stakeholders) view policies or positions taken on situations beyond work as invasion of privacy.

Roman, Trice (1972) claim that factors within an organisation that may be potential causes of alcohol misuse include low structural visibility, occupational obsolescence, absence of social controls (such as required on-the-job drinking), severe role stress and competitive pressure. Campbell and Graham (1988) contribute to this by stating that a lack of personal achievement and recognition and unchallenging work may also contribute to job-specific causes of alcohol misuse. To add to this debate Holland (2005) adds that the nature of work has an association with a culture of use and misuse of alcohol and illicit drugs. It is reiterated that workplaces with high stress factors, job insecurity and isolation or combinations of these factors are seen as catalysts for such cultures.

Typically, discussions about alcohol misuse have been centred on blue-collar industries such as mining, building and transport. However, the fundamental change in the nature of work across society and the volatility of the global economic environment (Holland, 2005), which the United Kingdom is a part of has seen professional and white-collar workplaces also mirror many of the traits linked with the misuse of alcohol and illicit drugs. Therefore with both white- and blue-collar jobs now exhibiting similar patterns in terms of increased stress, job insecurity and more longer and intensive work duration, most workplaces have become a fertile ground for the development of an alcohol culture. However, the IIDTW (2004) argued that there is no established link between the nature and/or working conditions of a workplace and the presence of a drinking culture. According to Lucas (2005), it is very important for employers especially, to focus and examine the type of workplace that they have created or shaped when the issue of alcohol misuse in the workplace is under discussion. Holland (2005) therefore suggests that the culture and expectation that management set is a central issue in any discussion regarding alcohol and other drugs misuse.

### ***THE WORKING ENVIRONMENT AND ALCOHOL USE***

Most organisations, and employers for that matter, often see the development of substance misuse policies and measures as a proactive and responsible stance, without an understanding of the reason for the problems. However this critically misses the vital issue of workplace culture. Henderson et al., (1996) dwell on the need to identify the relationship between general levels of drinking and particular working environments and how consumption may relate to the type of work conducted and the role played by 'normal and accepted' working practices in enabling and maintaining drinking in the workplace. According to Allsop, Pidd (2001), workplace culture is of central importance in framing workplace expectations and social environment and the use of legal drugs such as alcohol and tobacco and illicit drugs. For example:

"In a variety of cultures, formal and informal pressures encourage weekly after work team building and relaxation based on alcohol consumption. Sanctioned drugs such as caffeine and tobacco have been embraced in ritualised breaks in worktime" (Allsop, Pidd, 2001, pp.5).

Along with a study of workforce alcohol consumption by Midford (2001), it was identified that alcohol consumption level among both white- and blue-collar jobs was on par. In addition, Rigby (2005) notes that, in relation to the white-collar environment, drug and alcohol addiction in the financial services and the pressures that lead to addiction have been a celebrated part of popular culture since the coke snorting, heavy-drinking yuppie made his debut in the 1980s. Callus and Lansbury (2002) suggest that the changes in the nature of work over the past couple of decades have seen increased pressures of work intensification and job insecurity permeate all types and levels of work. Ames, Grube (1999) also add that issues such as lack of control, alienation and stress linked with the individual's

perceptions of powerlessness are important factors in substance misuse in all kinds of workplaces.

On the other hand, Holland (2005) emphasises the need to assess cultural issues, in any study relating to substance misuse, by especially dealing with the taboo nature of alcohol misuse in the workplace particularly from the employers viewpoint. For example:

“In the City, on Wall Street and in similar environments the world over, there’s no doubt that alcohol and drug use and misuse are widespread and even talked about – but almost always in the third person. And if individuals are cagey, the banks and brokerage houses are reticent still. The attitude is very much don’t ask, don’t tell...” (Rigby, 2005, p. 30).

Subsequent to this is the externalising of the issue of workplace alcohol misuse by employers, which as noted by Midford (2001), in order to gain an understanding of workplace substance misuse issues, one must look at the wide-range of factors that influence (pressures/powers) patterns of substance misuse. It is added that, “in the workplace, holding the view that drug use is a problem for the individual worker is functional from the point of view of the employers, because it avoids any exploration of how the workplace may contribute to the problem” (Midford 2001, p. 46).

The findings for the IIDTW (2005) study support this stance with regards to the issue of alcohol and drug misuse in the workplace. For example, the IIDTW argue that the introduction of testing and/or sanctions should not be viewed as a quick fix solution and may be inappropriate in certain circumstances. This position is supported by the Australian Council of Trade Unions (ACTU 1991) who state that in any consideration of alcohol and illicit drug misuse in the workplace, broad and diverse consideration should be paid to environmental factors that may form a catalyst and be affected by the issue. The level of drinking in a particular workplace may partly depend on the type of working environment that is present within the company (Henderson et al., 1996). This environment may exert a strong influence on the formation and continuance of drinking cultures through factors like the accessibility to alcohol and the ease with which it may be consumed on company premises, even during working hours. Cooper and Sadri (1991) cite the significance of the working environment and further argue that a working environment symbolised by overall excessive alcohol consumption is more of a condemnation of the working conditions themselves than a reflection on the people who consume the alcohol. The authors add that, for instance, a management may reinforce a drinking culture if there is alcohol present in board rooms and private bars in offices, as well as alcohol consumption within any context related to company work.

Henderson et al (1996) are of the view that, in addition to the working environment and job type, the attitudes of employees to drinking and the ‘normal’ working practices that exist also exert a powerful influence on workplace employee behaviour. That is, in certain situations, such behaviour may be more influential than the organisation’s rules about alcohol consumption. For instance:

“...there may be a formal policy about drinking mandated by upper management that is all but ignored by the majority of the employees, who are responding to less socially distant behavioural expectations that make alcohol use appropriate-even desirable-under certain circumstances... For example, while drinking on the job in a construction company may be against company policy, it may be understood by a group of bricklayers, painters, or carpenters that Friday afternoons are a time for ‘taking it easy’ and ‘having a few beers’. Similar drinking behaviour in another occupational group, computer programmers for example, may result in disciplinary action or dismissal” (Ames, Janes, 1992 cited in Henderson et al., 1996, pp. 31)

The above example therefore indicates that company policy on alcohol consumption may sometimes be disregarded by some employees who are responding to the more ‘immediate and powerful understanding’ that, in the case of the construction workers, drinking on a Friday afternoon occurs and is acceptable. Davies (1979) notes that not all drinking ‘norms’ should be viewed in a negative light as some of these norms have come about because they serve the immediate needs of the employee and the organisation in general. For instance, drinking norms may carry symbolic or actual functions significant for meeting organisation goals, in that it may encourage social team-building and sooth the burden of long shift-work routines.

Although there have been numerous studies (Hagen et al., 1992; Roman et al., 2000; Phillips, 2001) aimed at linking increased alcohol consumption, job insecurity and stress, and other harmful occupational attributes, Lucas (2005) points out that it is not always negative factors driving alcohol consumption. That is, the culture and structure of an organisation, and the society in general, may permit employees to indulge in lunchtime or after-hours drinking to boost networking opportunities.

### ***ALCOHOL CONSUMPTION AND ITS EFFECT ON ORGANISATIONAL PERFORMANCE***

Alcohol use at work has often been considered in terms of productivity, absenteeism, accident rates and the turnover rates of employees. The effects in the workplace have usually been linked to alcohol use in leisure time, at the workplace itself and in the ‘grey’ area between work and leisure such as after-work activities, office parties or other work-related occasions. The aim of this section therefore is to set out what is known and unknown about the alcohol use and its possible effect on the overall functioning of an organisation. Previous research have aimed to quantify the supposed effects, from an employer’s perspective, (Observer, Maxwell, 1959; Godfrey, Parrott, 2005; CIPD Surveys; IAS Factsheets) of alcohol on employees’ performance, however Register and Williams (1992) argue that there have been no significant relationships identified between effects of substance misuse and productivity.

## ***ABSENTEEISM***

It is clear that absenteeism may incur a number of costs to organisations, mostly as a result of decreased output due to days individuals are not available, tardiness, early leaving and unscheduled and frequent breaks. Godfrey and Parrott (2005) argue that although chronic use of alcohol may be associated with longer-term absences from work, the United Kingdom in this respect usually have shorter-term absenteeism cases reported in their particular workplaces. It is added that the relationship between recreational, acute or binge episodes and chronic use of alcohol or illicit drugs to shorter workplace absences in the United Kingdom is under-researched. It is therefore difficult to create a link between alcohol use and absenteeism because employees are unlikely to admit absences are related to alcohol-use behaviour. Godfrey, Parrott (2005) therefore admit that the extent of the effect of alcohol use on absenteeism among the United Kingdom workforce is problematic to assess, hence researchers have often had to resort to estimations as well as assumptions to support their claim.

Previous researchers who have aimed to quantify alcohol-induced absenteeism (McDonnell, Maynard, 1985; Godfrey, Hardman, 1990) have been challenged by Joeman (1992), who on the basis of data obtained from a General Household Survey, concluded that there were no direct and reliable differences in rates of absences between light, moderate and heavy drinkers. It was identified that a relationship between alcohol intake and absence became apparent only when general health and smoking were taken into consideration. The role of alcohol consumption in establishing rates of absence is very vague and the number of absences that can be linked to alcohol is uncertain (Henderson et al., 1996). This indicates the difficulty in determining the costs associated with alcohol-related absences, although calculations have been adopted on the basis of employees' gross earnings and other employers' costs to arrive at figures. Henderson et al (1996) argue that the accuracy of such figures and the true cost to the organisation cannot be justified. It is further stressed that in present working environments, absenteeism should not be included as a cost in the same manner as accidents and job performance losses can be. Besides, Martin et al. (1994) are of the view that:

“...substance abusers' absenteeism reflected efforts protect themselves from harm that might occur if they tried to work; obviously this protection can extend to co-workers and to the workplace itself. While seeming absurd, the suggestion that absenteeism can serve positive functions stands in the face of very imperfect systems of detection of employed substance abusers or implementing effective means for their behavioural change” (Martin et al., 1994 cited in Henderson et al., 1996).

This point of view thus exposes a positive side to absences from work that may be due to alcohol. For instance, in a workforce that has a developed drinking culture absenteeism could be viewed as beneficial since it would prevent accidents and poor performance that may result from intoxication. Hence, the cost from absenteeism which is regarded as a major cost in most organisations as a

consequence of alcohol use is usually estimated on the amount of time lost and the value of the lost production. However, it is clear that such calculations are open to dispute and therefore more accurate information on the nature and causes of absences and employee-employer agreement when assessing such costs would best clarify the association.

## ***ACCIDENTS***

The presence of alcohol use in the workplace has been characterised and highly publicised by its relationship with accidents. Alcohol consumption has been implicated in many high profile cases, particularly involving transportation and although it has not always been possible that alcohol has been the cause of most of these accidents (Henderson et al., 1996), it has always been cited as a possible factor. Findings from a number of studies (Health and Safety Executive, 1993; Davies, Teasdale, 1994) imply that alcohol consumption is likely to be related to accidents both within and outside the workplace. However, the precise relationship is poorly understood and precludes any accurate assessment of the exact part played by alcohol consumption (Henderson et al., 1996).

## ***JOB PERFORMANCE AND WORKING RELATIONS***

Alcohol consumption may affect human performance in a number of ways including gross motor coordination, reaction times and attention (Peterson, 1990; Collin, 1980; Critchlow, 1983). Thus it has been concluded in most studies that working under the influence of alcohol may affect efficiency and accurate at work. However, Henderson et al. (1996) argue that as it is difficult to calculate the overall effect that alcohol consumption has on performance, the decrease in productivity due to alcohol consumption, can only be guessed. Most of the effects that the consumption of alcohol has on behaviour and emotions are well documented (Critchlow, 1983), most especially its effect of lowering a drinker's inhibitions. Thus lowered inhibitions and the perceived benefits that this provides are totally opposite to the general view and often stated unwanted side-effects of alcohol consumption in the workplace. While such effects may be acceptable within a social setting, especially the United Kingdom, they have a particular relevance to the working environment.

Numerous studies have highlighted the positive and negative consequences of alcohol use within the workplace and some have attributed thefts, aggression, lost promotion and encouraging informal groups (Gustafson, 1983; Pernanen, 1991). In contrast, Davies (1981) notes that alcohol use may sustain informal groups, improve relationships between management and employees, and also help with team-building and work as a reinforcer to a certain extent. Example is given of how

alcohol plays an important role of reinforcement, at company gatherings, for reaching production targets or reaching particular organisational goals.

Henderson et al (1996) stresses the point that it is very difficult to quantify the costs, as done in numerous studies, be it positive or negative of alcohol consumption has on job performance or working relations. This is because such beneficial effects are rarely taken into account when cost of alcohol consumption is being calculated while consumption of alcohol in small quantities may not highlight many of the negative impediments cited in several studies.

### ***FIELDWORK RESPONSES - ALCOHOL AND PRODUCTIVITY***

The following section discusses a number of interviews held with different actors and 'experts' about their views on alcohol in the workplace and highlights the actual practices related to the use of alcohol in the workplace. In designing this qualitative research, the researchers were concerned with the data to be collected and the role of the participants in the research process. The use of qualitative research in this study ensured that issues of validity were effectively addressed in terms of how the data collection and analysis really addressed the aims of the paper. Validity may be defined as the extent to which our research explains or describes what it plans to explain or describe (Willig, 2008) and therefore its flexibility and open-endedness allows this kind of issue to be dealt with.

In using a semi-structured interview approach to undertake a research that involves any organisation particularly knowledge-intensive ones, it is essential to still strategically select your sample organisation and a sample of employees and managers to interview. For this research, three business organisations which have office-based work environments were selected for both the fieldwork study. Although these organisations, all located in the East Midlands, are parts of Multi-national Corporations, they still share common characteristics of the British workplace in terms of range of current work and employment practices, and workforce characteristics. These organisations are Knowledge Intensive Firms and this industry represents a major growth area in the Midlands, and the United Kingdom in general, and therefore relevant to consider when addressing any issues concerning the contemporary British workplace.

The question of organisational efficiency and employee performance was presented to the interviewees to identify whether they believe that the use of alcohol in the workplace can be a cause of low productivity, absenteeism and high staff turnover. Thus the interviewees were asked to share their perceptions on how much they felt alcohol use did or could impede the levels of productivity in their particular workplaces. Although most of them stated that they felt drinking could affect productivity in any workplace, majority stated that this would be the case in more blue-collared jobs than the white-collared ones that they worked in:

“I think that people in British society drink a lot, they are drinking people, and they are drinking than most nationalities because they drink everyday. I personally don’t drink because it is not in my personal nature. But I think typical British factory workers do drink and it causes lots of trouble”

One interviewee in a senior role stated that in terms of absenteeism and general performance, alcohol was highly related to productivity. The interviewee explained that in the monthly performance appraisals that were conducted in their workplace, it was evident that absenteeism and poor work performance often occurred on weekends or at the start of the working week. In the interviewee’s opinion, even though there was not much evidence to attribute this trend to alcohol, it was important to acknowledge that it could be partly due to it as some employees had admitted to calling in sick due to alcohol use the night before:

“But could you prove that those were related to alcohol? Not really, but pretty much yes. I mean it was no definite proof like they came in with bottles or came in drunk but to consistently be sick this time of the month and especially these days you could tell. And also people would say they saw them out in clubs the night before and they don’t come into work the next day, you don’t have to be a detective to figure out what the problem is”

On the issues of the British society’s attitude to alcohol and whether interviewees felt that alcohol was a problem in the British workplace, all of them answered in the affirmative. Some said that because alcohol forms part of British culture in general, it was not regarded as much of a problem in the workplace. Particularly in the case of an office-based working environment, most interviewees felt alcohol use was not as much of a problem as it would be in other industries like the manufacturing or entertainment sectors. Moreover some interviewees stated that if alcohol was consumed in moderation, its effects on the workplace would not be as bad or detrimental to productivity as it currently portrayed in the media. As a matter of fact, most of the interviewees mentioned the possible benefits alcohol could have on the individuals in the workplace in terms of team-bonding and socialising, although all of them stated clearly such effects were only possible in out-of-office work functions:

“Sometimes alcohol does make people loosen up and act friendlier and so at the party after work then it would help bonding and employees can work closer”

Such points raised by the interviewees prompted the need to acknowledge the diverse views that arise when the topic of organisational performance and its relationship with alcohol use or its misuse is being considered.

## ***CONCLUSION***

The many opinions about alcohol which are expressed through the interviews, statements from the managerial and official sources like the Charter Institute of Personnel and Development (CIPD), and the government statements are infused with particular appreciations of and world-views on the topic when makes it a very controversial topic. However what brings the issue of alcohol to the forefront in most discussions regarding the workplace is the association that has been made by the above stakeholders among others regarding alcohol and its role in workplace accidents, reduced work performance and loss of working time. Consequently these have been translated to economic and social costs, by numerous studies mentioned in the research, to both the employer and employee and the wider society. Aside these issues mentioned about alcohol and the workplace is also the notion of work which in recent years has been increasingly separated from 'leisure'. Thus the 'need' for the employer or management to ensure that there is a healthy and productive workforce during the working day and on the other hand a similar need on the part of the employee to feel that they are entitled to act as they please, with regards to alcohol consumption, so long as they are 'doing their job' has further strengthened the need to review and examine the issues of alcohol in the workplace.

In the case of this research, the need to address the effect of alcohol use or its misuse on organisational performance seems to be relevant because aside from the above mentioned discourses being present in these workplaces, at least with the ones studied for this research, there is also an ever increasing role of the employer or management in the discussion. That is, there has been a recent influx of discourses regarding employee health and safety as well as their wellbeing in the country and subsequently this has led to many organisations introducing restrictions and regulations regarding alcohol consumption under the guise of protecting the 'drinking employee' and his or her workgroup.

However, other contrasting views have expressed concern about the employer's role in this situation and cited these measures are all a ploy to regulate the individual's actions in the workplace and mould him or her into the 'ideal worker' and that alcohol just seems to be one of the media to achieve this. Nonetheless, aside these debates, there also lie the concerns of the United Kingdom government whom through numerous legislations and rulings have also tasked the employer or organisations with the duty of tackling substance misuse in the workplace. However, with alcohol being a legal and not illicit substance, it has been as much a difficult substance to address, and for that matter study, using the same conditions required to do so for other substances like cannabis and cocaine. Thus the organisation's role in this issue could, on the other hand, be viewed as having being thrust upon them by law and therefore their actions and views regarding alcohol consumption in the workplace, regardless of how harsh or lenient they may appear, are justified by the fear of the repercussions of flouting these laws.

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# **REFORM OF THE HUMAN RESOURCES MANAGEMENT FUNCTION IN THE MINISTRY OF INTERIOR OF THE REPUBLIC OF SERBIA - THE STRATEGIC BASIS, KEY ACTIVITIES AND CHALLENGES**

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## **ABSTRACT**

*The subject of this research is the reform of the functions of human resources management in the Ministry of Interior of Serbia. The aim of the research is that, in the context of complex transitional changes in Serbian community, to identify, describe and explain the strategic basis, key activities (sub-functions), and the challenges of reforming the functions of human resources management in the MoI. For identifying the current situation of human resources management in the police of the Republic of Serbia, and the predictions of the future state of affairs in this area, among other methods - the methods of content analysis, secondary analysis and examinations (surveys) have been used. Among the strategic bases for reforming the functions of human resources management, the following have been particularly described and explained: the need for de-politicizing and professionalization of human resources management function, the need for improving performance in carrying out police duties, the need for quality personnel, etc. This research briefly describes the key activities (sub-functions) of the human resources management function, such as strategy and human resources management policy, analysis and work design, human resources planning, recruitment and selection, employee training, and development of employees and the organization. Among the challenges in reforming the human resources management function, a special focus has been devoted to the design of the introduction of the prestigious human resources management standard, worldwide known as "Investors In People – IIP". For designing of the future model of human resources management in the Serbian police, foreign experiences and solutions of human resources management in the police and the public sector, especially in the Great Britain, have been used.*

**Key words:** *Reform, Human Resources Management Function, Strategic Bases, Key Activities, Challenges.*

**JEL Classification:** *M12*

**UDK:** *005.96:351.74*

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## ***INTRODUCTION***

Human Resources Management (hereinafter referred to as HRM) can be viewed as a scientific discipline and as a management function in the organization. As part of the science on organization, it deals with the study of all aspects of employment in an organization, and as a management function it is within the competence of the human resources sector and all levels of management in the organization. The purpose of HRM is to create and maintain the required quality of employees, and the achievement of strategic business objectives of the organization - the effectiveness, efficiency and economy. All managers, starting from the very top, must act as leaders in the field of quality, because it is their task to establish a quality system and to incorporate it into the structure of the organization (Filipovic et al. 2009, p. 382). Human Resources (hereinafter the HR) are the most important resources in any organization. HR quality directly affects the quality of business processes and their products (decrease of crime rate, increase of efficiency of solving crimes, crime prevention, improvement of confidence in the police and the level of satisfaction with their work, etc.).

Ministry of Interior of the Republic of Serbia has been in the process of reforming its core functions for the last decade; one of which, in the opinion of many experts and police employees, the reform of the HRM functions is the most important but also the most complex. The aim of this process is that the police, from the perspective of the international community, should become a reliable partner and the support of European integrations; and from the perspective of citizens - a public service to which citizens can turn to for help and protection. In order to achieve this goal, the Ministry has to raise its capacity and reputation that enjoys as an institution, which must include the internal reorganization so as to create a more efficient police service, which costs less to the citizens of Serbia (statement by the former Minister of Interior of Serbia, Ivica Dacic, in his opening address in the Development Strategy of the Ministry of the Interior 2011-2016).

The modern requirement of both the public sector and the general public that the police should be more effective in their work and at the same time cost less, represents a basic quality requirement that cannot be achieved without good HR and HRM quality. Such requirement opposes to many factors of traditional police organization and its environment, such as: system inertia, opposition of personal interests to the organizational and general social interests, lack of awareness about the essence and importance of the changes, political interests and the influence that changes should not be not implemented, poor coordination and communication in organization, excessive paperwork and outdated work technology, underdeveloped leadership and management, human resources surplus, etc. In addition, the tendency of politicians towards achieving a better quality of the police, is usually associated with a conceptual misunderstanding of quality, hypocritical statements and inconsistencies. Even though many politicians like to pay lip service to quality, other issues, such as tax levels, are important to them. (Bovaird et al., 2009, p. 166).

The contemporary HRM in police organizations in the developed EU countries is based on the developed activities, such as HRM strategies and policies, job analysis and design, HR planning, recruitment and selection, staff training, performance management, and other. Special contribution to the improvement of the HRM function in organizations has enabled the creation of standards known as "Investors In People – IIP", a prestigious quality management model in the field of HR. MoI of the Republic of Serbia during the past two years has adopted a number of projects relating to the reform of the HRM function, within which the introduction of the IIP standard has been envisaged. In addition to the many challenges in reforming the human resources management functions, the introduction of IIP standards will be the most demanding enterprise and the biggest challenge of this reform.

### ***STRATEGIC BASIS FOR THE REFORM OF THE HRM FUNCTIONS***

Strategic bases for the reform of HRM functions make part of strategic documents of MoI, the official reports of government bodies, the findings of the scientific research and other relevant documents. In the Development Strategy of the Ministry of Interior 2011 - 2016, the section relating to organization and management, emphasizes the need that HRM be reformed from the personnel department of the old type to a modern service that will be able to meet the challenges of the 21st century. In order to achieve this, it is necessary to establish a HRM system based on contemporary standards, criteria and principles of hiring, selection, training and promotion in professional career. Such developed system would allow competition among law enforcement personnel based on competence and results, resulting in high level of professionalism, job satisfaction and legal safety of employees. Moreover, the Strategy states that promotion should be based on transparent procedures, with the use of internal open competitions as rules when it comes to filling middle and senior level managers vacancies in the police, based on the results of the work and advanced training, with a standard test of knowledge and abilities.

The demographic changes in the Republic of Serbia also represent the important strategic basis. According to the data given by the Statistical Office of the Republic of Serbia in the publication "Population, age and gender - census 2011", Serbia has 7,186,862 inhabitants (without AP Kosovo). Compared to the 1991 census (7,822,795), and 2002 (7,498,001), a significant decrease in the population is evident - for 20 years by more than 600,000 residents. Contrary to the significant decrease of the number of inhabitants, in the above-mentioned period there was a significant increase in the number of employees in the Ministry of Interior. For example, in 2002 at the seat of the Ministry there were 7,728 employees, and at the end of 2012 approximately 18,000 (OSCE Mission 2004, pp.95). This has caused increased financial investment in the police, mostly for

staff salaries. MoI of the Republic of Serbia is the largest employer in the state administration, with over 46,000 employees, which is, when compared to some other countries with similar population, incomparably much more (e.g. Kingdom of Sweden has around 9.5 million inhabitants, and only about 28,500 police personnel). The large increase in the number of employees in the Ministry of Interior of the Republic of Serbia in the abovementioned period did not lead to any significant decrease of crime. According to the data of the Statistical Office of the Republic of Serbia, the total criminality of adult offenders in the abovementioned period was reduced only by around 10% (Table 1). However, within this slight reduction, there is a trend of significant growth in crimes of violence and drugs, which indicates a reduced efficiency of the police, the judiciary and the entire community.

*Table 1: The general trend of reported adults for the period 2002-2012*

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
104061	95733	88453	100536	105701	98702	101723	100026	74279	88207	92879

*Source: Bulletin of the Statistical Office of the Republic of Serbia No 558 "Adult offenders in the Republic of Serbia 2011 - Registration, prosecutions and convictions" and announcement No 12 "Adult offenders in the Republic of Serbia 2012"*

Juvenile delinquency in the mentioned period increased by as much as 20% (Table 2).

*Table 2: Reported minors in 2002 – 2012*

#### Republic of Serbia

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
3,251	2,415	3,120	2,945	3,041	3,434	4,085	3,497	3,747	4,323	3,913

*Source: Bulletin of the Institute of Statistics of the Republic of Serbia No 559 "Juvenile offenders in the Republic of Serbia 2011 - Registration, prosecutions and convictions" and announcement No 11 "Juvenile offenders in the Republic of Serbia 2012"*

The above statistics indicate that a large increase in the number of employees in the Ministry of Interior does not necessarily lead to a significant reduction in crime rates, nor does it lead to a reduction in crime rates in certain groups of offenses. Therefore, only the quantitative increase in human resources is not enough to improve the quality of work in the most important areas of policing - the prevention and repression of crime. It can be assumed that in the mentioned period the qualitative attributes of HR and management of these resources were not at the required level.

The following statistics from the Ministry of Interior - Directorate for Analytics, shown in Table 3, indicate that there are serious problems in the quality of staff in the Ministry of Interior. The data relate to criminal offenses committed by police officers of the Republic of Serbia for the period 2002 - 2012.

*Table 3: criminal offenses committed by police officers in the period 2002 - 2012, in total and by categories of employees: uniformed, authorized police officers, and other*

MoI	Year	Employees			
		Total	Uniformed	Authorized police officers	Other
	2002	263	194	31	25
	2003	346	273	44	23
	2004	280	222	32	19
	2005	334	289	22	27
	2006	290	239	22	13
	2007	385	267	76	24
	2008	251	190	31	20
	2009	312	226	23	18
	2010	254	117	22	10
	2011	537	373	67	97
	2012	529	386	72	71
Total		3,781	2,776	420	347

*Source: Statistics from the Ministry of Interior of the Republic of Serbia - Directorate for Analytics*

The average number of crimes, according to MoI statistics, the police officers perpetrated during the observed period of 11 years is 343, but there is a growing trend. Most crimes are perpetrated by uniformed police officers who are directly responsible for the safety of citizens. Participation of uniformed police in 2012 in criminal offenses was 72.96%, while for the remaining authorized police officers it was 13.61%. Statistics of a large number of criminal offenses included in the above tables indicate the major problems in the quality of police officers, especially in the ethical dimension, as well as in the function of HRM. Of particular concern in relation to criminal offenses committed by police officers is the lack of systematic analysis of these crimes, drawing relevant conclusions and recommendations, asking questions about management responsibilities, and taking preventive and corrective measures.

If we take into account the statistics of the presented criminal offenses, the criminal affairs of the senior police officials and managers, the existence of hidden figures of crimes perpetrated by police officers, particularly in the area of crime, corruption, as well as a growing trend of all these, one can say that the state of HR

and HRM is disheartening both for the police and for the society in general. Perpetrating offenses by those who are authorized by the community, equipped and paid to protect against crime; and coupling of some leading men of the police with the greatest criminals of organized and drug crime in the country, which is a topic often used in the media, are the most serious forms of tarnishing the reputation of the police profession.

The important strategic basis for reforming the HRM function is in the attitude of the citizens towards the police. Significant sources of public opinions about the police are found in the public opinion research agencies: Strategic Marketing (2008 - 2010), CESID (2011 - 2012) and the Office of the OSCE - Mission to Serbia on the attitudes of citizens of Serbia on policing, conducted in the period from 2008 to 2012. The above mentioned research show that the greatest number of citizens demand that the quality of the police employees should be improved. 90% of the respondents believe that the appointment to senior positions in the police is conducted on the basis of political and other non-professional connections and influences. In this regard, 30% of respondents demand to de-politicize the police and to improve the education and training of the police (33% in 2008, 68% in 2012). In addition, on average, about one half of respondents require the reduction or elimination of corruption in the police force. A particularly important requirement of citizens is related to the role of the police in the community. On average, around one-third of the respondents believe that the police is a service of the citizens, and the majority believes that it currently has the role predominantly oriented towards the Government of Serbia and the political parties.

In the recently conducted empirical research of opinions of heads of Criminal Police in the Republic of Serbia on the quality of HR and HRM function, the results also point to significant problems in this area. The results are shown in Tables 4 and 5.

Question: "How do you assess the competence of crime police officers?"

*Table 4: Assessment of competence of crime police officers*

Quality dimension	Quality level in %		
	excellent	good	poor
Expertise	15.5	64.3	20.2
Ethics	17.9	70.2	11.9
Motivation	7.1	65.5	27.4
Experience	12	67.5	20.5
<i>Average value</i>	<i>13.12%</i>	<i>66.87%</i>	<i>20%</i>

*Source: Klisarić, 2014, pp 451*

The distribution of the responses on the quality of competence of crime police officers is mainly at the good quality level, the average value of 66.87%, followed by the poor level, the average value of 20%, and lastly at excellent average value of 13.12%. The highest value was recorded for the dimension of ethics (17.9: 70.2: 11.9) and the lowest value for the dimension: Motivation (7.1: 65.5: 27.4).

The lack of motivation as the biggest problem in HR, seen from the perspective of the heads of Criminal Police, is the consequence of the poor quality of HRM, which was analyzed in the following question:

Question: "How do you assess the quality of human resource management?"

*Table 5: Evaluation of the quality of human resource management*

Quality dimension	Quality level in %		
	excellent	good	poor
HR planning	5	57.5	37.5
HR recruitment	3.7	52.4	43.9
HR development	6.1	57.3	36.6
Career advancement	4.9	61	34.1
<i>Average value</i>	<i>4.92%</i>	<i>57%</i>	<i>38%</i>

*Source: Klisarić, 2014, pp 452*

The distribution of the responses on the quality of HRM is mostly at the good quality level, the average value of 57%, then at the poor level, the average value of 38%, and lastly at excellent average value of 4.92%. HR recruitment in the criminal police was rated the lowest (3.7: 52.4: 43.9). Compared to the quality assessment of crime police officers competence, HR quality management in the criminal division was rated significantly worse.

The above research shows that the biggest problems of the human resources of the Serbian police is the lack of systematic, strategic and modern HRM, as well as the existence of a strong political influence on all of the key activities of HRM functions. This has produced a disproportionate increase in staff at the Ministry of Interior, the increased costs of the state budget and increase of the number of criminal offenses committed by police officers. State of crime has not improved either statistically or in the eyes of the public, and citizens believe that the police of the Republic of Serbia is still the dominant instrument of the Government and the political parties, and not a public service. All of the abovementioned should be sufficient reasons, and strategic basis for the reform of the HRM function in the Ministry of Interior.

## ***FUNCTIONS AND KEY ACTIVITIES OF HRM***

### ***THE CURRENT STATE OF AFFAIRS AT THE MINISTRY OF INTERIOR OF REPUBLIC OF SERBIA***

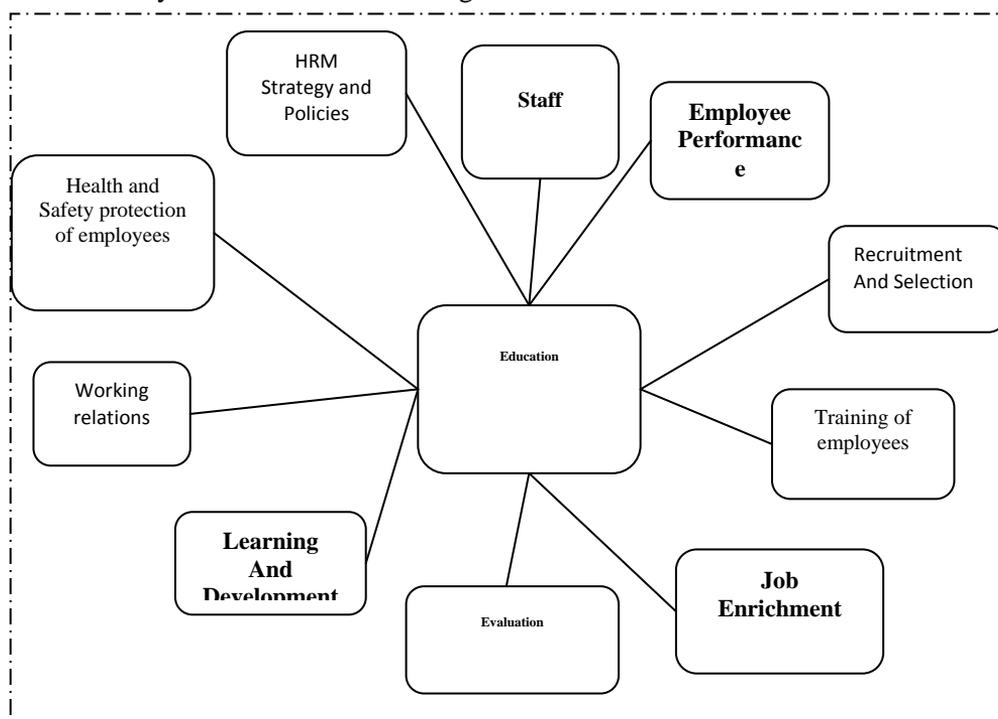
The HRM function is made up of a range of activities, policies, practices and systems that influence the behavior, attitudes and performance of employees in the organization (Bogicevic-Milekic, 2011, pp.5). A developed model of HRM includes a variety of programs, such as quality management, team building programs, measurement and management of organizational climate and culture, organizational performance management, etc. The current state of HRM in the Ministry of Interior of Republic of Serbia is characterized by numerous and various deficiencies and significant deviations from the modern standard or best practice HRM (Cezemier et al., 2012, pp.3-20). Firstly, HRM is much more bureaucratic administering to the employees than it has been a developed strategic managerial function. Management for HR, as the holder of the HRM function, does not possess the necessary authority for bringing decisions in the field of HRM. Recruitment is carried out without open competition and is strictly centralized, the deployment and promotion to managerial and other positions is done without transparent criteria and procedures. HR is not recognized as the potential of the organization which can provide a significant contribution to the way in which the Ministry is being managed in terms of labor costs and effective working practices. The key HR activities are generally either not executed at all, or not executed properly - there is no evidence that the best practices of HR support the MoI and its departments in achieving goals. Duties and tasks are delegated through a number of organizational units of the MoI, which leads to the unnecessary duplication and separation, where problems with coordination and information arise and lead to unnecessarily high number of employees, and similar.

The disunity of HRM affairs prevents a unique and systematic approach to people management at the level of the Ministry of Interior. Operating procedures in the field of HRM are not formalized and transparent. Many important tasks are not performed: HR planning, analysis and design of work, career management, performance management, etc. The lack of harmonization of regulations and inconsistent treatment result in a large number of lawsuits for violating the rights of employees. HRM processes in the MoI are slow, inconsistent and expensive. The management system is centralized, which in practice translates into an enormous written and verbal daily correspondence. There is the largest number of written acts on the assignment, transfer and promotion - which all must be signed by the Minister, but before that there are a lot of other parties that must give their consent, which significantly slows down the procedure. Employees are largely uninformed about HRM (surveys conducted in May 2013 by the Ministry of Interior and DCAF on a sample of 2,400 employees), which indicates that the system is not transparent. There is no a united approach to HRM in the MoI, ie. the HRM

function is disunited: Directorate for HRM collaborates with 27 police departments (PDs), which deal with similar tasks in the local police stations. Also, the management of HR in the MoI does not provide the necessary technical support to the direct managers.

### ***THE PROJECTION OF A MODERN SYSTEM OF HRM IN THE MOI OF THE REPUBLIC OF SERBIA***

A modern HRM system would primarily require a new unit for HR, which would be positioned at the strategic level. Also, a modern HRM system would consist of key activities as shown in figure 1.



*Figure 1: Projection of the key activities of the HRM function in the Ministry of Interior of Republic of Serbia*

*Source: promotional material of the DCAF project "The introduction of modern concept of HRM in the MoI", under the title: "Reforms"*

A more comprehensive scheme of the HR management function, so-called integrated HRM system, provided by Dr Gert Ahrer is shown in figure 2.

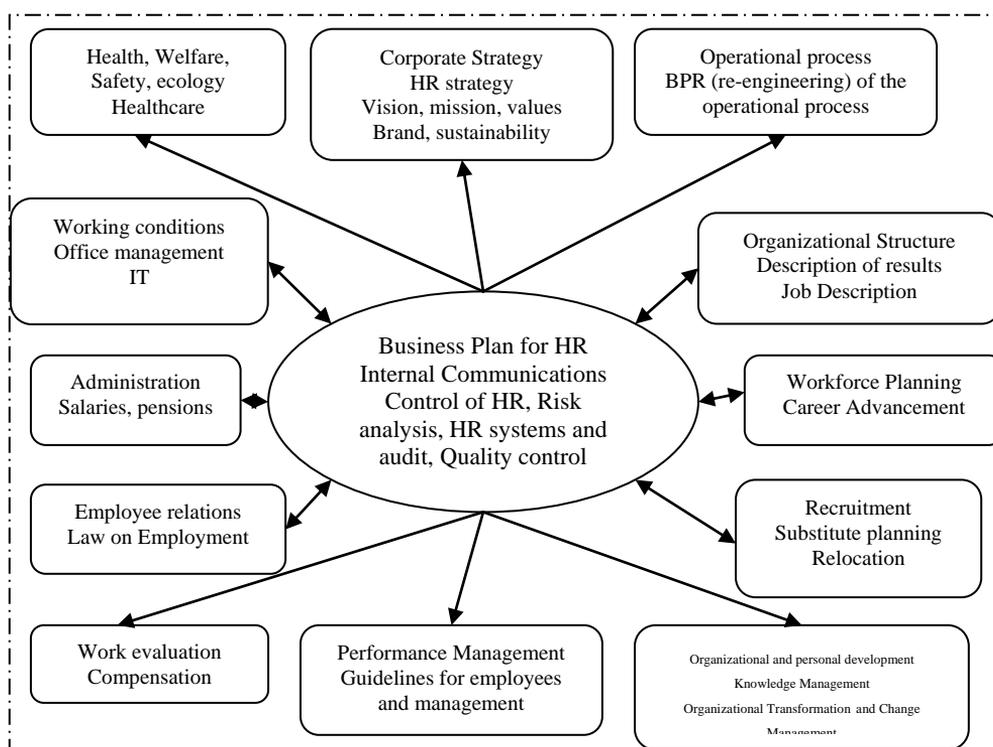


Figure 2: The integrated human resources management system

Source: Ahrer, G., pp.16

For achieving the broadly set activities of the integrated HRM as shown in picture 2, it is necessary to precisely define the key (sub) function units for HRM within the police organization, such as (Swanson, et al., 2008, p. 387-388):

1. Preparation of political statements, including the suggestions of HR strategies; also the standards of operational work relating to all areas of HRM, as well as issues for decision making by the executive managers of the police organization.

2. Maintenance of performance evaluation system (performance at work, the characteristics of the employees and the organization).

3. Creating an integrated information management system that includes all the necessary information about the employees.

4. Maintenance of program effectiveness for the purpose of recruitment of qualified candidates.

5. Management of carefully thought-out selection process.

6. Establishing and maintenance of criteria for the promotion of employees at various levels of the organization, together with a method for determining the necessary qualifications of employees visible for each position.

7. The implementation of the program for the development of employees, from entry into service to the highest positions in the police organization.

8. Developing and managing classification positions in the police organization.

9. Developing a plan of appropriate compensations, taking into account the different levels of complexity and responsibility for assigned tasks.

10. Presenting the police organization during negotiations with groups which seek employment in the police, and in other meetings related to HRM issues.

11. Conducting the exit interviews with police officers who leave the service, in order to identify and adequately correct the unsatisfactory conditions.

12. Providing advice to managers at all levels related to the problem of HR, paying particular attention to management and issues about the disciplinary procedure.

13. Implementation of the HR issues research program.

14. Presenting the police HRM unit to the Service of Human Resource Management in the Government of the Republic of Serbia, trade unions and other agencies and bodies dealing with HR issues.

For the purposes of this paper, we will include the first six activities of HRM functions shown in picture 1 – from the HRM strategies and policies to the development of employees and the organization.

## ***STRATEGIES AND POLICIES OF HRM***

HRM strategy is an action plan that includes both: the means and objectives. The objectives of HR may, for example, include the quality of performance, quantity of employees and an estimated cost of those goals. On the other hand, the means may include, for example, HR practices and HR policies (Brewster, according to Porter, et al. 2006, p. 382). HR management strategy should be well planned and implementable use of human resources in order to meet the objectives of the Ministry of Interior at all organizational levels. As a functional strategy, it should be an integral part of the development strategy of the Ministry. This means that HRM strategy must be focused on the key dimensions of employee quality, such as competence, ethics, character, behavior and enthusiasm. The strategic focus must be on the role of the police to the community, on the right of employees to fair competition in the professional development and advancement to senior positions, employee satisfaction with the various aspects of their work, and the fact that the quality of employees significantly affects the quality of organizational processes and their products, and particularly the effectiveness, efficiency and economy of operations. HRM strategy and policies provide the framework for all HRM functions and give them the desired development direction.

## ***ANALYSIS AND JOB DESIGN***

Job analysis is the process of collecting and evaluating relevant information related to the job: the content and nature of work, the required knowledge, abilities, skills and other requirements for the job (Schuler to Bogičević Milekić., 2011 pp 35). The analysis is focused on two groups of data. The first relates to the contents, characteristics and performance of a particular job, and the other to the required employee competencies at specific work position for the successful performance of the job. Under competence we mean the knowledge, skills and behavior, and often certain work experience is required as well. The result of the job analysis is the job description. Job description is a document that contains the purpose of the job, job tasks, duties and responsibilities, performance targets and reporting responsibilities. It contains details on the conditions, compensation and working hours. It represents the basis for the preparation of qualifications of candidates.

The conditions for a quality job analysis of each position separately in the organization, are process and functional analysis of the scope and jurisdiction of organization. The process and functional analysis are the framework for the description and design of each position. There are no records that at the Ministry of Interior of Republic of Serbia any process analysis has been conducted up to date, therefore this organization was able to irrationally and enormously increase the number of positions and employees in the last 20 years. What contributed to this state was the insufficient use of information technology and software (integrated database of human resources, training, crime, etc.), which allows the rationalization of employment, improvement of HR management, increase of the effectiveness, efficiency and economy of operations, etc.

The results of job analysis serve as a basis for other HRM activities: recruitment and selection, training, evaluating and rewarding employees, performance management. The qualitative analysis of work requires a special methodological approach, methods and tools for collecting, processing and interpretation of data (interviews, observations, questionnaires, content analysis, etc.). This means that people who are engaged to carry out the job analysis should have the necessary methodological skills. The best solution for quality analysis and job description is to engage an external expert who will work together with managers and executors at the specific workplace, and conduct this analysis at all levels of the police organization. Another solution is to train the managers for that job and for conducting job analysis following the clear, consistent, and complete instructions.

## ***HR PLANNING***

HR planning is the process where HR needs are predicted based on the anticipated changes in the internal and external environment. More specifically, work staff planning is making plans to fill the future vacancies in the organization, which is based on the prediction of vacancies and deciding whether those jobs will be filled by candidates who are already working in the organization or candidates outside the organization (Dessler, 2007, pp. 71). HR planning in the police of the Republic of Serbia, which would be based on predicting the need for staff, offering both internal and external candidates, has not been performed for the last 20 years. There is no annual plan for HR based on needs analysis. The reasons for this can be found in the impact of politics on employment and career system in the Ministry of Interior, the high centralization of decision-making on the recruitment and deployment of candidates, the absence of the list of qualifications of employees and others. It could be said that the only exception to this is the admission of candidates to the basic police training, which is defined by the Law on Police and the defined standards, criteria and procedures for the admission of candidates. One of the problems in HR planning is the outdated Act on working positions systematization in the police. Namely, the number of police officers, envisaged by the Act on systematization at the local level (police stations) has not significantly changed for the last twenty years, however the changing determinants on the basis of which this number is determined have changed, such as the number of inhabitants and the security issues (type and frequency of security problems, criminal acts primarily). Ministry of Interior, as all large organizations, should have a HR plan, especially for achieving the following objectives:

- Attracting and retaining the required number of quality staff (Vujić, 1008, p. 126). Namely, Ministry of Interior provides opportunities for high specialization of a part of its staff in different areas (forensics, information technology, cybercrime, analytics, etc.); however, there are no defined instruments how to keep the staff, in which they invested significant funds, in the situations when other agencies offer a much higher salary.
- Solving problems of staff surpluses or shortages. Rationalization of staff number is not possible without a clear and consistent methodological staff plan.
- Maximum utilization of employees' potentials, including the retired police officers, in a variety of necessary activities, etc.

## ***RECRUITMENT AND SELECTION OF CANDIDATES***

Recruitment of candidates is the process of attracting qualified candidates in such numbers that the organization will be able to choose the best for filling vacancies. Selection of candidates is the process of selecting among the applicants for the job and making the decision on hiring.

Organization may seek candidates internally, among the employees who desire promotion or transfer; or externally, at the labor market. Most organizations use a combination of internal and external candidates - promotion within the organization if there are qualified employees, and external recruitment when they are in need of new skills. Internal recruitment is particularly important in order to develop careers within the organization. In this way, organizations can retain valuable and effective employees by providing them with the opportunity of career advancement.

A number of selection techniques can be used, and they should be chosen depending on the vacancy to be filled. The techniques are designed to reveal the characteristics, skills and qualities of an individual for a specific job. The use of reliable and proven techniques will help lead to the correct decision and the appointment of a suitable candidate. Selection techniques include biographical information, interviews, psychometric test, assessment centers, checking references, test tasks, etc. (DCAF, 2014, pp.6).

Biographical information is information that can be objectively categorized, such as, for example, qualifications, years of relevant experience, positions of responsibility. Each category has its specific weight for the final score, so that each candidate gets a certain number of points based on biographical data. Interviews are conducted at various stages of employee's career, and represent a useful method for obtaining information and getting to know the person. The interview should ensure fairness and consistency, should be planned in advance, be well structured, and conducted by persons trained for that. The information obtained during the interview should be considered along with other sources of information so as to obtain a more complete picture of the respondents. There are different types of interviews, such as: the face-to-face interview, panel interview, structured interview, interview about expertise, focused interview, interview about behavior in a given situation, situation interview, and so on. The discussion should be conducted by people specially prepared and trained to avoid bad evaluation of candidates based on faulty perceptions, prejudice and other negative effects that may occur during the interviewing. Psychological test represents a wide range of tests that assess mental ability, behavioral preferences and attitudes/values. The tests are result-oriented, they include points that can be used to compare candidates one to another, or to a certain standard. It is necessary that they are conducted and interpreted by a psychologist. They can be divided into two types: (1) cognitive test / which measures the mental abilities of the person, such as IQ, spatial resourcefulness; awareness, reasoning, logic, arithmetic; (2) personality test / which evaluates the attitudes, values and beliefs. The collected responses constitute the candidate profile which could be compared with the profile that is considered appropriate for the job.

In addition to the developed selection for basic police training, there is a selection of candidates who are already employed to work in specialized units such as the Special Antiterrorist Unit (SAU) and the Gendarmerie (certain types of selection training). For deployment at the managerial functions there is no systematic selection. The promotion of police officers to police managers in the Ministry of Interior of Republic of Serbia, unfortunately, is not conducted on the basis of testing, i.e. verification of capabilities and aptitude for leadership and management. The biggest problem in the selection of candidates for police work is that there is no such test that will have all the necessary filters based on which the latent problems in the ethical dimension of the personality would be identified.

In modern time, for the purposes of selection of candidates/applicants, the so-called in-basket method is used: it is a candidate selection technique where the problems and/or challenges that await them at work are presented, and includes discussion groups without a leader. In-basket method is a test used by companies and governments in the recruitment and promotion of employees. In this test, applicants receive a variety of messages, phone calls, documents and notes. They have limited time to set priorities and to properly organize and respond to messages and phone calls. After the test, or exercise, applicants can justify their decisions during an interview with the assessors. In the discussion group without a leader applicants meet as a group to discuss a business problem within a given deadline. During the meeting, the behavior of the candidates, their mode of interaction, and the leadership and communication skills they exhibit are observed. The leader of the group usually stands out during a discussion. From the patrol officers in the 21st century it is required that, in addition to their usual duties to submit reports, they should also be managers who solve problems (Leonard, et al 1974, p. 522).

The quality recruitment and selection process is very expensive for the police organization. However, as it provides the highest quality professionals for the future, who create real value for the organization, it is also a cost-effective process in the long-term. Only the quality employees in the police can create a positive image of themselves in the public and the world, and provide the values of the organization.

## ***TRAINING OF EMPLOYEES***

Training is a process through which employees systematically acquire and improve the skills and abilities that are needed in order to achieve better work performance (Greenberg et al. 1998, p. 64). Training at any level represents a new skill and also socializes employees into their new work roles (Thibault, et al., 2007, p. 362). Unlike education, which is aimed at wider cognitive concepts, the training is focused on the job description of the specific position, the competencies that are required for successful job performance from that description, as well as solving specific work problems and achieving the desired effect. Today's experts increasingly use the phrase "learning and work performance" instead of the term

‘training’, to highlight the two main objectives of training – employees’ teaching and organizational performance (Dessler, 2007, p. 152). If the recruitment and selection are focused on filling vacancies with candidates with the best predispositions for work in the police, then the training is focused on the creation of quality employees. If candidates are not carefully selected with the corresponding potential for the performance of their job duties, then the proper training and proper management is a very expensive solution to the problem (Iannone, 2001, p. 62). The effective operational police force depends on the area of the qualifications of each police officer. The conscientious police managers know that the quality of police services is not solely in the function of numbers. Modern HR management is focused on intelligence, ability and skills that are at disposal to the organization in terms of its operations and the realization of plans (Leonard et al., 1974, p. 520).

The current management training process in the Ministry of Interior in Republic of Serbia is characterized by a disconnection with the HR management function. Specifically, the completed trainings of police officers in most cases have no significance for the development of their careers. Directorate for Police Education, Training, Professional Development and Science (hereinafter: the Directorate for Education) is in the hierarchy of the Ministry of Interior positioned quite low - it belongs to the Sector of Finance, HR and joint affairs, so it does not have sufficient authority to coordinate, control and promote the comprehensive training system in the MoI. Therefore, managing the training process is not functionally or organizationally set to be part of an overall strategy for HRM. Within the ongoing twinning project, as one of its key results the binding of Directorate for Human Resources and the Directorate for Education in an organizational unit – Sector for Human Resources, which will have significantly higher organizational position (next to the minister) and sufficient authority for the exercise of its jurisdiction.

## ***ORGANIZATIONAL AND PERSONAL DEVELOPMENT***

Employee development should be an ongoing process of acquiring and developing formal and non-formal education (courses, seminars, etc.), work experience and interpersonal relationships. It also includes an assessment of personality, skills and work performance. The basic objective of development is to enable the employee to acquire specific skills which are required for high-quality performance in the near future, whether it is horizontal or vertical career advancement. The development within the Ministry of Interior of Republic of Serbia is not based on a systematic approach. In fact, there is no planning for the development of employees as individuals. Moreover, some police executives are reluctant to further develop employees because they fear this way they will become competent (Iannone, 2001, p. 25).

Employee development system includes the career system. Career is a set of positions that an individual holds during work in a particular profession, from the date of his employment until retirement. A new employee of the MoI today has no clear picture of the possibilities of his/her career development, with no one to inform and guide him/her. The career system is not transparent, it is politicized, and many managers are not allowed to get the best candidates, because in fact there are no candidates. Usually there is only "one candidate".

Law on Police defines a dual career system for employees in the Ministry of Interior - for police officers with the status of authorized police officials to firefighters and other employees. Law on Police should define a career system for police officers only. Other employees should be included in the system of promotion of civil servants in the Republic of Serbia. Career advancement of police officers is solely based on the acquired level of formal education and years of service. The system of career advancement of police officers should, in addition to the above, also include the necessary training and development programs for the acquisition of higher-level ranks, as well as annual performance assessment. By implementing internal open competitions for advancement to higher ranks, competition would be introduced and the quality of candidates who advance to higher positions would be improved.

### ***THE CHALLENGES OF THE REFORM OF HRM FUNCTION IN THE SERBIAN POLICE***

The strategic challenges of HRM in Serbian police are the result of many piled problems in this function, and the need for the establishment of a modern HRM model in the economic, political, technological and legal context of the national and international level. The basic characteristics of Serbian society are: underdeveloped economy, high unemployment rate, large brain drain of the young and talented people, underdeveloped private sector, too large and bureaucratic and politicized public sector, etc. The request of the public sector is to modernize of the public sector in Serbia, within which a very important place has the modernization of the HRM function. Reducing employees' costs and improvement of performance (Dessler, 2007, p. 8) will be one of the most important and difficult challenges of reform of the HRM function in the police of Republic of Serbia. The strategic management of MoI of Serbia has decided that within the reform of the HRM function, the process of introducing Investors in People (IIP) standards should be started, which once is established, will solve numerous challenges and problems in this function.

Investors In People - the international standard, originally from the UK, is the first and the only framework for business improvement that focuses on people. IIP standard can be further defined as a quality system for HR development that shows commitment to excellence through employees; a tool that connects the goals and aspirations of the organization for individual performance and development; framework for the change management, defining the role of HR management,

performance improvement and organizational development; the international symbol of quality in the development of human resources, etc. (Oakley, H 2012, pp presentation). No other quality framework (Six Sigma, ISO 9001: 2000, EFQM, Kaizen Blitz, etc.) has such a long tradition (21 years), the trust gained worldwide, and the effect achieved (it is used in over 20,000 organizations in the GB). In addition to Great Britain, with a license, IIP standard has been applied in 10 other countries of the European Union (The Netherlands, Sweden, Austria, Belgium, Bulgaria, Cyprus, Finland, Greece, Hungary and Romania), and in twenty countries in Europe, Africa, Asia and America. Some recent research (CBI survey of education and training, 2008, Cranfield School of Management, 2010) show that IIP standard improves managerial skills - knowledge, experience and skills; supports the development of organizational learning culture, improves the effectiveness of management development, encouraging the creation of high-performance environment and increases manager performance. Also, research shows that the IIP standard is particularly useful framework for business environments facing with significant or rapid changes.

The basic idea of the IIP standard is to improve work performance by inciting all employees, which are characterized by effort without direction, to work together to achieve better results faster. IIP standard is based on three basic principles (analogous to the Deming cycle): planning, which includes the development of strategies to improve the organization's performance; application, which involves taking actions aimed at improving the organization's performance, and auditing, which involves the evaluation of the impact of the organization's performance. IIP standard has ten thematic sections or criteria (indicators) of the HRM quality and performance, based on the IIP standard and 39 evidentiary requirements. The criteria are: business strategy, learning and development strategy, people management strategy, leadership and management strategy, management effectiveness, recognition and rewards, involvement and empowerment, learning and development, performance measurement and continuous improvement. IIP standard criteria have been defined on the basis of best practice of the most effective companies and government bodies in Europe.

Some studies that have investigated the relationship between work performance, on the one hand, and the policies and HR practices on the other hand, show that certain policies and HR practices can have a positive impact on business performance (Management Journal, June 1995, str.635-672 according to Coulter, 2010, p. 179). The introduction of IIP standard in the HRM practice in the Serbian police will bring many benefits, especially showing the quality management system and public system to taxpayers and beneficiaries, as well as to the Government, donors and partners. The principal risks of introducing IIP standard in the Serbian police will be the opposing of the underdeveloped HRM systems, performance and processes accentuated by political influence, and organizational culture characterized by the lack of readiness for large and serious developmental changes. Therefore, it can be expected that the introduction of the IIP standard in police of the Republic of Serbia will be a very long and functionally non-linear process.

## ***CONCLUSION***

The initiated reform of HRM function in the Ministry of Interior of the Republic of Serbia is linked to a number of factors that influence its success. The most influential among them is the political factor, i.e. the will of the Government of Serbia and the key people in the MoI, who are now taking the test of democratic maturity. It is clear that without their support the real reform is not possible. Also, a very influential factor is the management of the Ministry of Interior of all levels, that are responsible to transfer the strategic vision of the development of the HRM function throughout the organization. A very important factor for the reform is the organizational culture, i.e. the awareness and attitudes of all employees of the necessity of development changes in the field of human resources. It is quite certain that a number of employees does not agree to the changes and seek to retain the existing system that promotes political suitability and other non-professional connections when it comes to employment and career advancement in the police.

In the process of the reform of the HR management in the police of the Republic of Serbia, it is necessary to use the positive experiences and models of HRM in developed countries of the European Union. In this regard, the reform projects in HR that are supported by the European Commission, financially and professionally, should assist the HRM function in the Ministry of Interior of Republic of Serbia to develop implementing the activities which now do not exist at all or are poorly developed. It is realistic to expect that the establishment of all HRM activities will contribute to achieving the key objectives of the reform of public administration in the Ministry of Internal Affairs, as follows: professionalization, decriminalization, depoliticizing, decentralization and rationalization, which are the key dimensions of contemporary public sector organization and the quality of its management.

To reform the functions of HRM as planned and with the anticipated activities and results, the Ministry of Interior of Republic of Serbia must seriously and systemically approach to change management, using the 'step by step' principle, or 'the switch' principle in situations where it is necessary.

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***III PART.  
CASE STUDIES***





## **INNOVATIVE GLOBAL COMPANIES – SOME CASE STUDIES**

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### **ABSTRACT**

*The world economy is becoming increasingly global and the magnitude of the globalization trend is so large that it is creating complexities for the managers and leaders of the organizations. Globalization brings both benefits and challenges for the organizations and striking a right balance between the two is critical for the organizations to succeed in the global marketplace. This paper aims to study and discuss the significance of globalization for organizations. The study is aimed at the complexities of the global environment and the competitiveness of the organizations. The paper elaborates the types of global organizations, followed by the role of managers and leaders in managing global organizations. The study also includes the role of the international business environment in the context of the global strategy of companies. Finally, an attempt has been made to study the importance of managing a culturally diverse workforce in a global organization. The method of study is primarily a literature survey and the websites of some of the organizations. The study proves the point that globalization is inevitable in the present economic scenario. Hence, companies that can adapt faster to this trend of globalization by adopting suitable management techniques will have a competitive advantage. The organizations need to strike a right balance between the challenges and the benefits of globalization and the four basic areas for striking the right balance are cost, strategy, people and risk.*

**Key words:** *Globalization, Global Strategy, Cultural Diversity, International Business Environment.*

**JEL Classification:** *F60, F23*

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## ***INTRODUCTION***

The globalization process involves the establishing of social, technological and political links among countries all over the world (E-commerce corporate infrastructure program, 2002). As a result of the integration of international economies, the last two decades have seen an unprecedented surge in globalization trends across industries and nations. And along with globalization, come significant opportunities and threats in the external environment to which the organizations have to respond. Globalization can be understood as a process which removes physical, political, economic and cultural barriers between different regions in the world, thus encouraging an exchange of goods, services, money and professionals between nations. As these exchanges grow, businesses become more and more integrated and interdependent (E-commerce corporate infrastructure program, 2002). Global companies can be defined as those that have a significant proportion of their sales, assets or employees outside their home markets although they are definitely not homogeneous. Globalization offers both benefits and challenges for the organizations (The Yearbook of International Organizations, (1978). Advancements in communications, technology and transportation have truly made the world a unified global field and have contributed significantly to the globalization process. The product development life cycles are growing shorter and communications are becoming instantaneous and thus, products can be manufactured and sold anywhere in the world (Fenton, Pettigrew, 2000). The employees within the organizations can be from anywhere in the world, since global organizations have offices in different locations and regions. Managing global companies poses many opportunities and challenges for the managers and the leadership of the company. For example, at the macro level, it could be property ownership arrangements, availability of resources and components, the role of government in business, as well as behavioral and cultural differences among nations and differences within the nations. Values, symbols, beliefs, and work cultures vary sharply between countries (Robbins, Coulter, 2012).

Managing these global organizations requires a fine balance of costs, strategy, people and risks. Globalization has become such an important factor in the survival and competitiveness of the organizations that those who do not think globally could get left behind.

## ***TYPES OF GLOBAL ORGANIZATIONS***

Companies conducting their business at international locations have been there for a while. For example, DuPont conducted business in China as far back as 1863 and the Ford Motor Company established its first overseas sales office in France in 1908. However, the concept and popularity of multinational corporations grew only after the mid-1960s (Griffin, Moorhead, 2011). Global organizations are conventionally

classified into three broad categories: inter-governmental organizations, international non-governmental organizations and multinational organizations.

1. The Inter-Governmental Organizations (IGOs) are based on formal agreements between the governments of nation states and consist of a permanent secretariat to perform their tasks (the Yearbook of International Organizations (1978)).

2. An International Non-Governmental Organization (INGO) is any international organization which is not established by inter-governmental agreement. These organizations may accept members designated by government authorities, provided that their membership does not interfere with the free expression of views of the organization (the Yearbook of International Organizations (1978)).

3. A Multi National Corporation (MNC) is a broad term used to identify any international company which has operations in multiple countries. Multinational companies have extensive experience in a number of international markets and have established marketing, manufacturing, and research and development facilities in many countries. A substantial portion of their revenues come from sales outside their home country.

4. Global Companies such as Royal Dutch/Shell, Unilever, Proctor and Gamble and Philips operate in a truly global manner and the entire world is their marketplace. These are also called Transnational Corporations and they maintain operations in several countries, while their management is decentralized into local countries. The management of such companies is based on interdependence rather than either full divisional independence or total dependence of their units in several countries on headquarters for decision-making and control.

5. Borderless Organizations are firms that have eliminated structural divisions that impose artificial geographic barriers and are organized along business lines (Robbins, Coulter, 2012).

### ***INNOVATIVE STRATEGY OF GLOBAL FIRMS BASED ON PROJECT MANAGEMENT***

“Changes in today’s business environment have been caused by globalization, increasingly stricter demands of the end buyers, tendencies towards reducing the shelf life of a product, the dependence of a company on business partners, as well as the focus of companies on key components” (Jovanović, Vasiljević, 2008).

Small and medium sized companies in the USA and Europe have spread their global holdings and restructured themselves in the aim of increasing their competitiveness on global markets. The globalization of the world market, rapid technological progress and the application of developed technology have led to the fact that many companies understood that the conditions for surviving on the market are contained within the ability of a quick adapting to variable conditions in the environment. Competitive advantage is the aim of every company and the

majority of them have become aware of the fact that today the mere satisfying of buyers' needs is not enough to be competitive, but rather along with this they have to exceed the expectations of the buyers, as this is the only way to persuade the buyers that the company is the best of all (Vujičić, Vukadinović, 2011). The majority of companies mostly use the innovative project management strategy, which via efficient planning and coordination can help a firm use its resources and the available time in a much more productive way.

Namely, in today's highly competitive environment, project management is used with all types of professional service organizations. Namely, a sure way to achieve success, whether this involves legal and lawyer services, consulting, accounting services, civil or other services, is to think and act outside the traditional framework. This implies using new knowledge in the application of the best practical experience, as well as the experience of other organizations which are involved with the same or similar services. The development of contemporary technologies, especially the Internet on one side, and changes in management practice, communication and the organization of work in companies on the other side, have led in the last years to changes in regards to knowledge type and acquiring method (Radovic et al., 2012). The new way of acquiring knowledge combines formal and informal learning with practical experience. Raising awareness, training and qualifying employees is a key factor in market competitiveness (Radovic et al., 2012).

In this way, managers can more efficiently manage projects, respond more quickly to the pressure of clients to implement new technologies, etc. The ability to learn more quickly than the competition can be the only sustainable competitive advantage in today's business environment. Individuals must constantly improve their knowledge and build themselves up as individuals who are bearers of the organization's abilities – after all, a successful organization is a group of successful individuals (Stanisavljev et al., 2011).

Except for this, there have been several suggestions to engage project managers on the side, that is, from other firms which are involved with other activities. In other words, it is considered that someone working in an accounting firm can better view the work in a lawyer's office, and launch the necessary innovations in its work. Also, it is recommended that firms overcome and gradually leave the traditional organizational methodology. Many firms have thus turned to project management and have realized admirable results. It should be stressed that project management is not only used in service activities, but also in many industries.

One of the managers of the famous consulting firm Bearing Point considers that he has found the formula of success of project management. It is made up of the following:

- An adequate business strategy
- Coordination between resources, teams, activities and stages
- Good communication between team members, as well as the consumers
- Careful planning and control via detailed planning

- A set structure for each project, including the description of their management and decision-making method
- A constant educating of project team members
- Ensuring that all team members understand the project aims, their tasks and way of realization.

Along with the mentioned conditions which are to be met by the project founded firm in order for it to succeed, it should be stressed that there is a degree of risk of possible failure. Primarily, considering the fact that project organized firms function in very uncertain environments, they need to be constantly formed, with the teams changing as well as the members working on the project.

Most of these project teams work virtually, considering they are not in the same place nor do they meet at the same time in order to deliver the project, but they work constantly networked and linked with different types of IT (Radovic Markovic, 2007a). In order for the virtual organization to succeed, it must meet conditions such as high technology, mutual trust, an endeavor to satisfy the buyers as much as possible as well as a striving for excellence. The most important feature of a virtual organization is its interdependence by certain members (persons or organizations) from the network, although they mostly cooperate between themselves.

The links between individuals in national firms are very close but they are also linked with international global services. In their research for innovation projects, Filippov and Mooi (2010) stress the significance of exploring the relations between innovativeness and project management. In that sense, very often an innovation project is equated with the development of a new product.

## ***GLOBALIZATION AND ORGANIZATIONAL CULTURE DIVERSITY***

Globalization has transformed organizations, societies, economics and politics all over the world. For global organizations, the definition of global diversity has become broader. Global diversity must encompass not only an understanding of the differences between different countries, but also the internal diversity of each country. The scope of diversity has become truly global and knowledge about each country's customers, employees and suppliers has become essential. Thus, global organizations need to move quickly towards the better management of a culturally diverse workforce. This movement towards better management has to be adopted by organizations due to three main reasons, as illustrated with some real examples. Some companies like Xerox were obliged to develop better management of a workforce made more diverse by affirmative action. Other companies like Hewlett-Packard grew very rapidly and then they realized that they had to work with multicultural constituencies. A third type of company like Avon Products needed to have a diverse workforce in order to match the diversity in the marketplace (Robbins, Coulter, 2012).

All these three kinds of companies had to work towards managing their diverse multicultural workforce better in order to gain a competitive advantage in the six dimensions of cost, resource acquisition, creativity, marketing and problem solving and system flexibility (Griffin, Moorhead, 2011). Thus, a culturally diverse workforce must be valued and managed well by all organizations in order to remain competitive in the present global scenario.

The workforce is becoming more diverse; hence, the companies that value and integrate diversity among employees will reap the benefits of globalization. Lower personnel costs and improved quality of the workforce are two obvious benefits for these organizations. In addition, a diverse workforce leads to diverse perspectives in problem solving, decision making, creativity, product development and marketing activities which are essential for creating a competitive advantage in an increasingly global marketplace.

Globalization has led to a growth of multicultural organizations which are characterized by six features, namely, pluralism, full structured integration, integration of informal networks, absence of prejudice, equal identification with goals and minimal intergroup conflict (Griffin, Moorhead, 2011). The table below depicts the characteristics and tools for creating a multicultural organization:

*Table 1: Creating a Culturally Diverse Organization*

Characteristics	Tools
Pluralism	Training and orientation programs
Full Structural Integration	Education, training, affirmative action, performance appraisal and rewards systems, benefits, work schedules
Integration of Informal Networks	Mentoring, social events, support groups
Absence of Prejudice	Bias-reduction training, focus, task forces
Equal Identification with Goals	Encourage participation of all employees from the diverse workforce in formulating goals, strategies and mission
Minimal Intergroup Conflict	Conflict reduction training, survey feedback

*Source: Adapted from Taylor H. Cox Jr. "The Multicultural Organization", Academy of Management Executive, August 1991.*

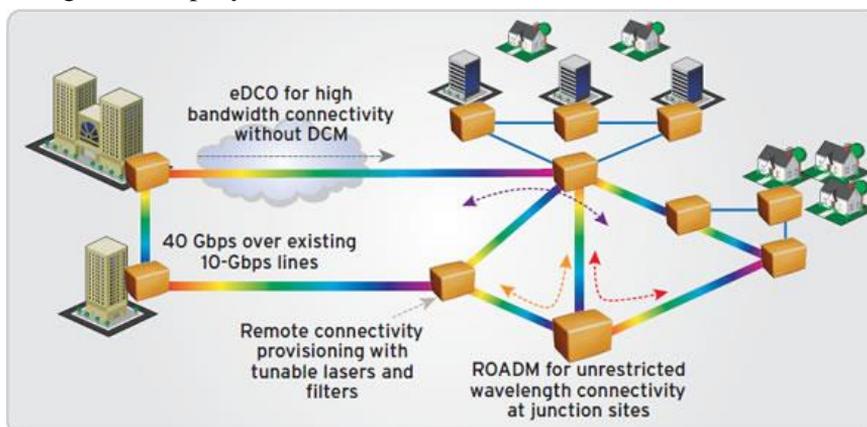
Global organizations are essentially multicultural organizations in which employees from different backgrounds, ethnicities, experiences and cultures can contribute and achieve their fullest potential, benefitting themselves as well as the organization. Developing a multicultural organization is a very important step in managing a diverse workforce in a global organization, and it is crucial for sustaining a competitive advantage in the global marketplace.

## ***EXAMPLES OF GOOD PRACTICES***

### ***NORTEL NETWORKS***

Nortel Networks is a global firm founded as far back as 1973, and today it is one of the largest world telecommunication providers, employing nine hundred people, 200 of which are engineers (E-commerce corporate infrastructure program, 2002).

When Nortel Networks started its work, the CEO came to the idea of introducing new standards into the company, managing projects which are orientated towards consumers. Considering this firm has a wide range of products, each project is independent and relates to a special product which is offered to the market. However, with time, consumers started to take an interest not only in certain products, but in the complete production range offered by the firm. In such circumstances, the general manager made the decision to establish consistent standards of project management for the organization. Thus, project management included all processes-deliveries, product installment, product testing, consumer training, etc. From 1999, this firm also started to carry out restructuring, that is, from an organization which is based on products it grew into an organization geographically based in six regions - America, Canada, Latin America, Brazil, Asia-Pacific and EMEA (Europe, the Middle East and Africa). In each region, the firm founded its representing offices and appointed directors, defining their responsibility for project management marketing. In fact, management teams worked with regional representatives according to standard management projects from all over the world. Regional managers formed the managing body, which voted on bringing all standard decisions. In the majority of cases, voting was carried out in secrecy and it was anonymous. Thereby, the managing body was the key for the firm to become a global company.



*Figure 1: Nortel Adaptive All Optical Intelligent Network*

Source: <http://www.networkworld.com/community/node/44588>

With global logistics, Nortel Networks has installed standardized automatic project management tools, integrated with Oracle database. Along with securing the standard tools, the global team also standardizes practice, combining it with the best regional experiences. The website of the firm lists the best experiences, divided into two categories:

1. A list with the tested experiences of the firm
2. A list with suggestions made by employees and associates

Considering that the list with suggestions is made public, the members of the management body vote for proposals. The best proposals are on the first list, while the others are erased or eliminated. In this way, the best ideas and experiences are stimulated, and individuals working on their own are not encouraged. Namely, only those ideas and practices which have the support of the majority are accepted. Twice a year, the firm presents awards, one for progress in implementing the global process, and the other for the best results in practice.

The firm also carries out training of project managers all over the world, while Nortel Networks organizes three types of training (Radovic Markovic, 2007):

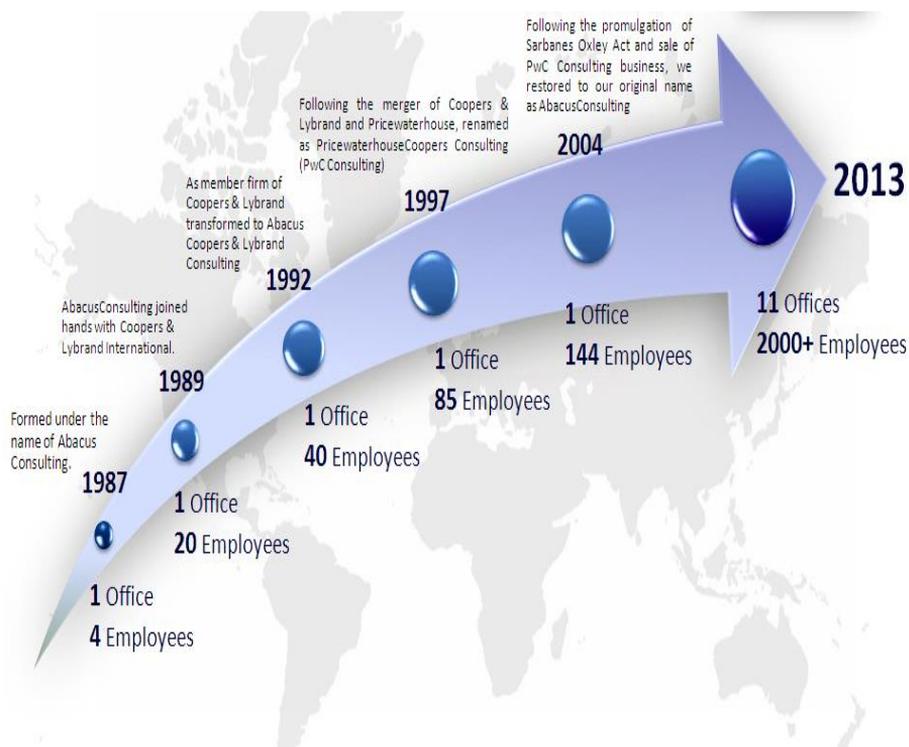
- First the managing body members visit the region and carry out training, organizing most often Walk-the-Wall classes. They create a network diagram or Gantt chart and set it up on the wall, in order to show to all those present the differences between planned and current processes, and then they determine what should be done to eliminate the differences (Radovic Markovic, 2007a).
- Second, the firm makes contracts with external associates for securing training and a large number of classes, which offers them enough knowledge about project management.
- The managing body provides the CDs which contain information which pertain to the new process, procedures, and tools.

This is just one aspect of the global dimension of project management from the organizational perspective. The experiences of Nortel Networks can serve as a guide on how to carry out successful implementing of global project management.

## ***COOPERS & LYBRAND***

Along with the mentioned example, we will also use research by Fenton and Pettigrew (2000), which tested the work of Coopers & Lybrand Consulting, which renders services from pharmaceuticals on a global level. At the time when this research was conducted, Coopers & Lybrand employed 70,000 people from all over the world (30,000 from Europe) in more than 140 countries (Radovic Markovic, 2007a).

At the beginning of 1989, this firm integrated with partner firms and this is how Cooper & Lybrand Europe came about, joined by Abacus Consulting in 1992. From its founding, this consulting firm increased the number of employees from 4 in 1987 to more than 2,000 in 2013 (Figure 2).



*Figure 2: Development consulting firm - AbacusConsulting, 1987-2013.*

*Source: <http://www.abacus-global.com/?q=about/abacusconsulting>*

The merging of these two consulting firms was carried out primarily in the purpose of rendering consulting services in Pakistan.

Along with merging and linking with AbacusConsulting, Coopers & Lybrand integrated the network of partner firms in 16 European countries. In this way, it created a virtual company without a center which would exert control, with two representing offices in London and Brussels. Also, some 74,000 people provide consulting services in 142 countries all over the world (PR Newswire, 1997).

Strategic decisions are brought globally, and it is significant to say that each network member can from time to time be included in one or more project teams. Thus, Richmond Groups is a perfect example of cooperation with individuals, whose expert services are used by this company. This cooperation is carried out on a global level through a great degree of integration of all the associates, during which they do not lose their independence and identity. This firm, with its cooperation with individuals and small firms endeavors to support and upgrade the interests of all the team members and function according to the principle of linking all the members regardless of their activity.

However, there is another side of the story, when individuals join the multinational project team and leave the country in order to manage the project in

another part of the world. On that occasion, they face certain difficulties, considering that it is not easy to build up relations, understand others and be understood by others properly in an unknown culture and environment. It is equally difficult when project team members speak different languages, when there are ethnic, national and regional differences.

## ***BENETTON***

The case of Benetton is a good example of the application of an innovative strategy and an innovative global company in the traditional sector.

Benetton was founded in 1965 in Ponzano, Italy, as a small company with 60 employees. Five years after its founding, intense development and the expansion of the firm started. In 1970 the firm employed 912 employees, and in 1985 some 1,446 employees. From 1970, Benetton was orientated towards exporting, a company which in the 1970-1985 period increased its placement on foreign markets from 5.3% in 1970 to 59.9% in 1985.

Today, Benetton products can be found in 124 countries and in around 6,300 stores all over the world, of which 95% are franchises.

The beginning of the rise of Benetton is linked with a specific franchising system which this firm applies in the textile industry. Through franchising Benetton imposed solid conditions of control, as salesmen of Benetton products cannot sell any products but those of Benetton in the stores. In this way, along with its products, Benetton has also exported its organization and marketing strategy.

The access to foreign markets and an export orientation put this firm in the situation to compete with other global competitors such as Gap and Zara for survival and further development.

The success of Benetton was enabled by numerous innovations which were realized in the following areas: products, processes and organization. In the 70s, Benetton based its competitive advantage on using light colors and conforming to the taste of young people. Furthermore, Benetton's strategy is global and famous all over the world for its brands:

1. United Colors of Benetton - UCB is the brand name which Benetton used at its beginning.
2. Sisley – this company participates in the total Benetton sale with 19%. Sisley is promoted as a high quality, high-priced product.
3. Playlife – Playlife was created to produce sportswear for the age group 20 to 40 years of age.
4. Killer Loop – a brand aimed at young buyers aged 14 to 27 and consists of urban clothing and sportswear.

In 1964, Benetton, in order to satisfy the taste of buyers, transferred from traditional to new processes, so instead of producing clothes in colors it started to

make clothes in natural fabrics and then, based on market information, marketed the trend. This was contrary to traditional production but this is how Benetton used the Just in Time (hereinafter: JIT) production strategy and in this way reduced the production time, increased efficiency and led to technological improvement. The most important innovations in the clothing industry relate to production flexibility, an accelerated goods turnover and the invested capital. A direct link from Benetton's headquarters in northern Italy with other Benetton branches all over the world was enabled by computer. The EPOS system (the electronic point-of-sale system) helped follow the trends of demand and realize the supply according to the JIT system. The profit was thus quite large and represented a unique marker of process management in the conditions of the globalization and internationalization of business.

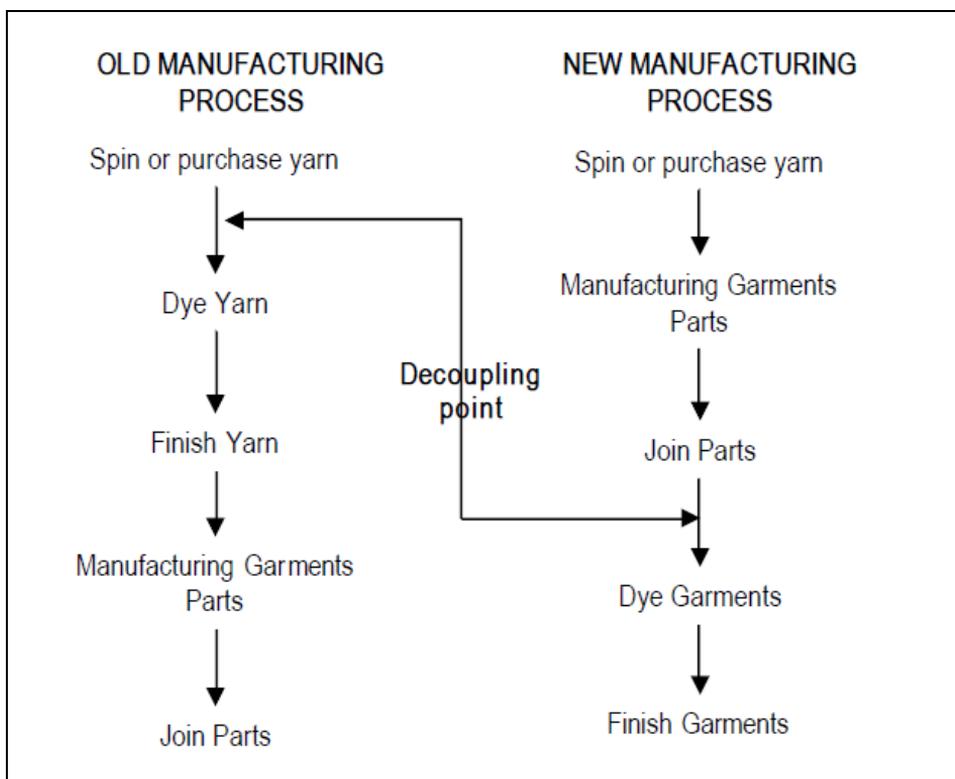


Figure 3: Postponement application in Benetton

Source: Yang, Burns, 2003

It can be said for Benetton that it grew through strategies of vertical and horizontal integration. At the end of the 70s, Benetton's organization could be defined as "quasi-vertical integration" (Blois 1972) as the company controlled the entire value chain, even if various activities were not organized through an exclusive hierarchical control. The main advantages of a vertical integration from

the aspect of the company are mostly better control and an optimizing of operational costs. If the company wishes to stay in step with the times, it must continuously invest into new technologies and system development. A common feature of all fashion companies is their vertical integration. They differ according to degree and integration direction (Figure 4).

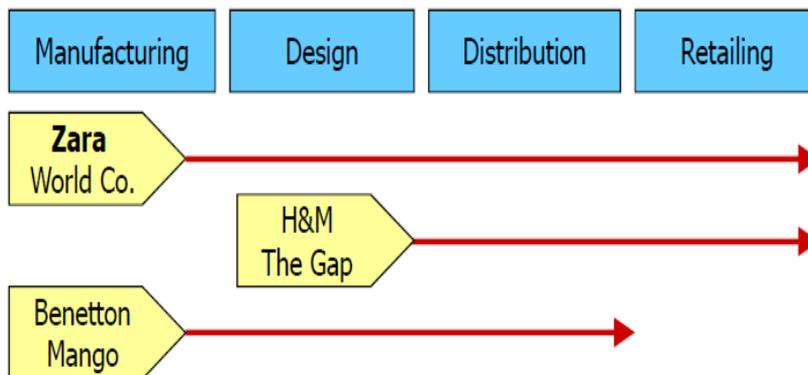


Figure 4: A presentation of different degrees of the vertical integration of fashion companies

Source: F. Caro, *The Fast-Fashion Business Model*, 2008.

Benetton also established a process of horizontal integration. The strategy of the total look was completed with the introduction of products such as shoes, spectacles, perfumes, watches and, most recently, jewelry. The Benetton strategy is global and communication and advertising are a significant area for innovations in the Benetton system. In its advertising strategy in the aim of stimulating consumers to think they will be happy by buying company products, Benetton managed to attract the attention of the public and single itself out among the other fashion companies. In 2012, with the UNHATE campaign, Benetton invited the unemployed aged from 18 to 30 to send their projects and participate in the innovations competition. The best 100 projects were awarded with 5,000 Euros which shows the interest of this company for innovativeness and creativity.

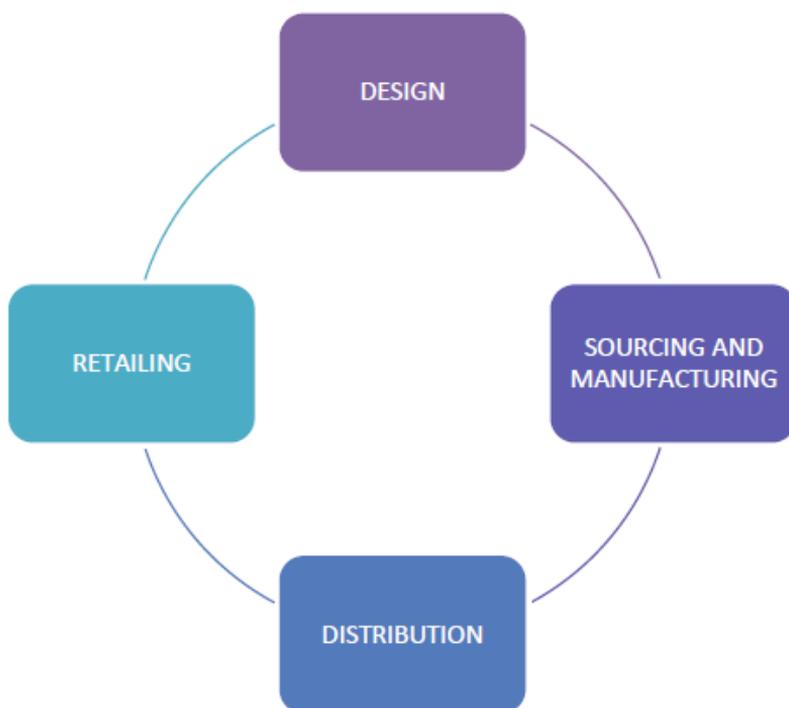
It can be said for Benetton that it is one of the most successful companies in the world, to a large extent thanks to a sophisticated IT system which it innovates every 10 years.

## ZARA

Zara is the leading store chain in Inditex, owned by Spaniard Amancio Ortega. The first Zara shop was opened in 1975 so that today Inditex is one of the fastest growing retail world companies. This company with the Zara brand has managed to enter the market with quality brands and very reasonable prices.

The strategy applied by Zara on the international market is a combination between a generic strategy of cost leadership and a strategy of differentiation. From the very beginning, Zara has invested in opening new stores all over the world, and Zara's business model has the features of vertical integration which is very high in comparison with the models developed by other international companies. Zara's business model enables the satisfying of the needs of the buyers as the key of this model is in adapting to the wishes of the buyers in as short a time as possible. Vertical integration enables shortening processing time and achieving high flexibility, reducing supplies to a minimum and reducing risks.

The figure shows Zara's business model which it uses to adapt to changes which occur during the season, reacting to them by sending the products to the stores as quickly as possible and in this way managing to retain its position on the market.



*Figure 5: Zara's business model*

*Source: <http://cmuscm.blogspot.com/2013/02/design-and-forecasting-case-of-zara.html>*

## **CONCLUSION**

The concept of global organization is definitely not new; it has a long history dating back to the 10<sup>th</sup> century Venetian trading empire. But in recent years, the importance of being global has increased tremendously. It is largely driven by the emerging markets and facilitated by the advancements in communication technology.

The increasing trend of globalization is evident by the fact that companies are becoming global earlier in their lifecycles. In line with this, while organizations like Sony and Honda took more than 15 years to become global organizations, AbacusConsulting became a global company in only 5 years. The global companies are no way homogeneous; rather they belong to one of the five archetypes, namely, resource seekers like the mining and oil & gas companies, researchers like pharmaceuticals or some high tech companies, the global offers like the luxury goods manufacturers that offer the same product worldwide, the customizers that make customized products for the local markets and the networkers such as airlines or logistics companies. Essentially, the true value of being global lies in the fact that global organizations are able to strike the right balance between the challenges and the benefits of globalization and the four basic areas for striking the right balance are cost, strategy, people and risk. Striking the right balance can be difficult, but there lies the importance of management and the role of managers and leaders in the organization.

Benetton and Zara are the best examples of global firms which have in an efficient and effective way combined a production and commercial strategy with technological innovations. Such an approach has enabled them a high competitiveness and a strong position on the global market.

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## **PROFESSIONAL EDUCATION AND YOUTH EMPOWERMENT THROUGH ENTREPRENEURSHIP FOR SOCIO-ECONOMIC DEVELOPMENT IN NIGERIA**

Isaac Elijah Esema, PhD<sup>43</sup>

Sasa Stefanovic<sup>44</sup>

### **ABSTRACT**

*Nigeria as a nation is a potentially great economy, which has always lingered on the fringes of economic prosperity. However, swift steps need to be taken to save the ship of state from hitting the rocks due to widespread corruption, insincere leadership and an industrious people disillusioned by abject poverty; occasioned by clueless managers of the polity and the economy. Something positive needs to happen to alleviate the worrisome trend of economic depression pervading the land and retarding the well-being and progress of the people - or the gaseous atmosphere of unease, which is a direct consequence of the people's economic hardship explodes into a conflagration worse than the inferno of terror and crime plaguing many parts of the country today! Without doubt, it is the obligation of any responsible and responsive government to devise practicable ways of providing the basic infrastructures necessary to ease the suffering of its much beleaguered people; especially uninterrupted power supply, potable water, motor able roads, a seamless telecommunications service, etc. Governments at all levels must dynamically and sincerely formulate policies which would engender economic development amongst grassroots people. This paper discusses the urgent need to empower the de facto leaders and futures of Nigeria - the youths - to become seasoned entrepreneurs, who would then develop Nigeria's socio-economic terrain. Entrepreneurship is a crucial force necessary for socio-economic growth in a developing country like Nigeria, which urgently needs to live up to her positive reputation as the Giant of Africa. Nigeria is unarguably the largest economy on the African continent as well as the most populous black nation in the world. The education of the nation's youths has to be purposely tailored towards professionalism in entrepreneurship in order to stimulate the social development process, and to ensure that Nigeria takes her rightful place in the comity of developed nations.*

**Key words:** Entrepreneurship, Entrepreneur, Professional, Education, SME, Innovation, Socio-economic, Economy, Development, Youth, Empowerment, TVET

**JEL Classification:** I25, L26, O10

**UDK:** 005.961:005.914.3-053.81(669)      374.3(669)

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## ***INTRODUCTION***

Entrepreneurship is the lifeblood of any nation's economy – whether developed or developing. This statement could be taken literally, as the people of any nation must be fecund in profitable enterprise in order to overcome the demons called deprivation, desperation and despair. Desperation and despair often give rise to social malaise such as armed robbery, hooliganism, cult-related activities, terror acts, kidnapping, ritual murder, arson, drug abuse, insanity, homicide, suicide, etc. Entrepreneurship starts with innovation – the birthing of new ideas which could result in the manufacturing of products or provision of services to meet existing market demands. When the social milieu is conducive, ordinary private citizens would be inspired to set up enterprises which would meet certain societal needs, while simultaneously putting money in their pockets. In this process, more job opportunities, dependable income and enduring wealth are generated. Consequently, unemployment and its resultant evil effects are significantly reduced.

Without entrepreneurship, economic growth and social development would be seriously retarded. Human capital is of utmost relevance in the production process in entrepreneurship. Nigeria is rich in human resources, who can be trained in areas pertaining to entrepreneurship and science/technology to wholly imbibe the entrepreneurial spirit.

Nigeria's educational system should be redesigned and reprogrammed to produce generations of young entrepreneurs who can positively change the economic landscape of Nigeria. Today, the world makes reference, with awe, to the Asian Tigers. Such nations like Malaysia, South Korea, Singapore, Hong Kong and other such swiftly developing nations in Asia have determinedly invested in their human capital over the decades. They have consistently and determinedly empowered their people, especially their youths through structured technical, vocational and entrepreneurial training for the sustainable development of their Fatherlands. Their level of development today is an incontrovertible proof that their investment in human capital is a right and commendable one. It is highly recommended that Nigeria should implement favourable policies, build infrastructures and encourage her people to acquire relevant entrepreneurial skills in order to achieve socio-economic development geared towards improving the people's standard of living.

## ***DEFINITION OF TERMS***

1. Professional Education: According to Wikipedia, in workplaces, Professional Development or education refers to the acquisition of skills and knowledge both for personal development and for career advancement. It is the knowledge that one needs to get ahead in one's career or business, improve one's management skills or simply pursue learning for its own sake.

2. Youth Empowerment: Wikipedia further defines Youth Empowerment as an attitudinal, structural, and cultural process whereby young people gain the ability, authority, and agency to make decisions and implement change in their own lives and the lives of other people, including youths and adults. The United Nations identifies youths as individuals between the ages of 15 and 24, while the Federal Government of Nigeria defines them as all young persons of the ages 18-35 years. By this definition, the youths constitute some two-thirds of the country's population; making them the critical mass of the instruments of national development. As at 2011, the average youth unemployment rate was an appalling 46.5%. (Tunde Lemo, *This Day Live*, 2013).

3. Entrepreneurship: Whenever the concept of the "Entrepreneur" is mentioned, some clear images immediately come to mind: "someone with the Midas touch", "business czar", "business tycoon", "business mogul", "captain of industry", etc. Hence, some of the keywords that readily pertain to entrepreneurship are: Innovation, Creativity, New Ideas, Risk-taker, Enterprise, Doggedness, Disciplined, Inventor, Leader, Pioneer, Shrewd, Product, Service, Hands-on, Feasible, Calculated Risk, Can-do Attitude, Wealth Creation, etc. An entrepreneur is therefore a person who organizes and manages a business undertaking, assuming the risk for the sake of profit. An entrepreneur: Sees an opportunity. Makes a plan. Starts the business. Manages the business. Receives the profits. (U.S. Small Business Administration)

4. Small Scale Business: This is a business enterprise that requires relatively little capital investment, producing in small quantities and consequently controlling a small segment of the market share, employing not more than fifty workers – with management, marketing and other entrepreneurship functions vested in the proprietor.

Although in Nigeria, there is no clear cut definition of who an SME is, but according to the CBN, a Small and Medium Scale Enterprise is an enterprise that has an asset base (excluding land) of between N5 million –N500 million and labour force of between 11 and 300.

Another broader definition that can be found in the archives of the CBN (2005) defines industry in the following way:

- Micro/Cottage Industry

An industry with a labour size of not more than 10 workers, or total cost of not more than N1.50 million, including working capital but excluding cost of land.

- **Small-Scale Industry**  
An industry with a labour size of 11-100 workers or a total cost of not more than N50 million, including working capital but excluding cost of land.
- **Medium Scale Industry:**  
An industry with a labour size of between 101-300 workers or a total cost of over N50 million but not more than N200 million, including working capital but excluding cost of land.
- **Large Scale**  
An industry with a labour size of over 300 workers or a total cost of over N200 million, including working capital but excluding cost of land.

5. **Socio-economic Development:** Wikipedia defines Socio-economic development as the process of social and economic development in a society. It further explains that socio-economic development can be measured with indicators, such as Gross Domestic Product (GDP), life expectancy, literacy and levels of employment. Changes in less-tangible factors are also considered, such as personal dignity, freedom of association, personal safety and freedom from fear of physical harm, and the extent of participation in civil society. Causes of socio-economic impacts are, for example, new technologies, changes in laws, changes in the physical environment and ecological changes.

## ***LITERATURE REVIEW***

According to Peter Drucker (1984), a world-renowned management expert, as cited by Alawiye, (2004), the entrepreneur is the innovator who searches for change, responds to it and exploits it as an opportunity. It means creating something new, doing something different, rather than doing better what is already being done. An entrepreneur shifts resources from areas of low productivity and yield to areas of higher productivity and yield by creating a new market and a new customer.

Tijani-Alawiye, (2004) cited by P.U Akanwa et al defines entrepreneurship as the process of increasing the supply of entrepreneurs or adding to the stock of existing small, medium and big enterprises available to a country by creating and promoting many capable entrepreneurs who can successfully run innovative enterprises, nurture them to grow and sustain them, with a view to achieving broad socio-economic development goals. Binks and Vale, (1990) also cited by P.U. Akanwa et al, defines entrepreneurship as an unrehearsed combination of economic resources instigated by the uncertain prospect of temporary monopoly profit. Entrepreneur is also defined as the instigator of entrepreneurial events for so long as they occur.

Pinchot, a university based in Seattle explains in its website (<http://pinchot.edu/what-is-entrepreneurship>), that entrepreneurship is the willingness to take risks and develop, organize and manage a business venture in a

competitive global marketplace that is constantly evolving. Entrepreneurs are pioneers, innovators, leaders and inventors. They are at the forefront of technological and social movements – in their fields, in their forward thinking, in their desire to push the envelope. They are dreamers and most importantly – doers.

Furthermore, the Microsoft Encarta defines an entrepreneur as one who assumes the responsibility and the risk for a business operation with the expectation of making a profit. The entrepreneur generally decides on the product, acquires the facilities, and brings together the labour force, capital, and production materials. If the business succeeds, the entrepreneur reaps the reward of profits; if it fails, he or she takes the loss.

Again, [www.quickMBA.com](http://www.quickMBA.com) posits that the concept of entrepreneurship has a wide range of meanings. On the one extreme, an entrepreneur is a person of very high aptitude who pioneers change, possessing characteristics found in only a very small fraction of the population. On the other extreme of definitions, anyone who wants to work for him self or herself is considered to be an entrepreneur.

Therefore, one could safely put it across that entrepreneurship is a person's readiness to take calculated risks which propels him or her to develop, organise and manage and improve on a business enterprise within a competitive marketplace that is constantly evolving.

### ***THE IMPORTANCE OF ENTREPRENEURIAALLY-INCLINED YOUTHS IN NIGERIA'S SOCIO-ECONOMIC DEVELOPMENT***

Entrepreneurship is the bedrock of economic growth. No economy can truly grow and impact the people's lives without the input of the myriads of Small and Medium-scale Enterprises necessary to drive a healthy economy. Entrepreneurship does not only bring about economic growth, it also brings about social changes in the environment which make life better for the citizens. It is necessary for entrepreneurs to be focused, disciplined and highly professional in their activities in order to generate wealth and build sustainable organisations, thereby increasing the size and the reach of the market.

To be a professional entrepreneur means to be highly-skilled and disciplined in all the day-to-day activities which one does in driving one's enterprise towards profitability and continuous sustainable growth. It entails proficiency, efficiency and effectiveness; purposely geared towards the production of quality goods and delivery of impeccable services, while one continues to seek better ways of improving on whatever one does. Professionalism, like excellence is not a destination, but a journey.

Holcombe (1998) cites Kirzner (1973) who describes entrepreneurship as the process of acting upon a previously unnoticed profit opportunity. The connection between entrepreneurship and economic growth is that these previously unnoticed profit opportunities must come from somewhere, and the most common source of

profit opportunities is the insights of other entrepreneurs. Entrepreneurial ideas arise when an entrepreneur sees that the ideas developed by earlier entrepreneurs can be combined to produce a new process or output (Holcombe, 1998).

Apart from stimulating economic growth, entrepreneurship also initiates social changes in the society which make life and living more conducive for citizens. Getting involved in entrepreneurial exploits helps in wealth creation. It increases the size and the reach of the market. It also allows for specialization as entrepreneurs see and create niches through innovation. The increased entrepreneurship also creates jobs, infrastructures necessary for business development such as roads, transport, communication, power supply, education, health services and supply of various goods demanded in the market. All these enhance social development.

Tunde Lemo, the former Deputy Governor (Operations) of the Central Bank of Nigeria in his article titled Policy & Execution published in This Day Live online column, Development and the Entrepreneurial Challenge on January 11, 2013 argues that development has many dimensions. He posits that on balance, it is connected to improvements in human capacity, living standards and overall societal well-being. For a nation to attain development, its social, economic & political institutions must be in tandem with the Millennium Development Goals (MDGs). Within this framework, Nigeria is rated one of the developing countries with slow progress in education, gender equality, income equality, employment generation, wealth creation and poverty.

He further explains that the economic benefits of youth participation in development process are varied. Youth empowerment has multiplier effects on the national economy, including boosting productivity, wealth creation, consumption and tax revenue. The rate of development of a country depends largely on how productive and creative the youths are. Since youths constitute about 70% of Nigeria's population, the nation cannot achieve development when they are mostly idle and unproductive. This is the basis for their productive engagement in entrepreneurship.

## ***PROBLEMS OF YOUTH ENTREPRENEURSHIP IN NIGERIA***

As it is with most developing nations of the world, Nigeria is faced with so many challenges, capable of retarding the economic growth and prosperity of her people. Chief amongst these are: Poverty, Unemployment, Corruption, Visionless Leadership, Conflicts and Diseases.

The falling standard of education and persistent illiteracy is another problem limiting youth entrepreneurship. In Western Nigeria, about 90 percent of rural small-scale entrepreneurs had less than Primary VI education and 44 percent were virtually illiterate (Aluko, 1973 cited in Chuta 2012). Increasing the number of literate small entrepreneurs could facilitate the upgrading of their managerial

processes in general and could obviously facilitate improved record keeping (Chuta, 2012). Decision-making, sound management and accounting practices are very low among Nigerian SMEs operators (Aremu, Adeyemi, 2011).

Moreover, Okello-Obura and Matovu (2011) argue that the growth of an enterprise may depend - among other things - on the entrepreneurial spirit and qualifications of its owner and on the quality of Business Development Services (BDSs) it can access within the designed system. The term, Business Development Services (BDSs) refers to the provision of information, knowledge and skills - as well as advice on the various aspects of a business (Finnegan, 2000 cited in Okello-Obura, Matovu, 2011).

It is obvious from the foregoing that with the proper professional education, Nigerian potential and existing entrepreneurs would imbibe the right attitude and entrepreneurial spirit necessary to drive their business idea towards the creation of lasting wealth made possible by well-grounded business enterprises.

El Brown, an online blogger also gave further insight into some of the constraints of Entrepreneurship Education in Nigeria:

1. Poor knowledge-based economy and low spirit of competition;
2. Poor enterprising culture;
3. Lack of entrepreneurship teachers, materials and equipment;
4. Unavailability of funds;
5. Non-inclusion of entrepreneurship programme in the school curricula;
6. Poor societal attitude to Technical and Vocational Education development;
7. Inadequate facilities and equipment for teaching and learning;
8. Insensitivity of government to enterprise creation and expansion strategy;
9. Poor plan and execution of processes of action.

One major flaw of the Nigerian educational system, with special emphasis on university education, is that it is too theoretically-inclined. Nigerian universities produce people who are only suited for white-collar jobs and have little or no basic skills of any other vocational relevance. This has led to high rise in unemployment especially among university graduates (Ejere, Tende, 2012).

The BUSINESS DAY (Monday, 3 September, 2012) editorial column corroborates this by stating that:

The manufacturing sector is increasingly technology dependent, especially the multinationals. Unfortunately our training institutions have not revised their curricula to meet the rising demand for highly-skilled technical manpower to install, operate and maintain these new machines. There is a dearth of talent in the sector. This lack of technical talent mars Nigeria's economic growth story.

## ***HOW ENTREPRENEURSHIP CAN BE PROMOTED AMONG NIGERIAN YOUTHS***

The Organisation for Economic Cooperation & Development (OECD), cited by Tunde Lemo (2013) characterizes entrepreneurship as a motivating force for initiating business ideas, mobilising human, financial and physical resources for establishing and expanding enterprises and creating jobs. The organisation argues that given the Nigerian youth unemployment situation, entrepreneurship remains the viable option to create jobs and reduce poverty. Entrepreneurship empowers them to develop their businesses, pursue their dreams and contribute to overall productive capacity and national development.

Highlighted below are some of the ways in which entrepreneurship can be promoted amongst Nigerian youths:

1.Ensure that schools deliberately provide sector specific skills needed for the development of human capital, use professional and entrepreneurs as instructors and mentors.

2.Operation Catch Them Young. That is, the government should make it mandatory for schools to teach entrepreneurship and creativity at an early age.

3.Organize for curricular integration of education, entrepreneurship and community development.

4. Plan practical programmes to reorient and transform Nigerians.

Nigerian youths need to be transformed from laid-back, employment seeking graduates into confident, positively-aggressive, innovative, dogged and purposeful individuals. The ideal profile for emerging professionals (products of our ivory towers) with respect to entrepreneurial education, this would include a strong scientific, technical and factual base with good background information and research skills.

## ***EFFORTS BY GOVERNMENTS AND NGOS TO PROMOTE ECONOMIC GROWTH THROUGH ENTREPRENEURSHIP DEVELOPMENT***

Over the years, governments at every level in Nigeria and some local and international non- governmental organisations have made efforts to initiate programmes which would empower the people for entrepreneurial success, at the same time reducing the alarming increase in unemployment rate in the nation. Unfortunately, in Nigeria, such Government policies are often seen as being insincere in many instances or self-centred by the masses due to past experience with visionless leadership and pervasive corruption.

## ***THE NIGERIA VISION 20:2020 POLICY***

The Nigeria Vision 20:2020 policy was a goal set by the Nigerian Government during the Olusegun Obasanjo Administration (1999 – 2007) to place the country among the top 20 most developed economies in the world by the year 2020.

While the goal is commendable, the fact remains that basic infrastructure necessary for development must be put in place. Paramount amongst these are uninterrupted power supply, motorable roads, potable water, an efficient telecommunications network and a dependable security system to protect the lives, properties and investments of the people. Historically, Nigeria used to be a predominantly agrarian economy during the postcolonial times. However, she is now heavily dependent on the oil and gas industry as the mainstay of her economy. Efforts are now being made to diversify the economy by investing, for example, in agriculture and also creating a conducive environment for the manufacturing sector to thrive. The Government and people of Nigeria are gradually becoming aware that proceeds from the export of agricultural products could help increase the country's revenue.

However, in making these efforts, development strategies which are entrepreneurship-focused should be emphasised as these have proven successful in several developing countries. South Korea, Malaysia, Singapore, Hong Kong, Taiwan, China and India have taken entrepreneurship related strategies (SMEs) to fast-track their economic growth. Entrepreneurship is being seen as the key driver of not just economic development but also social advancement. Small and Medium-scale Enterprises (SMEs) in developed countries - especially USA, Canada and Europe are still being used successfully for economic growth.

### ***SMEDAN***

The Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) was established by the SMEDAN Act of 2003 to promote the development of micro, small and medium enterprises [MSME] sector of the Nigeria Economy. The Agency positions itself as a One-Stop Shop for MSME Development. Micro Enterprises are included in the clientele of the Agency since they form the bedrock for SME's.

## ***THE ILO-SIYB PROGRAMME***

About 24 years ago, an International Labour Organisation technical cooperation project in Fiji embarked on the development of a specially-designed and packaged programme for the training of potential and existing entrepreneurs (TOPEE) which is called the Start and Improve Your Business Programme (SIYB). This programme has three modules: Generate Your Business Idea (GYBI), Start Your Business (SYB) and Improve Your Business (IYB). Today, the SIYB Programme is recognized in more than 100 countries in Africa, Asia, Europe and South America as a successful ILO trademark. Many young potential and existing entrepreneurs who have participated in the programme have commended it for the simplicity of its language and the practicality of the programme, as evidenced by the entrepreneurial success recorded by participants in the training programme.

According to the International Labour Organisation website, <http://ilo.org/empent/areas/start-and-improve-your-business/>, the Start & Improve Your Business (SIYB) programme is a management-training programme with a focus on starting and improving small businesses as a strategy for creating more and better employment in developing economies and economies in transition.

With an estimated outreach of 4.5 million trainees, continuously growing network of more than 17000 trainers and 200 Master Trainers in 2500 partner institutions SIYB is one of the biggest global management training systems used for the support of micro and small enterprises (MSEs) currently on the market. Initially developed in the 1980s, it has now been translated into more than 40 languages and introduced in more than 100 countries.

With a consolidated step by step approach, the organisation's immediate objectives are:

- To enable local Business Development Service (BDS) providers to effectively and independently implement business start up and improvement training and related activities
- To enable potential and existing small entrepreneurs, both women and men, through these BDS organizations to start viable businesses, to increase the viability of existing enterprises, and to create quality employment for others in the process.

Potential and existing entrepreneurs who participate in such hands-on trainings provided for entrepreneurial development such as the ILO-SIYB Programme, Fate Foundation, etc can be certain of picking up practical skills needed to succeed in their business enterprise.

## ***CONCLUSION AND RECOMMENDATIONS***

As a nation, Nigeria is blessed with abundance of both natural and human resources. Nigeria has the potential to be great and indeed attain the Vision 20:2020. This would be possible if steps are taken to put the basic infrastructure necessary for economic development and social advancement to take place. As SMEs and entrepreneurship are seen to be the driving force behind growth and transformation, these should be encouraged through favourable investment environment and supportive government policies. Nigeria should also take deliberate steps to invest heavily in development of her human capital by increasing funding for education, Technical Vocational Education and Training (TVET) programmes, entrepreneurial training, and development in technological knowledge and skills in order for human capital to become an advantage for development as it has turned out to be for China and India.

In Nigeria, TVET should be encouraged and given due recognition because it is crucial to technological and sustainable development. It is an avenue to equip the youth with knowledge and skills for employability and productivity. TVET graduates should not be looked down upon. They should be remunerated appropriately.

There is need also to upgrade the programme to use modern equipment and ICT to meet the global modern practices in industry. Nigeria needs to take a cue from the Asian Tigers countries which invested heavily in TVET for human capital development between 1960 and 1990s. Taiwan built 80 vocational schools in 2 years and set a ratio of 1:1 vocational enrolment with secondary school enrolment. This ratio was later increased to 7:3 in favour of the vocational enrolment. In China where skilled labourers represent the backbone of her economic expansion, one third of all secondary students are enrolled in vocational schools (Adenipekun, 2007, Diallo, 2005 cited in Erwat, 2010). The Asian Tigers countries are also committed to fund and pay important attention to basic education. The school enrolment in 2007 in these countries was 86% and above while that of Nigeria was 63.4%; their gender parity index was 1.0 for all the countries while that of Nigeria was 0.82 (World Development Indicators, 2007, cited in Erwat, Fabunmi and Isah, 2009). The benefits of these investments in their human capital are now being seen in the rapid socio-economic development experienced in these countries.

Furthermore, to equip Nigerian youths, entrepreneurship courses should be included in the curricula of secondary schools, colleges of education, polytechnics and universities, not theoretical, but in a more practical way incorporating issues young entrepreneurs would encounter in business. Study modules could cover various aspects of business from opportunity identification, idea/plan development; fund sourcing, start-up and running/managing a business, record keeping, customer relations, marketing and so forth. For example, the Indian state of Gujarat established a Centre for Entrepreneurship Development (CED) 1979 and the programme consists of the following components: motivation development, project counselling and management orientation, project planning and confidence

development. In over 14 years of existence, the Gujarat CED has created over 8,000 new entrepreneurs (El-Namaki et al, 1987 cited in Ejere and Tende, 2012). Tertiary institutions as well as secondary schools should teach entrepreneurship skills as well as encourage entrepreneurship spirit among the students. Nigeria should harness her large population to human capital advantage for development just as Singapore, India and China have done.

Entrepreneurship development and encouragement of SMEs would see the country enjoy many benefits such as job creation, self-employment, skills and talents development, innovation, wealth creation, economic growth, economic stability and social advancement.

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# **FEMALE ENTREPRENEURSHIP AND THE WOMEN CHAMBER OF COMMERCE AND INDUSTRY: ECONOMIC EMANCIPATION AND CLOUT FOR PAKISTANI WOMEN**

*Iqbal Khan*<sup>45</sup>

## **ABSTRACT**

*Socio-economics, culture, religious entrepreneurship and taboos have massive impact on societies in South Asia. Pakistan is a Muslim society that has lived aside other cultures also driven by religion. Muslim characteristic is an identity and practical way of life. In defining the entrepreneurial portrait of Muslim female entrepreneur in Pakistan, it has to be borne in mind that culture plays the dominant role. There is so much of complexity in the culture of South Asia that Amartiya Sen raises the question “How much of this can a foreigner with no more than a cursory knowledge of the factors involved – feel and respond to”? And furthermore Roomi (2005) contends women face deep rooted discriminating cultural and social factors that hamper their growth. Yet the empowerment of women entrepreneurs in Pakistan has come about following the example of Prophet Muhammad’s (SAW) wife Khadija (RA). This contradiction in terms and this evolution among Muslim women is a subject of interest to researcher, such as what inhibits the growth of female entrepreneurs in a Muslim society like Pakistan?*

*There is constraint owing to limited literature on Muslim female entrepreneurs of South Asia. Qualitative methodology, in-depth interviews and case studies were adopted. The findings indicate that under the garb of religion, false philosophy is practiced. Women have discovered clout comes from having platform and hence the long down struggle to setup the Women Chamber of Commerce & Industry; this is the contribution of the paper.*

**Key words:** *South Asia Culture, Clout for Women, Women Chamber of Commerce & Industry, Cultural Influence on Muslim Female Entrepreneurs, Women Leadership Styles and Practices, Psychological Advocacy, Forum for Women*

**JEL Classification:** *L26, J15, J16*

**UDK:** *005.961:005.914.3-055.2(549.1)*

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## ***INTRODUCTION***

The research paper aims to explore what environment prevails to prevent or foster female entrepreneurship in Pakistan. It explores the role played by some prominent female entrepreneurs that resulted in creation of a forum in the economic environment of Pakistan. The selected entrepreneurs all belong to a similar status except their leaders. It discusses some entrepreneurial leadership characteristics of the Pakistani female entrepreneurs. This paper attempts to analyze women's emancipation and 'economic emancipation' of women. The question arises how can you define the characteristic of a female entrepreneur and leadership characteristics without understanding the culture and the impact of culture on a society. In South Asia, culture is all pervasive. Therefore does this aspect of culture, impacts entrepreneurial characteristics and entrepreneurial leadership aspects.

Culture is the most dominant influence in this region. So strong is the impact of culture that any minor deviation from the set pattern of life can spell disaster. A lot of culture revolves around women in South Asia. The culture in this region may be said to be female driven. Cultural practices lay barriers on a woman's marriage, her inheritance, her education, her independence, her emancipation, and her entrepreneurial inclinations. The classical 'caste system' practiced by the Hindus of South Asia is an extended form of culture. In the wake of the dominance of culture and 'caste system', among the Hindus we have seen 'sati' An Indian woman who burned herself on her husband's pyre: the custom of so doing is SATI Chamber's Twenty Century Dictionary, 1968, W & R Chambers Ltd. Edinburgh, we have seen women married to the Holy Book among the Muslim a practice whereby Muslim women are made to swear by the Holy Book that they forsake marriage. In this way men are able to hold their sisters, women's share of inheritance. This is a custom among some societies not to share inheritance of their sisters with anyone and keeping it within in the hold of men, circumventing their religious requirement and we have seen 'Karo Kari' (honor killing) prevailing in all the societies of this region. All these cultural practices show a complete hold on women by men, restricting their mobility inheritance, marriage and contact with males outside the families. These are customs that have come down for ages. Breaking these shackles would mean a heavy price to pay. Hence the paper lays the case of culture which is a barrier for the Muslims or other societies or the religions existing in the South Asian region. It has to be seen if some women have penetrated the culture barrier, if yes, then they are the proverbial 'Trojan Horse'. It should be understood that a significant influence of Hindu culture exists on the Muslims of this region and these practices hence are motivated culturally rather than religiously.

Cultural divide between the East and West is not easily understood. In this region under the garb of religion ill-fated customs are practiced and sometimes it becomes difficult to separate religious from cultural practices. Hence this paper has

presented the events in a cultural format showing where these are different from religious facts. Therefore the paper begins with the assumption that not enough research exist on the cultural and religious dimensions of female entrepreneurship among Muslim countries. It is planned to review literature pertaining to female entrepreneurs of South Asia. Their activities as entrepreneur are bound by cultural factors and the struggle is being analyzed, to see what they may have achieved.

The cultural status of women in Pakistan has been summed up by Roomi thus:

“The status of women in Pakistan is not homogenous because of the interconnection of gender with other forms of exclusion in the society. There is considerable diversity in the status of women across classes (the socio-economic status of a woman’s family), geographical regions, ethnic origin and the rural/urban divide due to uneven socioeconomic development and the impact of tribal, feudal, and capitalist social formations on women’s lives...”

This observation touches almost all those multifarious aspect that have stood as barriers and shackles for women in this region. A close examination of the culture of this region gives the realization that the entire culture revolves around the women of this region and these are almost 1.5 billion people. And among them Muslim community is bigger than the entire population of USA. The size alone commands the need for research of the women’s claim to entrepreneurship.

### ***RESEARCH QUESTIONS AND PROBLEM STATEMENT:***

The objective of this paper is to bring out the nature of the environment and the impact of customs, tradition, culture and religious entrepreneurship on the female entrepreneurs in Pakistan. And the study is driven by the research question.

- Given the cultural overcast, what entrepreneurial traits or characteristics or competencies can be indentified among the Pakistani female entrepreneurs, causes for gaining recognition and clout?
- Especially what entrepreneurial leadership characteristics are depicted through the case studies?
- What brought about the Women Chamber of Commerce and Industry in Pakistan, and did it create a platform and forum for the women?

Hence we will be looking into the cultural context, the religious context, the characteristics of the female entrepreneurs in Pakistan and through in-depth interviews and case studies of the main players building momentum through their leadership of the women in Pakistan.

## ***LITERATURE REVIEW***

For the purpose of this paper we will study literature that have bearing upon the objectives to look at culture, religion, female entrepreneurs and clout for women. Culture and environment, massively influence entrepreneurship phenomenon, though there are many dimensions of influences on women entrepreneurs. As reported by Global Entrepreneurship Monitor (GEM 2007) that even the most enabling environment for entrepreneurship, USA, indicates that the male entrepreneurial activities surpasses female entrepreneurial activity almost two to one. Kauffman Centre for Entrepreneurial Leadership compiled a report on obstacles facing women entrepreneurs and identified human, social and financial capital as major constraints (Guerrero, 2008). The Diana Project was and is the major push for research on female entrepreneurship. It brings in the Western societies female entrepreneurship out of the domain, of minority or marginalized society's entrepreneurship. It is considered an extra ordinary and high impact research. Prior to this female entrepreneurship was an under-researched field (Holmquist & Carter 2008). However irrespective of culture & environment, women are found to be less active as entrepreneurs then men (Minitti 2005)

Female Entrepreneurship Development Theories have therefore emerged primarily from research carried out in developed countries with specific social norms and values regarding women's participation in economic activities. The initiative to setup the Diana Project itself is an example of the way women in the West think and act to create an enabling environment for themselves. There is a dearth of studies conducted in different social contexts especially in Islamic societies. But what compound the issue is the cultural aspects of some societies. Women have not been seen to-gather together a rally for a cause as has been done in the West. It is unheard of as no literature exists.

Female entrepreneurship research domain grew in phases though a pioneering study as early as 1976. Schwartz notes that women were motivated by need to achieve or having economic necessity and desire to be independent. These motivating factors have prevailed in the West. But it was in the real sense in 1990s that female entrepreneurship became well established. The development in this domain is literature driven and a constant search for novel topics. But all of this does not apply to the South Asian women development (Holmquist & Carter 2008). These researchers have also stated that women generally are found to run smaller business compared to men as entrepreneurs. This disparity and imbalance is generally an accepted norm. Contemporary existing disparities that are universal on a global perspective are that a typical female entrepreneur is more educated than her male counterpart, but her professional experience often falls short and is usually outside the traditional business sector (Gurrero, 2008). It was also found that they seldom founded their business in sectors that had to do with their educational qualifications and it was observed that they had high need for achievement, were highly educated, had someone in the family as entrepreneur, have a strong support system from her spouse or family but having limited network of resources (Brush, Greene et al, 2001)

showing distinctive behavioral differences from male. “*Glass ceiling*” was one factor that drove most women to entrepreneurship. They are known to be steadfast to their business and customer satisfaction as compared to their male counterpart and these are the general characteristics of female entrepreneurs universally. This paradox is universal across all societies.

Iris Aaltio, Paula Kyro, and Elisabeth Sundin (2009) make this observation quoting Mills “The feminist researcher may be better served avoiding a search for cues that support a notion of progress over a period of three years progress, instead examining events to see what they tell us ...” Thus change is more important than progress. I concur with this observation because the experience of researching the women entrepreneurs in Pakistan, this researcher, also faced similar experience. Hence the evidence gathered was empirical and through in-depth interviews by repeated visits. The examination of events over a sufficient length of time (5 years) revealed the change in status rather than the progress overtime. The events typically went back and forth but the ultimate development was the establishment of a platform (PWCCI) Punjab Women Chamber of Commerce & Industry for the women entrepreneurs. As to the progressivity of the women entrepreneur it was minimal. Dr. Shehla the popularly chosen leader of these women entrepreneurs felt that there was still very low involvement of the members and a general apathy. The author of the paper suggests that Women Entrepreneurship be studied from multiple angles and especially one of them could be Self-Efficacy and Leadership. Information on the struggle for Women Chamber of Commerce & Industry is available on [www.reformsnetwork.org/women](http://www.reformsnetwork.org/women)

### ***THE FEMALE ENTREPRENEURSHIP LANDSCAPE ACROSS SOUTH ASIA***

Beginning from the perspective across the border in the neighborhood of Pakistan in India and Bangladesh the cultural tradition and situation has a number of similarities though there is a significant difference at the level of culture tradition and development. In “A reflection of the Indian Women in Entrepreneurial World” Kollen & Parikh (2005) trace the history of economic emancipation of the Indian female entrepreneurs from the era of the fifties to the 21st century. The women of the fifties would give up their education to support their families at the expense of their aspirations if there was no income generating males. There were also those who were landed with the family business in their lap in the event of loss of the male family member. The paper calls them ‘extremely courageous women’. In the sixties the educated females had started taking small steps to start their small enterprises. Whereas the women of the seventies were new radical women. They were those who had completed their education and were in the field to take professional assignments. They opened the new frontiers for women entrepreneurs. But they showed clear cut evidence of wanting homes, marriage and children as well as occupation, who accepted the restrictions of their

parents and grandparents but expected their husbands to give them understanding for their choice of occupation. By the eighties the women entrepreneurs of India were educated in highly sophisticated technologies and professional education. So many preferred degrees in engineering, medical field and bioengineering. But the choices of business were typically clinics, nursing, boutiques, garments, beauty parlors, schools and the like. Yet the society was hostile and environment was male dominant. The Nineties was a qualitative different era for women. They had two decades of role models and hence these become more assertive entrepreneurs. They had now acquired economic independence, high self esteem and could deal with situations single handedly. Whereas the 21st century's first decade is an era of telecom, IT and financial institutions. Many pioneered in these new ventures and the opportunities were alike for men and women and a melting pot for professionally trained and enterprising women.

The real change visible in the 21st century was somewhat different as the focus shifted to the elite class of women. Women have become aware of their existence, their rights and their work situation. However, women of the middle class are not too eager to alter role in fear of social backlash and this was reflected in other part of the region such as Pakistan. The progress is more visible among upper class families in urban India. "Society designs and defines roles for women", where as each country has its cultural, social, religions and political back ground, it in turn develops for the society its economic thrust trough industrialization resulting in new occupational roles for women. A parallel change in Pakistan is also visible as we see the emergence of the Women Chamber of Commerce lead by a couple of elite women in the Pakistan society. One can draw a parallel with the status of the women and in particular the female entrepreneurs in Pakistan though at a lower degree. The authors go on to say that despite the dilemma of being an entrepreneur the women maneuvered into this position out of a desire to be independent and do something meaningful and to have their own identity instead of remaining "closeted behind their husband's name plate". They also found that they were less concerned with making money and often choose entrepreneurship as result of career dissatisfaction. Indian female entrepreneurs were either house wives or fresh graduates with no experience. Generally ran traditional business like garments, beauty care and fashion designing which grow usually from hobby to serious business. The famous Indian examples of a successful female's entrepreneur are of Herbal Queen Lady Shehnaz Hussain who began from her kitchen and ended with an herbal empire and a chain of beauty parlors. And Sarabai, Mrinalimi set up dancing schools and later Malika expanded the 'Darpana Institute' as a household name in dancing (Kollen & Parikh 2005).

Sujal Kumar Maiti (2008) has given a profile of Bengali urban educated women entrepreneurs in Kolkata India. The paper focused on the women who were engaged in home delivery catering services in Salt Lake area Kolkata, West Bengal India. The paper has concluded that educated Bengali women are not shy to engage in the business ventures. They are ready to take risk for their economic freedom. They are quick to adopt to this business as a source of income and source of pleasure to utilize their leisure after having given adequate time for bringing up

their children and taking care of their families. The average age of these women was above 40 years. All 40 surveyed happen to be married and were above graduation qualification, and rarely did they have more than five years of professional experiences. But their education and independence to pursue a business gives them a status of being elite. This again explains the similarity of women entrepreneurs across the border in Pakistan. Afreen Haq and Abdul Moyeen (2008) have also drawn similar conclusion about Bangladesh women entrepreneurs. Bangladesh has witnessed a growing group of well educated urban based women who have shown potential for starting their own business as an economic option. This growing phenomenon has not been noticed much in developing countries but developed countries have witnessed a surge of literature and research on this subject of urban educated elite business women. This phenomenon has been referred to as “*the quietest revolution of our times*” by Afreen Haq and Abdul Moyeen (2009) with respect to Bangladesh. Such women have demonstrated that the key elementary factors that have brought about this phenomena are good formal education, work experience, socio economic status, networking, and type of business. In the past the main focus on research on women entrepreneurship has been on rural poor or urban poor. However it was observed that women have smaller network restricting their access to business support services. They are also handicapped by being unable to access business associations and government agencies. (Haq, Moyeen, 2008). This creates an awareness of the need and significant importance of women chamber of commerce.

### ***FEMALE ENTREPRENEURSHIP ENVIRONMENT IN PAKISTAN:***

To understand the Pakistani environment and to study the women entrepreneurs and their efforts, the findings of USAID survey gives a fairly good idea. Nabeel Goheer and Susan Penksa (2007), have made some observation about women in the Pakistan economic context? We quote the relevant text as the USAID report also signifies the socio-cultural context for studying female:

“It is imperative to understand the unique socio-cultural context of Pakistan before planning to “engender” economic growth. A characteristic feature of Pakistani society is its family orientation and an inside/outside (private/public) dichotomy of gender relations.

As can be observed almost all research touched and felt the sensitivity of the family orientation in the environment and the mobility aspect of the women. Roomi (2009) has also described this phenomenon.

Even while considering ‘engendered’ economic growth report recommends to understand socio-cultural context of Pakistan. Which varies from place to place even within a Province based on variation in language and ethnicity of the society?

“The intensity of this social feature may vary from urban to rural areas and from one province to the other but its flavor can be seen almost everywhere in Pakistani society”.

Roomi observe: -

The male members of the family are supposed to take care of the productive or more precisely, the remunerative aspect of public life while women work in private, “inside” their homes. They bear and rear children, maintain social relationships with the extended family and friends perform household work. The gendered division of work effectively prohibits women from participating productively (and remuneratively) in the economic growth of Pakistan”. (Roomi 2009)

The report goes on to emphasize the gendered division that prohibits women from economic activity outside the home. The concern ranges from security to reputation.

“Another important feature of Pakistani society is a cultural restriction on the mobility of women. This restriction is due to concerns for the safety and security of women who venture outside the home and fear that the family will lose “reputation” or “honor” due to illicit relationships in which females might become involved (either through consent or by force). Secondly, and related to the former problem, is the social stigma attached to women working outside the home”. (Roomi 2009)

Cultural restriction on mobility has safety, security, honor and stigma concerns but there are indication of change.

“A number of factors are altering these social norms but the pace of change still is incremental. Two potent forces of change are the spread of secular education for women and men and increasing economic pressures. Pakistani women - especially those from the middle class - are now emerging and participating in the productive sphere of life both as employees and as entrepreneurs but their ratio of participation, as compared to men, are still very small”. (Roomi 2009)

An incremental change is visible in the social norms but huge majority still labors under these cultural norms. Breaking away from these traditions are considered radical and courageous.

Another survey has brought out some converging observation examining recent development of women entrepreneurship in Asian developing countries. Tulus Tambunan (2008) has taken account of the entrepreneurship enabling environment among women entrepreneurs in South Asia. Some studies have shown that successful women entrepreneurs generally belong to rather well to-do families and live in nuclear family rather than extended families as it gives them freedom from social & cultural restrictions. As a part of the profile it was observed that female entrepreneurs are generally found in sole proprietorship, they also have a higher closure rate. But the motivation behind female entrepreneurship comes from the desire for economic emancipation because entrepreneurship ‘implies being in control of one’s life and activities’. The factors identified in this paper that hinder

& growth are psychological, social, cultural, religious, economic and educational factors depicting lower status of women in Pakistani society. The under estimation of women's economic contribution is confounded by factors that emerge from factors such as tribal, feudal culture and cultural practices in the name of religion; inadequate public transport and the notion of 'Pardah' & 'Izzat' as also pointed out by Roomi (2008).

### ***CULTURE: AN ALL PERVASIVE IMPACT ON FEMALE ENTREPRENEURS: EXPLAINING THE IMPACT OF CULTURE***

Generally there are two meanings of culture; in the narrow sense civilization (Art Science and Education). In the broad anthropological sense "A collective programming of the human mind". The Western society lives in the individualism mode but the Eastern society of South Asia lives the collectivism mode. People belong to in-group are supposed to be looked after by in-group. It is dangerous to be kicked out of your in-group. Loss of face has to be avoided. Face saving is important.

For the purpose of this paper and its objective a deeper look at the environment and culture of the region needs to be taken. This region has been the cradle of a typical culture for all the nations residing herein. Opinions are pre-determined by groups. Everyone has to fulfill obligation to and society and in-group. Otherwise face shame and penalties are sever.

Amartya Sen (2005) explains through the works of Satyajit Ray that the environment consists of indigenous 'factors such as habits of speech and behavior, deep seated social practices past traditions, present influences and "so on". He asks "How much of this can a foreigner with no more than a cursory knowledge of the factors involved – feel and respond to?" and goes on further to say "which can only puzzle and perturb – and consequently warp the judgment of – the uninitiated foreigner". In effect both these notable thinkers and keen participants of this society feel that the tendency to assume that there cannot be such big difference in the culture of the region with that of the Western society would be a fallacy.

Sen quotes a Singaporean Foreign Minister at a Human Right Conference in Vienna 1993, which further elaborate the Asian perspective of culture as opposed to Western perspective thus "universal recognition of the ideal of human rights can be harmful if universalism is used to deny or mask the reality of diversity".

In the "Argumentative Indian" Amartya Sen (2005) the winner of the Nobel Prize in Economic defining this region says "Cultural conservatism and separatism that has tended to grip India from time to time" has left an indelible mark and each society is an Island on its own. He also establishes Rabindarnath Tagore's pride in Indian culture by saying that "India's culture is not as fragile and in need of 'protection' from Western influence". Such is the impact of culture in this region. It is strengthened by the lack of education in this entire region, and Pakistan or

Bangladesh have not escaped the strong impact of culture. Each has its own flavor and doses of religious edicts by the ‘religious entrepreneurs’. And to use Amartya’s quote “Important as history is, reasoning has to go beyond the past” where then do we go from the influence of culture? Of course he is advocating opening up of culture of South Asia to the world. How do we deal with culture with such pervasive influence? And in speaking of Indian culture one takes it to a great extent to include the Pakistani Culture where of course there is also the expansion of religious sectarianism – and fueled by ‘religious entrepreneurship’ for vested interest. Even when it is not religious motivation, the garb of religion is quick to invoke severe punishment.

Henry Kissinger (2011) in his book “On China” explains the stark difference in the Eastern (Asian) Cultural thinking and Western Cultural thinking by giving an example. The Chinese philosopher Confucius was unlike Machiavelli. The Confucian philosopher is concerned with the cultivation of social harmony not with the accumulation of power and using power. Rather it was incumbent as a spiritual task to recreate proper order and recovery of forgotten principles of self-revelation (p.14). Harmony is the drawing force in the Asian culture. Furthermore Sun Tzu (Art of War) proclaims that not every problem has a solution and too much emphasis on total mastery over specific events upset universal harmony. Harmony has to be maintained. In contrast the Western traditions prefer decisive clash.

### ***THE SIGNIFICANCE OF ASSOCIATION AND CHAMBER OF COMMERCE IN BUILDING CLOUT FOR WOMEN ENTREPRENEURS: THE NEED FOR EXTERNAL SUPPORT SYSTEM.***

In a paper “Women Entrepreneurs in the Global Economy” Susanne E. Jalbert (2000) has examined how women entrepreneurs affect economy, why women start businesses, how women’s business associations promote entrepreneurs, and to what extent women contributed to international trade. She has also emphasized economic clout that women have built up and quotes Irene Natividad, Chairperson US National Commission on Working Women at the 15th Global Summit of Women “Global Markets and women are not often used in the same sentence, but increasingly statistic show that women have economic clout – most visibly as entrepreneurs and most powerfully as consumers”. She finds that women bring commitment and integrity because they care about economic empowerment. But according to her finding women entrepreneurs are dependent upon professional and personal support that is found in business associations. The paper goes on to say that women entrepreneurs look for role models and mentors that help them to carve out paths to follow. Citing Susan Caminiti the paper says that conventional mentoring role of women has changed. Women by nature are given to offering advise based upon years of experience they have gained. Mentors usually see mentoring as a responsibility. It’s a payoff for the gains of their life. Therefore

members of associations, consultants, and trainers are all acting as role models. This finding supports the findings of our paper and the role played by Dr. Shella with the role models discussed in Jalbert's paper and the Chamber of Commerce has taken on the role of association. She displays leadership and vision and mentoring ability as will be seen in the case studies. The economic empowerment of women, the clout, comes from being together on a platform that provides the support services discussed above. This platform is the associations or the Chamber of Commerce. Talking of support systems from within the family and society Rajani & Sardar (2008) state that enterprises started by women are influenced by the interest and influence of the relatives and family. Two contrasting cases have been analyzed in their paper. Once again the research within this region reveals that similar problems and difficulties are faced by female which revolve around culture, and tradition and way of life.

The external support system is of great significance in such environment. This does therefore brings out the significance of associations. Business women's associations in Malawi, Nepal, Brazil, Canada, Ireland, Mexico and UK all have provided psychological advocacy required to start small businesses. They create growth oriented atmosphere and vision for their members through wide spectrum of activities such as networking and political and economic empowerment of women. In many societies women's ability in accessing mainstream organizations is limited. By establishing and joining a Chamber of Commerce, one can demonstrate economic clout and force larger organizations and government to pay attention to their cause. Associations also provide a system of bonding because they share same problems & issues and the bond of being a business woman overrides the cultural differences. The paper most powerfully establishes the significance of Associations or the Chambers of Commerce as a platform. In other words Chambers of Commerce or associations provide a formidable clout to women and gives them economic emancipation. (Jalbert 2000)

The realization of the acquiring clout by being together in the Chamber of Commerce has played a significant role to overcome cultural barriers. We will see this in some of the interviews of Pakistan female entrepreneurs and in the case studies.

The conceptual understanding of female entrepreneurs, of their role in the family and then in the society weighs heavily on the women in Pakistan. The number of female entrepreneurs has increased. Hence there is a need for research that covers the area of female entrepreneurs and their efforts in a male dominant society like Pakistan. But the phenomenon is much the same in other societies as well as we see from the observation of Brush and Matlay

"... Despite the tremendous growth in the number of women-owned enterprises and their increasing aggregate impact on society and the economy, there are few studies researching women business owners in general" (Brush, 1992)

The observation made much later on by Matlay (2005) still paints a similar tone. But also refers to the difficulty in theory building aspect in female entrepreneurship.

“The dramatic rise in female entrepreneurship in contemporary Europe cannot be realistically or adequately investigated, let alone explained or theorized, as a new and isolated phenomenon. It is our contention that theory building in this as well as other aspects of entrepreneurship should be conceptualized in the wider body of knowledge. -----”.(Matlay, 2005)

Despite a growing enthusiasm among researchers, there has been a greater failure to build adequate theory around the concept of female entrepreneurs in Islamic societies. This vacuum is more pronounced in a wider socio-economic context because women business has a growing contribution to the economy. The challenge here is to understand what motivates female entrepreneurs in society as traditionally patriarchal and difficult for woman as Pakistan. The best we could make of this was from the series of interviews that were conducted on the 30 female entrepreneurs and we are in the process of analyzing and discussing their views. Not all have been reported but they all belong to a similar status in society and similar educational background. Except for their leadership which happens to be highly qualified and educated abroad also.

Female entrepreneurs in Pakistan are realizing their status and position in society. They have also improved their conditions in society to some extent. Roomi (2009) goes on to present the role of women entrepreneurs in a Muslim country like Pakistan.

“Two factors especially influence women’s occupational roles: the cultural norm of *pardah* (veil) and the notion of *Izzat* (honor) (Roomi and Parrott, 2008: 2). *Pardah* has significance as an instrument of sexual segregation and seclusion based on spatial boundaries, (Roomi, 2008) In the strict sense these are inclined to be socially and culturally oriented. The definition has to be more precise to demarcate the social & cultural from the religious requirements. ‘*Izzat*’ is the notion that women are repositories of a family’s honor, and that their chastity and good reputation, being highly valued, must be guarded.” (Shaheed, 1990) He further goes on to state “There is considerable diversity in the status of women across classes (the socio-economic status of a woman’s family), geographical regions, ethnic origin and the rural/urban divide due to uneven socioeconomic development and the impact of tribal, and feudal, social formations on women’s lives” (Roomi and Harrison 2008: 2).

While he has also hastened to support the conditions of openness for women in Pakistan by saying they are able to cross the barriers and participate in economic activities. But in his conclusion he has confirmed “that socio-cultural variables play an important role in the growth of women owned enterprises in Pakistan.” This statement establishes once again the inter connectivity of culture and business venturing of female entrepreneurs. In the true Islamic sense, religion has not forbidden business to women. A lot of confusion prevails with regards to social norms and cultural practices and religious biddings.

This doubt is put to rest as he says in his Practical Recommendations about the role of women in the Islamic context by quoting the Quran and Sunnah/ Hadith (sayings of the Holy Prophet Muhammad S.A.W.W.)

“The most important point to mention is that there is nothing in the Qur’an or in the Hadith which prevents women from working outside the home. In fact the Qur’an extols the leadership of Bilqis, the Queen of Sheba for her capacity to fulfill the requirements of the office, for her political skills, the purity of her faith and her independent judgement (Al Naml, 27:23-44). If a woman is qualified and the one best suited to fulfill a task, there is no Qur’anic injunction that prohibits her from any undertaking because of her sex. The hadith literature is replete with women leaders, jurists and scholars, and women who participated fully in public life. There is another hadith which states that 9/10 of our sustenance comes from business. For those who are able and are competent, Islamic society should encourage them to become entrepreneurs or get involved with other types of business activities.” (Roomi, 2009)

He concludes by indicating that women face deep-rooted discriminating cultural and social factors that hamper their growth. Only few receive encouragement from family members, who have spatial mobility, private transport, tend to grow. The paper also highlights educational qualification, good HR policies. The paper comes up with original identification of socio-cultural variables affecting growth of female owned enterprises in Islamic countries.

The empowerment of the women in Pakistan has been the result of the precedent and the Role Model of Prophet Muhammad’s (SAW) wife Khadija (RA). Women in Business are no new phenomena in the Muslim society but the traditions in Pakistan have prevented the development. Despite its significance, recognized worldwide, not much work has been done to study the growth of women entrepreneurs in a Muslim society. In a more, homogenous society it becomes all the more necessary to study the growth of females in business so as to establish closer linkages among the Western society and the Muslim society. Dove Seidman the Author of “How” says “When the world is bound together this tightly, everyone’s values and behavior matter more than ever ... we have gone from connected to interconnected to ethically interdependent” all the more reason to research the female entrepreneurs of Pakistan because they are growing into a force and are going global as well. The Muslim of India, Pakistan and Bangladeshi are roughly estimated to be a little over 500 million and all representing the cultural complexity of South Asia.

In Pakistan, many women are able to cross these barriers and this is the new trend observed by Roomi, 2008 & 2009. One of the strength of Pakistan Female Entrepreneur has been their social capital. They are able to actively participate in economic activities. It has been found that women in Pakistan are receiving moral support from immediate family members. A correct interpretation of the perceptions of Islamic values have played a role in allowing spatial mobility, access to transport, and interaction with male members at school, college, university and office level, has helped them grow confident and to venture in business (Roomi: 2009). This correct interpretation of Islam has come about because of wide range of translating the Islamic literature to English and Urdu which is a Pakistani language. Previously the Quran & Hadith was only read in Arabic without understanding what it meant. Today it is read bilingually and not through a teacher but by most students in their language. It has corrected many perceptions.

## ***RESEARCH METHODOLOGY***

This study took a case study approach as a tool of gathering data & information, and has a Qualitative methodology, and now spreads over a period of 05 years. Outlining the preliminary results of 30 illustrative case studies from Pakistan out of which 10 have been reported in this paper. The selected entrepreneurs have a similar status in society and similar educational background except the few leaders such as Dr. Shela who have been educated abroad and belongs to upper class of society. Case study approach has been adopted as it provides in-depth knowledge regarding the phenomenon being studied such as the understanding of the culture, the sentiments and to understand personal self-reflection need for advocacy and mentoring captured through the story telling. In this research paper female entrepreneurs were interviewed repeatedly over a spread of time and reported the ‘voices’ of the female entrepreneurs. It presents a valuable opportunity for understanding their learning experiences (Guerrero, 2008). These case studies helped to uncover commonalities with female entrepreneurs of this region and the learning experiences shared by female entrepreneurs (Rae, 2005). Further this research methodology may determine the underlying factors responsible for their progress and success in getting ‘clout’ and recognition. Case studies are narrated incidences of life experiences. They have focused on two variable: one the problems faced in getting started and two the building of the platform in the shape of the Women Chamber of Commerce & Industry. The story format has acted as historical background with a multiple of case studies to support the understanding of the prevailing environment. The main case study is that of Dr. Shehla the entrepreneurial leader of this movement which has been embedded with smaller case studies. However the theoretical framework has also been embedded with these case studies. The survey took place in the same period that the women were struggling to establish the Chamber of Commerce hence the women were overwhelmed by their efforts and were inclined to bring in their experiences. No doubt it was something new happening and they knew it, considered learning experience as central to development of entrepreneurial leadership. Further findings may contribute to the further development of a conducive environment for women entrepreneurs. The interviews generally took more than one hour at the premises of each entrepreneur. But the interviews and discussion with Dr. Shela extend over months intermittently. The case studies thereby support the theory and create evidence of sentiments, the emotions the experiences the leadership, advocacy, clout and growth oriented atmosphere and the behavior pattern of a whole social environment surrounding the emergence of these entrepreneurs. Those case studies that were not included have been screened for further research papers.

## ***INTERVIEWS AND CASE STUDY DATA***

There were two parties claiming ownership for the women's struggle and challenge for the Women's Chamber of Commerce and Industry (WCCI). The platform was divided into two zones and Dr. Shehla was made PWCCI president for Islamabad and Punjab and NWFP cities. (Northern Pakistan). The other claimant to ownership of the women's chamber was a Karachi-based woman entrepreneur named Salma Ahmad, who was given responsibility for SWCCI offices in Sindh and Balochistan (Province of Pakistan comprising Southern Pakistan).

Dr. Shehla said, "We felt there was a need for such a chamber because the existing institutions of this kind do not pay enough attention to women. We feel that one of the most effective methods of promoting women entrepreneurship is to empower them; this requires an institution solely devoted to this cause'. For many months I have argued with government officials and private organization about the ownership of the WCCI and finally, I have won even if its been divided into two territories".

This aspect of dedication and willingness to take the mantle of leadership is the hallmark in her personality. Her leadership acumen was high and she knew there would be a price to pay.

One of the steps taken by PWCCI which brought immediate acceptance was the conference organized as "National Beautician Conference" in the September of 2005. This event turned out to be a resounding success and it somehow gave great confidence to women entrepreneurs. It laid the foundation for women to recognize their own strength that came through networking and through being united on one platform. It propelled them into a higher economic status. As Lahore has a large number of small and micro beauticians they took pride in their profession and felt encouraged to carry on their business. Some found support from their family for their business because this business pertained to women. It was a female oriented business area. It received less hurdles from family and society though a decade ago this profession and this business was looked down upon.

Uzma Beauty Clinic and Institute- Living with extended family & petty bureaucrat.

Uzma belongs to a modest middle class background. Her story began when her husband supported her dream to setup a beauty parlor; The Uzma Beauty Clinic. Though they pioneered the venture at a time when there was an absolute vacuum in the market, 1984, she faced numerous threats some real and some perceived. She could not stabilize her business as she was constantly firefighting. Her relatives at one time turned their back on her family and her children suffered humiliation within relatives. "The family plays a very important role in a traditional Pakistani woman's life. Face saving is essential within the family. Your profession or your activities can damage the reputation of the entire extended family from uncle and aunts to in-laws of the family members. You cannot cut yourself off from your

family to do your business. Women are not generally seen as bread earners or businesswomen in this culture” explained Uzma, as she remembered how she had to deal diplomatically with her father-in-law to continue with her profession.

“Today I find that our society has turned more ‘grey’ and she explained this by saying “To establish my business I have had to work 18 hours a day. Today I can say that my networking and my membership of PWCCI has been a great support. However, the journey was never easy. My real problem has been dealing with these petty bureaucrats that come from various government agencies. It is not easy to deal with these Mettlesome officers from Electricity department, or from Municipality or from the Police, or from the Tax department. They come threateningly and spreading fear among my girls working for me. At that moment it appears as if someone has pulled the rug from under your feet”.

She narrated incidents of how she continuously wastes time in firefighting and depriving herself from quality work. She feels she could do much more if the environment was more conducive. “Our system has evolved as a culture of unfriendly environment. Everyone perceives that women entrepreneurs can be harassed and made to give illegal gratification to avoid further disturbance. Its this ‘grey’ culture, immature attitude, towards your own society that is depriving our society the fruits of growth and development. I think we, the members of PWCCI can now contribute towards improvement and empowerment of women for a better tomorrow”.

#### Moral of the Case:

Uzma has identified all the areas that were mentioned in various literature reviews. Her emphasis on face saving and her experience of the petty officers is a reminder of the way the environment existed. But her positivity is reflected in her statement that ‘our society has turned more grey’ meaning that there was a slight change in the environment. This shows exceptional emotional intelligence and resoluteness to continue. She had learnt from this experience and took care of her staff with mentoring and comforting attitude to give them confidence. She has the vision to set the changing environment. She reflect a women leadership capabilities.

Another event that gave boost to the Women Entrepreneurs was the public display by the Government that they supported the struggle of women entrepreneurs. The then Prime Minister Mr. Shaukat Aziz awarded a shield to Shehla, President PWCCI, on September 14, 2005, in recognition of her accomplishment and performance of promoting the Chamber of Commerce for Women. It was an acknowledgement for the struggle for this Forum. Until this time it was not recognized officially or legally as the Women Chamber of Commerce and Industry, though even this was not a legal recognition, yet it gave them enough clout to be heard.

#### ‘Re-Grow’: Herbal Hair Oil

Taking Care of Members: Counseling and Mentoring by the Chamber of Commerce Leadership of the WCI was a responsible and understanding role by Dr. Shela as an women leader.

The events that led Rukhsana Zafar to become an Entrepreneur is yet another story. She had a master's degree in zoology, and had invented herbal hair oil that she named as 'Re-grow'. She wanted to sell it. However, her husband was a businessman and was doing quite well so he did not allow his wife to pursue it. So she came to Shehla and said "I have invented this product and I want to sell it in the market and you have to take care of my husband, I have a lot of faith in you".

"This meant that I would schedule a counseling session with her husband and giving him confidence and assurance of his wife's capabilities, which he should empower and take pride in".

Shehla was thinking of the past on providing this account said; "She was one of the first who came to me when my chamber was announced, she brought with her a very old and shabby looking pamphlet which I think she might have made when she was in school or college. She also brought with her a very old packaging. I didn't know how old it was, but all I can say is that it was years and years old. One good thing by now, her children were grown up. Now she is very successful and is traveling with us everywhere we go. It was all done with a bit of counseling". One of the thing she felt that this incident taught her was to become a counselor to the families of her members. It had become essential in her capacity as a leader of these women to give counseling. She felt she was strongly positioning herself for counseling not just the women but also their husbands.

Moral of the Case:

Once again this depicts an educated entrepreneur having conviction in her idea and going about it with an approach to achieve it. Dr. Shela once again displayed a high sense of emotional intelligence and adopted the role of a mentor and leader and not shirking any responsibility in her role as a leader of women entrepreneurs. She knew she had to build membership o the PWCCI but also empower women to take on role as serious entrepreneur. She successfully counseled the spouses of the members and took her role of mentoring and counseling seriously as leadership is more demanding today, especially for women. She was willing to go back to her followers to support them to walk the distance.

### ***SOCIAL, CULTURAL AND TRADITIONAL TABOOS: WOMEN'S ROLE IN BUSINESS***

The social, cultural, and traditional taboos on women allow men to carve legitimacy for themselves in public affairs, as well as in the sphere of production and related economic activity. Women are not acceptable, seen as running businesses. Tradition and convention and culture have never allowed it. This culture and traditional taboo even prevented women from obtaining education.

As Shehla said "The main issues were ownership of property, lack of control over capital land and business. That if a woman wants to do any business her husband or her father would not give her property (to be used as collateral). They

will give it only to the son, but not to her. This puts her at a disadvantage with her banker, who advances only against collateral". There is also inherent lack of encouragement from male family members. The absences of networking mechanism and patriarchal social norms have prevented women from running businesses. The situation was more grave, serious and to great extent dangerous for rural women. There were no role model of rural women who rose up against the traditions and taboos till then. It was inconceivable that a woman would have the guts to defy the norms of society and become an entrepreneur or a social entrepreneur.

#### Mukhtara Mai – the rural scenario

It was probably the worst of times or best of times for women.

One could see that an environment was developing that supported the rights and recognition of women. It was in June 2002 that a woman, Mukhtara Mai was raped by the landlord family of Meerwala near Jatoi in the remote corner of Rural Punjab. She was the victim of one of Pakistan's more 'politics of rape' a infamous crime against women. She shocked the traditional mindset by approaching the Government and the Police for help against 'politics of rape' in Pakistan. This incident also received international attention. "After she was brutally assaulted the illiterate Pakistani was supposed to restore her family honor by killing herself. Instead, Mukhtara Mai chose to live, to fight for justice and to find a better life for women like her. She became the symbol of women's right". "I want to remain a symbol of oppressed women until someone shoot me" she says. The Government rose to the occasion and supported her and provided her legal support. (Reader Digest JAN 2008). Ultimately, it was the financial support from the Government of Musharraf and donors from Canada and Norway that helped her in setting up the Mukhtara Mai Model Girls School and Mukhtara Mai Women's Crises Relief Centre, home for women hit by crises. Today its educating 650 girls who would have faced a dismal future and it employs 50 providing shelter to women exploited. She remains today a source of inspiration, relentless to pressure to withdraw case against the perpetrators of that horrific crime. (Express Tribune July 25, 2010)

#### Moral of the Case:

The case study of Mukhtara Mai depicts – the change and empowerment of women at this period in time. What is important is that these little incidents add to the change of the whole picture. It's the progress which is more relevant for such a movement and change follows. The point in this case is that women as social entrepreneurs or as entrepreneurs are noticeable. They have learnt to stand up for their rights. The clout in this case come from media.

The logical outcome of a gender biased environment was the low status and weak bargaining position of women. That indicated the disadvantaged position of women who try to start or run a business in Pakistan. However as we have seen in Islam women in business are not frowned upon.

## ***CHARACTERISTICS OF WOMEN ENTREPRENEURS IN PAKISTAN AND IMPACT OF PWCCI***

According to a survey report, (prior to the emergence of WCCI), 'Women Entrepreneurs in Pakistan' (Nabeel Goheer) ILO Islamabad 2003, eighty percent of the women in business were between the age 20-49 years. They were generally found to have only one or two children (65%). It was also found that a woman entrepreneur usually belongs to family living away from extended family with husband and unmarried children. That helped them to keep out of the social cultural influence. Similarly their literacy rate was above national average, and had obtained professional training. Barriers, some real, some perceived and some self-imposed, confront women entrepreneurs. In the area of export marketing, obstacles include limited international business experience, inadequate business education and a lack of access to international networks. A similar observation was made by Roomi (2008). His sample consisted of 265 and of these 54% managed micro enterprise, 36% managed small enterprises and 10% medium enterprises. Roomi found 82% engaged in traditional sectors of textile, apparel, education, food, beauty, and health sector. It is here he noted deep rooted social cultural values segregating female entrepreneurs they were serving female customers. Small investment and they usually began with pilot project at home. Usually in their sector male, female interaction was almost nonexistent.

Whereas Goheer also observed most women headed businesses operated from home, and financial matters were taken care of by male family members. Women entrepreneurs were seen in subordinate roles; with low levels of education and technical skills; low exposure to business; lacking role models; lacking peer support and business associations; and, low income and poor investment capacity. About sixty percent of women entrepreneurs in Pakistan have opted for traditional business such as parlors, bakeries, boutiques. However, the largest numbers were in the garments and handicrafts businesses.

Other than these, societal, cultural norms and forces of patriarchy and a systemic subordination of women by men also impeded women in business. Other challenges faced by women in particular are; financing, globalization of social and economic environments, marketing, and management. Economies such as Pakistan's economy can pose difficult hurdles such as banking, legal contracts, political contracts, customs tariffs, and impediments by petty bureaucrats who daily invent new mechanism for the simplest procedures. However Roomi (2008) states that literacy rate plays important role in creating awareness of their rights. 82% of his samples were high school graduate, 53% had bachelors and 15% post graduate. Roomi (2008) states that women have been denied the right to education despite Islam having made it compulsory for men & women to peruse education. He also draws attention to the rights given to own property, inheritance, business, to keep her madden name and to hold political office. Based on these facts verified from Hadiths and the Quran, the dichotomy is that religious entrepreneurship is

misleading the general public and wrongly denying the female entrepreneurs of their position in the economy.

Yet the major problem seen was the lack of confidence of women entrepreneurs and extreme shyness to approach organizations for support. In the opinion of Shehla, they also did not have the capability to present their case or proposal hence they were unconvincing to the bankers or the financiers.

The below mentioned cases reflect a spectrum of experience over a long time span. It is a fairly good description of the environment confronted by the women entrepreneurs.

#### Nikki's Beauty Saloon

Mrs. Ayesha had lost her husband at a very young age. They had four daughters and a son and three of whom were minors and two were as yet teenagers. 'Nothing is more devastating then to have your world shattered while you are still young. In a country like Pakistan, women take the backseat and are taken care off by their husbands. It takes time to get your bearings and I found myself fumbling with my husband's business - an auto car sale agency "Soon I realized I must do some business to survive but it was not my cup of tea to run a car agency. Therefore, I soon negotiated a sale of my husbands business and went into the beautician business".

What had raised her confidence in the business of beauty saloon was her friends who admired her makeup skills. Occasionally she would do the makeup of some brides getting married in her family and among friends. She had a natural talent for it and now she was being appreciated by her friends and peers. It was at that moment in time when she was convinced that beauty saloon was the kind of business she wants to be in.

As a matter of fact the business of beauty saloons had come of age. PWCCI had given it a big boost by organizing a conference on the subject. The concept in Pakistan of beauty saloon was initially introduced by Chinese Parlors. All weddings require bridal makeup and the Chinese beauty parlors performed this service. Another source of business were the professional working women who had no time to take care of themselves. Hence beauty saloons were becoming responsible for grooming women. Technology too had played a vital role. (Based on the interviews conducted by Maira Taqi and Kinza Malik)

#### Moral of the Case: Taking a Stand to fight for your cause:

This case depicts scenario when women inherent business when they loose the male member of the family. But it also depicts the enterprising side of the female entrepreneur. It's a case when a family business is dropped in your lap by circumstances. But it also depicts how a woman chose her path and line of business. The confidence comes from the availability of a forum and from role model. These women have become the pioneers Women Entrepreneurs of Pakistan and have proved it.

Anjum Rafi the owner of 'Qashang Boutique' and 'Heritage School System' is a Masters in Textiles. Though she successfully came out of her teething problem,

still faced numerous problems. She quickly learnt that to be a member of a chamber or association was really beneficial for her in a male dominated society. Hence, first she joined Lahore Chamber of Commerce and Industry and later the Pakistan Association of Women Entrepreneurs. It was a great boost to her to join the PWCCI. She felt that this had empowered her to think in terms of international business and to participate in fashion shows abroad. But most of all, this gave her status among the Business Community.

Moral of the Case:

Despite her experience she needed the clout and the forum of the PWCCI. It opened other vistas such as the international market.

On the other hand, Bushra Iqbal who had been running one of the first beauty clinics Bushra Iqbal Beauty Clinic in Lahore after qualifying from Hannereuth says that “The worst of all was dealing with orthodox government officials”. At that time, there was no support or sympathy for a woman entrepreneur.

Moral of the Case:

There was no growth oriented atmosphere from women until they setup their forum the PWCCI. The petty bureaucrats stopped harassing these ladies realizing the establishment of the platform the PWCCI.

Farah Yousaf of Comeily Collection, a garment unit, reflected questions she confronted, “Doing business is the responsibility of men. Why are you doing it?” For a long time the absence of a support system hampered her growth as with every woman entrepreneur. It was essential for her to join the Women Entrepreneur Society of Pakistan and the Lahore Chamber of Commerce in 1998 and eventually the Punjab Women Chamber of Commerce and Industry.

Moral of the Case:

Women in Pakistan needed to be members of an association to be heard and to carry a clout. They have setup role models for the world.

Robina Jamil not only confronted the humiliation of the male dominated business environment but also the derogatory attitude of the relatives. On the other hand nobody was willing to do business with her because she was a woman. All the whole-sellers would not respond to business deals handled by her and would insist on doing business with the male.

Moral of the Case:

It was very difficult for women to penetrate the networking platform for business without being members of a Chamber of Commerce or an Association.

These mini cases are reference points that lay the ground to establish the theory of female entrepreneurship in Pakistan environment. The multi-dymentional social factors that hinder women entrepreneurship and despite the cultural taboos these women have emerged as a force and have gained acceptance. There may be the need to study deeper to profile the emerging picture of Pakistan female entrepreneurs.

It was Dr. Shehla’s persistence and conviction that the women need a full-fledged chamber. She used every resource in her reach to propagate a separate

chamber for women. But it was on 'bridge championship' organized by the family in memory of her father that she had got a chance to meet the President of Pakistan and talk about promulgating an ordinance for a women's chamber. She finally approached President Musharraf at the Bridge Championship and the President eventually agreed to promulgate a new Ordinance to support the establishment of Women Chamber of Commerce and Industry.

Eventually after long struggle by the Women in Karachi and Lahore a final recognition of the women's right to do business was established in the Pakistan 2006 Ordinance called the Trade Organization Ordinance (2006). It allowed more representative associations including the women to have their own Chamber of Commerce and Industry. The women are now able to form their own associations without male sponsorship. Hence women such as *Shehla* in Lahore and *Salma* in Karachi moved for achieving legal registration of their respective Chambers. But it was not as easy as it seemed.

## ***ANALYSIS OF FINDINGS***

What choices did women have? They have always led a dominated life without an outlet. The options were limited. With that kind of background, it was not possible to conceive a Women Chamber of Commerce and Industry. As a matter of fact there are only a handful of examples of WCCI existing in the world though progress has been made in Asia and Africa. But Pakistan is a society of paradoxes where a women's exclusive bank existed (First Women's Bank). It is a society where all over the country there are many schools, colleges and universities segregated and exclusive only to women, besides co-education institutions. It is a society with tradition of a woman being its Prime Minister twice. It proves that the women have a conviction of purpose and cause to pursue. Yet the paradox is that women are really very weak in this culture. The other paradox is that where as women are striving for economic emancipation, they never desired emancipation from their family. There is no place for a single woman; she must have her family standing in the back ground. Her husband or her children have to be in her picture. Their strength comes from the association with the family. (And *Muktara Mai* is one example of a woman finding her way back in her society among her own people). Legitimacy came from the strong association with the immediate family so a new norm of society has emerged. PWCCI was the new platform of culture and emancipation from dependence but not from family. Culturally Pakistan is an emerging culture, a society which has influences of different cultures of societies, specially those that were in the subcontinent like Hindu society, the Turkish and Iranian culture. This brings us to the Research Questions.

1 Given the cultural overcast, what entrepreneurial traits or characteristics or competencies can be identified among the Pakistani female entrepreneurs, for gaining recognition and clout?

Women entrepreneurship in Pakistan is in a transitory phase. The emerging role models in the 21<sup>st</sup> century have given a lot of weight to women entrepreneurs.

This can be seen in each entrepreneur displaying her characteristics. Each woman is a case uniquely responsible to bring about a change. The case studies are not in isolation from the theory but support them. They are the “voices” of the Forum the PWCCI. They are the evidence of the sentiments, the emotions the experiences and the behavior pattern of a whole social environment surrounding the emergence of these female entrepreneurs. On the other hand they also reflect the grit and perseverance of Dr. Shehla and the challenges she accepted as a leader of the women entrepreneurs. The displays leadership by showing dedication and willingness to take the mantle of leadership.

2. Especially what entrepreneurial leadership characteristics are depicted through the case studies?

The leadership style of women entrepreneurs in Pakistan has been the same as in other regions. The consultative style has been the hallmark of their leadership traits. Shehla herself showed flexibility and accommodation to the prevailing circumstances, yet stood her ground relentlessly to achieve her goals. Culturally neutral concepts such as the theory of leadership have been equally applicable in this environment. What could not be considered suitable was the entrepreneurial intention or motivation of other regions such as European or American or Russian. Each region has its own unique characteristics and traits. The conclusion that one can draw from the comparison of different cultural background and different societies is that theories developed so far in the western societies do not apply to Pakistani environment as there is not sufficient evidence and research knowledge of the women in business.

It was observed that the experiential learning developed the entrepreneurial competencies of the women and in turn increased the confidence and level of entrepreneurial leadership capabilities among all the women entrepreneurs. Yet the most basic principal of management was the most sought after training by the members of the newly formed PWCCI.

Some of the characteristics that emerged from the case studies have been; mentoring, psychological advocacy, willingness to search for opportunities, networking, using the platform for their problems, bond of being a business woman overriding cultural differences, dedication willingness to take the mantle of leadership, resoluteness, long hours of work, learning leadership and entrepreneurship through experience.

It was also observed that the female entrepreneurs are more educated than her male counterpart as seen in the western societies. But her professional experience often falls outside of traditional business sector e.g. an engineer may set up garment business or a boutique or bakery.

3. What brought about the Women Chamber of Commerce and Industries in Pakistan as the forum and platform for women?

Women by nature are inclined to go for mentorship or coaching and it has been amply demonstrated that the success of the establishing the PWCCI was because of the coaching & mentoring role of Dr. Shehla and the team. Women entrepreneurs look for role models and mentors that help them carve out paths to follow. However the impact

of experience and training has been observed as a factor for building leadership self-efficacy among the female entrepreneurs similar to western societies. Such theories are culturally neutral. Mentoring and coaching is a payoff for the gains of their life. The Chamber of Commerce and Industry and its leadership is being looked upon for psychological advocacy required to start small business, to create growth oriented atmosphere, create networking and economic empowerment. The WCCI is also being looked up for providing guidance how to approach banks and force governments to pay attention to women entrepreneurs' requirement. It also provides a system of bonding because they share the some problems.

None of the barriers that stood in the way of these aspiring pioneering women entrepreneurs were religious or Islamic ideology based. These were socially and culturally oriented and represented the norms of the society. (A society that still preserved certain customs and traditions and norms). Some were deeply rooted for centuries and had taken this form and appeared to be religious edicts. It is the realization that culture is the biggest hurdle in the economic emancipation of women entrepreneurs, which led to a growing desire to have their own platform. Hence the long drawn struggle by a set of women to establish and have it recognized.

It has also been established that economic emancipation was not emancipation from men dominance or against family bond. It was economic freedom and more an expression of capability, an expression of an art form, an expression of skill and ability and competence to do what one had chosen to do. In fact it was an expression of equality given by Islam as stated by Quran and Hadith. Women entrepreneurship is not alien to Islam. The 'Izzat' and 'pardah' was the defensive mechanism provided to women and it, protected her if she knew how to allow it to be implemented. Religious entrepreneurship imposed its own version of Islam on women entrepreneurs; it was under the guise of religion that this concept was being used to prevent women from spatial mobility. But the awareness and education has made women realize their status and position in society.

## ***CONCLUSION***

The social cultural and traditional taboos on women allow men to carve legitimacy for themselves on women. It was this exploitation by men that led the women to set up a common forum to claim equal rights that were theirs by virtue of Islam. Once the platform was legally established and officially recognized, it brought more opportunity and clout to assert their economic and legal rights. As time passed these members realize their growing strength and the value of the association or the platform of Women Chamber of Commerce and Industry. They have opened the gateway for women in other parts of this country. Today Pakistan has experienced growth of more Women Chamber of Commerce. Almost every province has its own Chamber of Commerce as of 2015.

Family and spouses played a very strong supportive role as in the case of their western female entrepreneurs, acting as advisors and legitimizing the

entrepreneurial ventures in the society. However successful women entrepreneurs were found to be living outside the domain of extended family allowing the parental controls but expecting husbands to give understanding and support.

We also conclude that the economic empowerment of women, the clout, comes from being together on a platform that provides the support services and to be able to raise their voice. This platform that fit the requirement of all their needs was the Chamber of Commerce & Industry. It infact it provides a formidable clout to women and gives their economic emancipation.

Though the serious work on female entrepreneurship has not been attempted but is the need of the hour now. However now there is a range of it available. There is always reference to the influences of culture on women but it has not brought out the strong South Asian impact that exists among the female entrepreneurs of Pakistan; Roomi has time and again emphasized the freedom to do business in Islam and has given the role-model in Islam for the Muslim women but has not focused on the various crucial cultural barriers which are the real hindrance and precipitators of sufferings by the women in pursuit of economic independence. In this respect much work remains. Researchers could well bridge this gap by undertaking step by step cultural taboos, geographical regions, ethnic origin, rural and urban divided, tribal & feudal bearing on culture and influence women in Pakistan. There is vast scope for such serious research, which will evolve into a situation of change as has the correct knowledge of Islam done to the current leaders and female entrepreneurs in Pakistan. This would have an impact on all other neighboring countries of South Asia.

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## **IMPORTANCE OF OWNERSHIP TRANSFER PLANNING FOR FAMILY BUSINESS ENTITIES**

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### **ABSTRACT**

*There are a number of definitions of family enterprises in literature. Depending on the fact which definition is used, the statistical data about their number and results will differ. According to one short definition used by the EU, family enterprises are those enterprises in which the company founder and his family members (including the descendants) have, based on their participation in basic capital, a minimum of 25% voting rights. In such a way, family members become the most significant interest group which influences business activities of the business entity. Family business entities on a global level take up 30% to 90% of the total number of enterprises, with an annual profit level of over a billion dollars. It is a common expectation that family companies can be found in the group of small and medium enterprises (hereinafter: SME), but they are also present in the group of large corporations such are Toyota (Japan), Hilton (USA), Walmart (USA), BMW (Germany), FIAT (Italy), IKEA (Sweden), Lego (Denmark), Tata Group (India), etc. With the aging of one generation of founders and their retirement, there occurs a transfer of ownership to the heirs. In certain cases, after this type of ownership transfer, family business entities are sold to new owners. This is the case when the heirs have chosen other business activities. Each change in ownership structure can cause a series of other significant changes in the way of implementing the business activities of the business entity which leads to larger or smaller crises in business activities. In fact, ownership transfer from one generation to another is something that is repeated in numerous cases. This is the reason why transformation stages are recognizable, so that the entire transformation process can be systematically influenced. Thus, the problems caused by the change of founder can be minimized and the advantages of ownership transfer supported. The aim of this paper is to define the key elements and effects of the long-term ownership transfer process in family business entities. Based on research, the possibilities of increasing efficiency through the process of long-term planning can be reviewed.*

**Key words:** Family Business Entities (Companies), Ownership Transfer, Planning of Organizational Development.

**JEL Classification:** D23, O21

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## ***INTRODUCTION***

The terms family business entities or enterprises, family companies, family-owned businesses, companies under the control of one family are the various names which can be found in literature to describe family enterprises (IFC, 2011).

In accordance with the Charter on SMEs (European Commission, 2008) business entities are “each entity engaged in economic activity, no matter its legal form.”

According to Serbian legislation and in accordance with the Law on Economic Entities (National Assembly of the Republic of Serbia, 2011) economic entities are companies and entrepreneurial businesses. The common feature is an engagement in economic activities and these entities are taxpayers regardless of the legal form of registration. In the further text, the term family companies (or FCs) will be used as a synonym for family businesses due to simplification and a following of global statistics.

Due to the way in which families and businesses are connected, FCs have a series of specificities by which they differ from other enterprises. Namely, problems within the family can be reflected on the business activities of the enterprise and vice versa.

In FCs, the long-term benefit of the family and the enterprise are tightly connected. The long-term goal of the family and the development of their business are continuation and increase of mutual benefits. Both the material and non-material values of the family and their business are also tightly connected and cannot be observed separately. To manage them in the long-term, they should be acknowledged and understood.

They are a very common phenomenon in all parts of the world, the development levels, activities, sizes and various legal forms. The most common form is within small and medium enterprises (hereinafter: SMEs), even though there are large international companies which are successful family companies.

There are a large number of definitions of the term ‘family firm’ which differ between themselves. In each definition there is a tendency to connect family, enterprise (legal entity) and the method of managing business development.

Family business is, according to IFC (2011) a company in which most of the votes are in the hands and under the control of one family, including the founder (or more of them) which tend to transfer their business onto their descendants.

According to the Family Firm Institute, Inc. (2014) family companies are defined in various ways. In one definition, family companies are enterprises which manage and/or lead dominant coalitions of one family or small number of families through the multiple generations, with the intention to follow the vision of business activities. The same source gives multiple definitions which are primarily connected to the participation of one of more families in the ownership of the enterprise.

Family companies are those companies in which several family members are involved in managing the structure as majority owners or managers, at the same time or during a period of time (Miller et al., 2007).

A somewhat different definition of family enterprise is offered by Deakins & Freel (2012) according to which the enterprises in which two or more capital owners have more than 20% of the voting right and are mutually connected through family relations, are called family companies. The enterprise, in order to be called an economic entity, must have at least two family members who are within the ownership structure.

According to the definition offered by the European Commission (2009) family companies are enterprises of a certain size if they meet the following requirements:

1. The major managing rights are owned by one or more individuals who have founded the enterprise and/or by spouses, parents, children or their descendants.
2. Most of the managing rights are direct or indirect.
3. At least one representative of the family or relatives is formally involved in the process of enterprise management.
4. The enterprises satisfy the definition of family enterprise if the criteria of founder or family members (including the descendants) are based on participation in the capital, with a minimum of 25% voting rights.

The noted definition is very wide and most of the private (solo) enterprises with one owner can be classified into this category, even when there is no change of generations of founders in the ownership structure of the enterprise. This group also includes enterprises with only one founder who can potentially extend into the second generation in real family enterprise, but this time in a narrow sense. This definition of FCs will be used in this paper, as EU statistics have been compiled on the basis of this officially adopted classification.

According to the foreword written by Boris Vukić (Ward, 2006) it can be noted that one company will become a family entity only after a change in the descendants of the first generation of founders or, in short, family companies are enterprises which are owned by more than one generation of the same family members.

All the given definitions observe three crucial elements:

1. The number of founders.
2. The minimum voting rights of the founders based on owning the basic capital of the enterprise.
3. Ownership transfer from one generation to another one. If we apply this criterion we have a definition of FCs in the narrow sense of the word.

Without the third criterion, a large number of private companies, including those with one founder, fall under the category of FCs. If we include the third criterion in the definition we will have FCs in a narrow sense as they now represent enterprises which have already been through ownership transformation in the family and they are in the second stage of the life cycle. Applying the third criterion, we get a significantly (around 50%) smaller number of enterprises which meet this condition.

These definitions do not insist on a vision of development but only on voting rights based on participation in capital. During the founding of small and medium enterprises (SMEs), the founder can with certainty predict that the company will become a family enterprise. It can be a founder's desired development policy although this undoubtedly is not the only factor which can influence such a policy. It is hard to speak about the vision of business activities of one family during generations as it can be related to attitudes about the values and beliefs which in turn are a reflection of the attitudes of the founder's family.

The ownership transfer from one generation to another is much more than a simple ownership transfer. Besides the inheritance of the capital share, the heirs also receive a series of material and non-material benefits from the life experience of the older generation. The following generation of family business heirs, along with property, also receives the family social status, knowledge about surviving in business, and a reputation in front of other interest groups on the market, such as suppliers, buyers or financiers.

According to Ward (2006) almost one half of the total number of family enterprises fail to survive to the next generation. Matters are also changing in the USA, and thus it is predicted that in the future, 40-50% of family companies would be led by sister and brother co-owners.

This is the reason why planning the ownership transfer of one family generation to another is a part of a more extensive subject which is in the world of traditionally successful enterprises called the long-term plan for developing family businesses (FBC, the Family Business Development Center, ASEE, 2014).

The aim of this paper is to define and analyze the crucial elements and effects of the long-term multiple process of ownership transfer on family business entities. Based on this research, the possibilities of increasing its efficiency through the process of long-term planning are reviewed.

## ***THE ROLE OF FCS IN THE ECONOMIES OF DIFFERENT COUNTRIES***

FCs are very much appreciated as partners and loan borrowers in financial circles, as the survival of such an enterprise is connected to the financial interests of an entire family. This is the reason why everyone is devoted to preserving the family business, even when the personal interests are not the same as the family interests. There is an ingrained attitude that FCs are more reluctant to borrow money even when there are rational reasons for it. FCs founders would rather sacrifice a higher growth rate than increase the risk and potential higher growth rate through engaging external financial sources. Thereby, a lower growth rate is intentionally accepted, as well as the responsibility for business survival. FCs, furthermore, tend to secure continuity in business activities and have a tendency toward long-term planning.

According to the data published on the Family Firm Institute Inc. website (2014) from the total number of registered economic entities, 70% to 90% are family companies of various legal forms and sizes (Figure 1). There are large FCs such as the Fiat Group (Italy), Walmart (SAD), Ford Motors (SAD), Porsche (EU), Benetton (EU), Henkel (EU), BMW (EU), the Samsung Group (South Korea), Tata Group (India), Foxconn (Taiwan) and numerous others.

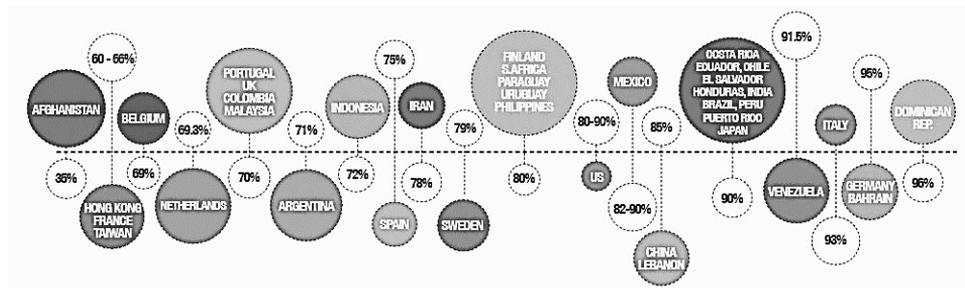


Figure 1: Percentage of family businesses in the private sector

Source: Family Firm Institute Inc., 2014

According to data (Deakins, Freel, 2012) two thirds of private companies in Australia are FCs, while the situation in Great Britain is even more in favor of family companies, as almost  $\frac{3}{4}$  of all enterprises are owned by families, and in Italy 90% of all companies are FCs, while this number in the USA is 96%. If we take Italy under consideration, it is obvious that the most developed part of Italy is Lombardy, whose economy is characterized by a large number of successful family companies.

Most FCs, per number of employees, work volume and capital under their disposal, belong to SMEs. It is estimated that FCs on the global level participate with 70%-90% of the world annual GDP. On the levels of national economies, FCs participate in creating the national GDP with 50% to 90% (Figure 2). FCs are showing a higher level of profitability related to the other enterprises if observed long-term.

According to Professor Blagoje Paunović, research indicates that in the future there will be more FCs. The EU in their documents recognize the significance of family economic entities to whose further development full institutional support is given. In Serbia, knowledge of the advantages and disadvantages of family economic entities is still not sufficiently promoted, as there is no real information.

The feature of all FCs is that one family is the owner of significant shares in the ownership of the company (more than 20%, mostly over 51%) and based on it, it has acquired the right to manage the company in proportion with its participation in the capital. The larger the participation, the greater are the managing rights of the family.

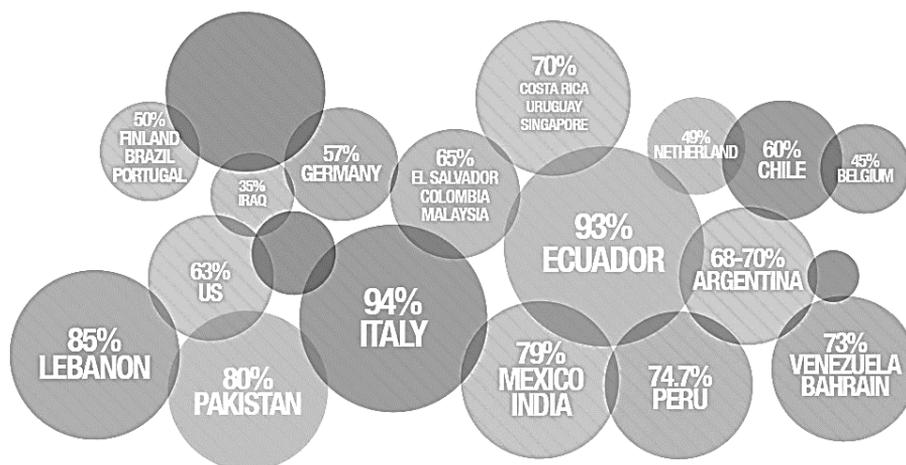


Figure 2: Percentage of family business contribution to the national GDP

Source: Family Firm Institute Inc., 2014

## **EMPLOYMENT POLICY**

The major and basic motive of the entrepreneur to start his/her own business, in most cases, is to provide a source of financing for the family and himself/herself. All other reasons such as self-reliance, self-realization in certain areas or independent time managing, etc., are less present.

During the foundation of their own SME, entrepreneurs create their own work environment. They employ the needed labor force, one which could fit within their system of values and working mode. The entrepreneurs are the ones who create the job and working atmosphere, giving direct orders and directly communicating with all employees. This is the reason why most SMEs never grow into large companies and furthermore, only a small number of entrepreneurs, 5-10% according to Deakins & Freel (2012) create the enterprise as a system which should develop and grow during time.

According to data from the Family Firm Institute Inc. website (2014), during 2012 between 50% and 80% of workplaces in most world countries were created by FCs (Figure 3). For financing the start of business, 85% used family funding.

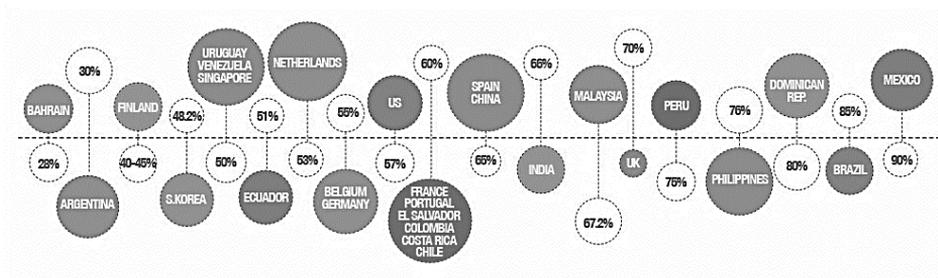


Figure 3: Percentage of workforce employed by family businesses

Source: Family Firm Institute Inc., 2014

Same sources claim that in the EU, family companies create over 5 million workplaces which make 40% to 50% of the total number of workplaces. During an economic crisis, FCs will delay the positioning of new people in management positions, as well as engaging professional management, but will attempt to retain or employ a new labor force. The tendency of retaining a labor force, even in negative macroeconomic trends, is a fact which can be seen in the statistical records of the number of employees in EU SMEs (Gagliardi et al., 2013), during an economic crisis and the decrease of the GVA created by economic entities.

According to research by the Agency for Regional Development (TNS Medium Gallup, 2013) the reasons for starting a private business in Serbia during 2012 differs according to gender. Firstly, there is a desire to be independent (self-employed) (33% of men and 30% of women). Secondly, unemployment is a major factor for 17% of men and 22% of women. Thirdly, another reason for founding a SME is spotting a business chance in the area of the founder's previous professional area (with 23% male and 18% females).

### ***FAMILY ENTERPRISES AS SMALL SOCIO-CULTURAL SYSTEMS OF THE FOUNDER***

Family enterprises reflect the features of their founders. As illustration for such a theory is quoted by Boris Vukić (FBC Family Business Development Center, ASEE, 2014) which gives the following three axioms of family enterprises:

1. All founders see their companies as their own children.
2. All children look like their parents.
3. Possessive parents make their children 'imbecilic' and incapable of fighting through life.
4. If the founder fails to personalize the company (enterprise) and does not move forward from 'entrepreneurship to professional management' and does not make clear rules, then his biological grandchildren will not get to know the family enterprise.

Adopted values are of a long-term character and are very hard to change. They represent some sort of starting point in forming the long-term strategy of the development of the family and family business.

Family companies represent socio-cultural systems of the countries where the family originates from and/or in which family members have spent a significant part of their lives. This is firstly related to the value judgments and culture which the family members have accepted as their own standards in life. It can also be connected to the environment which they originated from, with small or large influences from other environments and cultures where they spent a significant part of their lives.

Just like family enterprises can reduce the unemployment of emigrants from other cultures and speaking areas, they can also, in the long term, represent the restrictive factor of their own development. The problem of the inclusion of ethnic minorities is one of the big problems which even the most developed countries have failed to solve, albeit investing significant sources into various programs.

The family enterprises of immigrants as a rule employ firstly their relatives and employees which come from their own regions, speak the same language and belong to the same culture. Their premises usually abound with national symbols of the culture they originate from. To facilitate communication with customers and suppliers, they are often located within quarters and parts of the city where other members of their national minorities settle. Thus, districts in where members of one nation or culture dominate are created, such as Chinese, Indian, Muslim, Christian, etc neighborhoods.

In some cases, many years pass by and immigrants from various countries never learn the language of their host country. In a certain way this isolates entrepreneurs from national minorities and limits the development of their family enterprises in regards to the possibilities offered by the country. Due economic migration, migration directions as a rule develop from less developed to more developed countries and regions. The host country offers much greater possibilities than the settlers had in their home environment but due to insufficient language skills and a lack of formal education, the immigrants often cannot meet the employment conditions and when they do, they often have smaller wages than their hosts. It is without doubt that there is discrimination but the mentioned reasons make false differences. Thus, family enterprises formed by immigrants can be a restrictive factor for employment.

Ceja et al.,(2010) claim that an organization can create strong emotional relationships between the employees if it has goals and values which coincide with the individual values of the employees. Sharing the common values and accomplished results can make employees feel proud to work in such an organization, no matter how big or significant the business activity is. In this way, each employee striving to fulfill his/her own goals will contribute to accomplishing the goals of the organization. This is characteristic for successful FCs and gives strength and a recognizable corporative culture. Each member of a FC knows what the acceptable behavior for an organization. Basically, values are the essence of the spirit of FCs and lead to accomplishing all matters between a family and its business. Shared family values of a family business are the basics for making a strategy and long term plans.

## ***MANAGING A FAMILY ENTERPRISE***

The long-term goal of family business development managing is preserving and developing of the family business, which in turn should provide a growth of wealth and values for the family in time. In the conditions of extremely negative macroeconomic trends, the goal of managing is continuation of business or minimizing in the case of profit loss.

Each FC during time goes through a recognizable life model, which can be completed, depending on the company, in a certain life cycle. According to Ward (2006) during the generation shift of the founders, each family enterprise is faced with two crucial challenges:

The transition from one to another generation of owners and enterprise leaders, Adopting new and unconfirmed approaches for managing a family enterprise, which the new generation of owners most likely wish to implement.

The family enterprise, according to Irena Bulat (FBC Family Business Development Center ASEE, 2014), can have several models of ownership transfer:

- Family transfer – a successful ownership transfer from one generation to another. A new generation of founders often holds the value standards of their predecessors and culture from which they originate. It is reflected in the continuity of work by the customers and suppliers, etc., of their ancestors. A new generation of heirs usually introduces smaller or larger changes in FC business activities.
- Insider purchase - this usually implies selling the company to the management or the employees. If the heirs are not interested in the company, there is a possibility for the company to be bought by the management or the employees.
- External purchase - selling the company to new owners.

## ***THE MOST SIGNIFICANT FEATURES***

In order to completely understand the problem of transfer of ownership from one family generation to another, the correlation between the family and their business must be understood. This correlation is depicted through the features of family companies. In the further text, some of the most significant features of the correlation between a family and business related to the various aspects of managing and the business activities of family enterprises will be reviewed.

Members of family enterprise are, due to family relations and common business interests, usually loyal to each others. Occasional conflicts and misunderstandings regarding the managing of the enterprise are secondary compared to the family business and family relations. Managing of the enterprise is based on family consensus and the main priority of a family business is the

development of the family business and protecting personal property. The business policy is based on safeguarding the long-term interests of the family which gives a special stability to these enterprises in comparison with their competitors, especially in times of turbulence. According to the research by KPMG and Family Business Australia (2013) 83% of the respondents believe that a family business and family way of business activities help to attain economic stability.

According to the Family Firm Institute, Inc. (2014), the basic features which depict the most successful FC business activities are the following:

- Optimism of family members - most family members believe that a family will retain control over a family business in the following five years.
- Loyalty, based on blood and family relations.
- alertness based on the trust that family members will take care of family funding.
- Competitiveness.
- Innovations.
- Agility.
- Dedication and a desire to create a legacy for future generations.

In their research, IFC (2011) noted that FCs have strong as well as weak sides. Numerous FCs are not sustainable in the long term. Two thirds to three fourths of all FCs fail or are sold by the owners. Only 5%-15% of family owned companies survive to the third generation of an ownership transfer. However, the numerous deficiencies of FCs can also pertain to other SMEs. They too have strengths and weaknesses, as follows:

Strengths:

- Dedication of the family to the preserving and progress of the family business. This is the reason why family members identify themselves with the enterprise, working hard and reinvesting part of their salary into the company.
- Continuity of knowledge. The family has a priority of transferring their accumulated knowledge, experience and skills on to the next generation.
- Reliability and pride. The family business is connected to the family name and the reputation is linked with their products and services.

Weaknesses:

- Complexity. Managing a FC is, from the standpoint of management, more complex in comparison with the other companies. A crucial problem in the management of enterprises is the link between the family and the company. Family members take up various positions and have different roles in the management and leadership of the enterprise. Their status in the family and in the enterprise are not necessarily equal.
- Informality. Considering that they have the feeling that they are managing their own business, family members pay attention to formalizing relations and following procedures. If a FC grows, there can occur a problem of an

inefficient managing of larger and more complex relations, which if escalated, can be a serious threat to further growth and business development.

- Lack of discipline. Numerous family members lack to synchronize their decisions with the chosen FC development strategy. It is customary that influential family members are more interested in employing their relatives than engaging a skilled workforce from the labor market. This fact leads to a work inefficiency and nepotism.

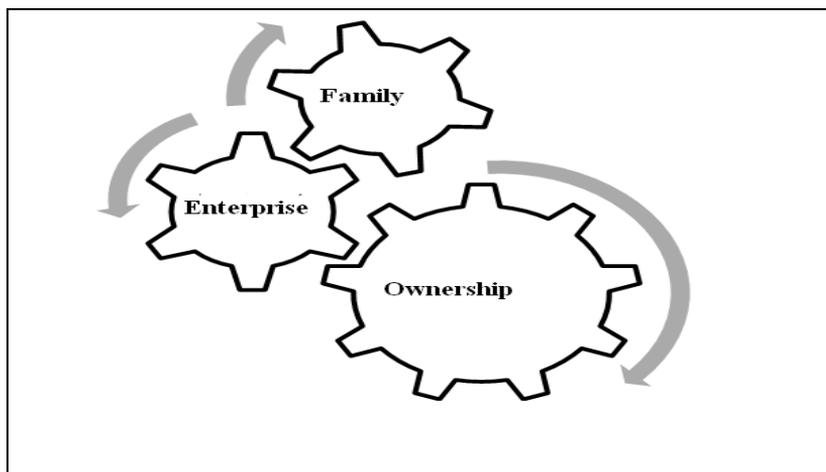
Research conducted by KPMG and Family Business Australia (2013, p. 10) states that private enterprises have the following competitive advantages in comparison with other enterprises:

1. Mutual values and a code of ethic.
2. A strong network of family members support.
3. Vision and strategy.
4. A strong brand and participation on market.
5. Customer service.
6. Possibility to make decisions rapidly.
7. Possibility of long-term perspective.

The basis of the relationship between family and their business is the complex correlation within the family, ownership and the enterprise (Figure 4). Thus, there are three dominant perspectives for an analysis, these being the following correlations:

- Family-ownership. This correlation implies the link between personal funding and that of the enterprise.
- Family-enterprise. This aspect analyses two dynamics of the development of biologic heirs through forming family relations (sons-in-law, daughters-in-law, heir of the second line, etc.) with the dynamic of the family enterprise.
- Ownership-enterprise. This aspect is engaged in the problem of inheritance of the ownership and enterprise managing.

Even this aspect is crucial for this paper, although all three mentioned aspects have to be observed jointly. A change in one aspect of the correlation impacts changes in the other two segments.



*Figure 4: The connection between family and enterprise with finances and ownership*

*Source: the Family Firm Institute, Inc., 2014, p. 39*

Passing on the business reputation and the experiences of one generation to another can have very positive and significant effects, along with numerous problems. These are the following: a transfer of knowledge from one generation to another, an introduction of innovations and harmonization of the FC with changes in the environment, using the reputation acquired by older generations with suppliers and customers, etc.

Due to preparing heirs to take over a private enterprise, older generations usually invest a lot of effort and time to transfer their management experiences to their heirs. With some business activities, this can be a significant way to create a competitive advantage.

Growing up in an environment of a family business, the new generation of heirs perceives the needs for harmonizing the enterprise with the new market requests. While older generations are more interested in the traditional leading of business, younger generations are prone to introducing innovations in their businesses.

The reputation which an entrepreneur enjoys can make it significantly easier to introduce a young generation into business without the customers fearing any changes in business conditions or the quality of the products and services. The same attitude is related to the correlations with the suppliers which together makes a financial position of a FC more stable. This resolves the numerous problems which entrepreneurs face during enterprise start-up.

Family enterprises can usually count on the financial help of family members. In the situations when entrepreneurs are starting a new business, this sort of help is especially significant, considering that newly-founded enterprise have insufficient funds for normal business activities, as well as no credit rating at business banks.

Due to years of familiarity long-term mutual family interests, the system of decision-making in well-organized FCs can be faster than in other economic entities of the same size.

Along with the significant positive effects of ownership transfer from one generation to another generation of heirs, there are numerous problems which should be solved in time and in an adequate way.

The dynamics of family development and the number of heirs can have a totally different development dynamic than the growth of the family business. Thus, it can happen that family enterprises, with time, have a smaller number of heirs or even no heirs at all. The successors which are not family members or are more distant relatives may not see themselves running a family business when inheriting ownership shares in a family company. When the number of heirs grows, then the ownership share of each member decreases. It could happen that in time a part of the ownership share which a family possesses starts to decrease and thus, a major family owner becomes a minority shareholder. In any case, the bigger the number of heirs, the larger the problem of managing a family business is.

The direction of family business development is an issue which can be a potential problem for forming the long-term policy of the enterprise. Different family members or even different family divisions can have varying interests and visions about the development of the family business. In these situations, the problem how to make decisions about the strategic direction of family business development arises. The decision about the development direction is usually made collectively or is made by the family member with a major ownership share, in consultation with other family members. Family businesses last until there is harmony in the family and until it is possible to find a common interest.

A long-term family interest can be in conflict with the personal interest and ambitions of one family member. It has been established that a major long-term interest of the family members is continuation and improvement of the family business and property. However, the personal skills of one member can be out of proportion with his/her personal ambitions. If an individual, as a family member, has limited mental and physical abilities for managing the enterprise, making him or her the manager of the family enterprise can endanger the company, which is a common occurrence. Inheritance law has minimized tensions in struggles for power, but it has also imposed the question of who will operatively manage the state or the enterprise. During the history of operational management, persons which have managed and provided the normal functioning of the enterprise and/or the state have been chosen.

The issue of professionalizing manager positions and nepotism is ever-present as the conflict in the choice of family members and engaging professional managers. If there are no clear rules, FCs could become social institutions in which members air their unresolved social problems. During the choice of staff, families may prefer their relatives, instead of experts. As additional problem could be rewarding family members instead of other employees, due to a lack of any criteria.

The problem of separating or inheriting FCs is especially sensitive. Family circumstances and problems, separation, divorce and inheritance are linked with ownership distribution in FCs. With the breaking up of a part of ownership, there is always the issue of financial as well as strategic nature. How to separate property and not imperil the entire business entity? In some countries, inheritance rights are separated according to gender. In contemporary economies, inheritors of different genders have the same inheritance rights.

In the case of managing a family enterprise, it is difficult to distinguish personal from family finances. Thereby, financial problems are transmitted to the personal sphere due to bad business-conducting.

The family is the owner but also often the participant in managing these enterprises or the executor in regular business activities. Top management positions are usually taken up by prominent family members. In a large number of cases, especially within SMEs, family members manage and work in the same enterprises, which means that family members are also in the structure of the ownership and the managerial structure.

Family members can be engaged in family enterprises in the following roles:

- Owners (a minimum 20% in the structure of the capital with two owners).
- Managers (not compulsory).
- Employees (nor compulsory), whether as family members (in entrepreneurship), temporary employees or employed on contract.

Professor Walter Zoki, the department chair of the Strategy and Control of Family Businesses and a consultant describes it quaintly as sitting at four tables. The first table are the owners, that is the stakeholders, who together with the other co-owners establish the FC strategy. The second table are the board of directors, with the representatives of the owner structure or the co-owners themselves (although it is unnecessary for all of them to sit at the table). The role of the board of directors is to carry out strategic decisions and protect the long-term interests of the owners. The third table is the manager team which manages the FC operationally. The fourth table are the supervisory board members. Their role is to control the work of the managers, supervise the carrying out of the decisions and whether the company is conducting business within the confines of the law. If the same people sit at these tables, a confusion regarding authority is inevitable.

In order for the FC to do business successfully, the roles must be defined. The most important matter is to define the owner and the operational FC manager. The system of decision-making and authority must be clear or otherwise the FC can have problems making decisions and managing. The larger the enterprise, the greater are the needs for professional managers to manage the business. This fact separates the roles of owners and professional management all the more.

This process is shown in Figure 5. The smaller white circles symbolically represent the owners and the larger black ones the business itself. At the beginning of the process, when the enterprise was founded, the owner and the enterprise coincide. With the growth of the enterprise into a complex business system, the

demands for management and development of a business system surpass the mental and physical abilities of the entrepreneurs, and thus professional management is engaged. In the situations when the FC becomes a large enterprise, the owners increasingly start to get involved with social and humanitarian work, promoting enterprises and family values.



*Figure 5: Separating ownership from the function of management in SMEs.*

*Source: Churchill, Lewis, 1983*

In the beginning stages of developing, FCs belong to SMEs. The essence of the problem of separating ownership and management in SMEs is introducing professional management into the companies where there are certain prerequisites.

### ***THE ISSUE OF OWNERSHIP TRANSFER***

Even though family enterprises are a usual occurrence everywhere, there are many stereotypes about them. Many consider that they rarely survive more than three generations. According to this stereotype, the first generation creates an enterprise which is successful. The next generation uses the benefits and the third one is left with nothing, and must start from the beginning. From the point of view of strategic managements, this is a failure.

A family develops a model of a life cycle of a family enterprise through many generations. The mentioned model represents a recognizable predictable model in family enterprises during time, which can be used for long-term planning of the development of a family business, where ownership transfer is one of the main issues. The long-term strategic planning of a FC is based on the idea of knowing the basic FC life cycle mode, and creating the activities to create the desired future of the family business (Ward, 2006).

Ownership transfer from one generation to another implies much more than ownership transfer in itself. Except for inheriting a market share, the successors gain several material and non-material uses from the life experience of the older generations. The following generations of successors of the family business, except property, also gain the knowledge on how to lead and survive a business, as well as benefit from a reputation with other interest groups on the market such as suppliers, buyers or financiers. Also, the new owners are faced with the problem of introducing innovations and changes in business activities in order to adapt to changes in the environment. This from one side represents a potential crisis but also a way in which an enterprise can adapt in the long term to environmental changes through a business vision of the new owner generation. A change in

ownership thus represents a moment of crisis in the development of enterprises as well as a chance for enterprises to be revitalized and directed towards new business directions. In this way, a fundamental flexibility in strategy management can be achieved.

IFC (2011) defines the life cycle of an enterprise through ownership transfer. It records three stages in the life cycle of a FC:

Stage 1 – The founder (or founders). This implies owner control.

Stage 2 – A partnership of brothers and sisters.

Stage 3 – An alliance of relatives.

Table 1 presents the issues and problems faced by owners in life cycle stages:

*Table 1: Key issues linked with FC management according to their life cycle stages.*

<b>The stage of a life cycle of ownership transformation</b>	<b>Dominating owner issues</b>
<b>Stage 1. Founder (or founders).</b>	<ul style="list-style-type: none"> <li>• Leadership transformation</li> <li>• Legacy</li> <li>• Planning property</li> </ul>
<b>Stage 2. Partnership of brothers and sisters.</b>	<ul style="list-style-type: none"> <li>• Maintaining teamwork and harmony</li> <li>• Sustaining of family ownership</li> <li>• Inheritance</li> </ul>
<b>Stage 3. An alliance of relatives.</b>	<ul style="list-style-type: none"> <li>• Allocation of corporate capital: dividends, loans and profit levels</li> <li>• Pay-out of dividends to capital owners</li> <li>• Resolving family conflicts</li> <li>• Participation of family and their roles</li> <li>• Family vision and mission</li> <li>• The link between family and the business</li> </ul>

*Source: IFC 2011, p. 16*

In literature, there are several works which mention the model with three more or less same stages in the life cycle.

The paper will present the model presented by Ward (2006) with four stages, of which the first three are the same. He claims that FCs have four stages of life cycles which they pass through:

Stage 1. The company managed by the entrepreneur as the owner.

Stage 2. Partnership of brothers and sisters.

Stage 3. An alliance of relatives.

Stage 4. Long-term perspective.

### ***STAGE 1. THE COMPANY MANAGED BY THE ENTREPRENEUR AS THE OWNER.***

Entrepreneurs found their enterprises in order to carry out their business idea. An entrepreneur identifies himself and his idea with the fate of the enterprise. When the demands of the enterprise exceeds the possibilities of the entrepreneur, it is necessary to leave the work to professional management.

With the growth of the business, the entrepreneur first engages his family members, the work force from the labor market and after that professionals in order to secure a long-term business success. The family forms its value system which it conveys to the enterprises, and which is the basis of the reward system of all the members. In order to motivate the professionals who come from outside and are not family members, the family is given the possibility of acquiring wealth. The conducted research (Family Firm Institute Inc., 2014) points out that the reward system for working in FCs is less stimulating than in other enterprises.

Successors are taught about family values from early childhood, whereupon the family is in the first place and business in the second. They are first trained in formal education and later on acquire practice in their family business. A significant part of the education system are representatives of the older generation which spend a lot of time in contact with the young people in order to convey knowledge and experience in business conducting.

If they achieve success in business, the older generation feels it is their commitment to educate the young family members of the future generations how to behave with family wealth. The problems which occur in personal lives and the functioning of the family are passed on to the business of the private enterprises, and this is the reason why a family takes care of each member, even getting involved with the private problems of individuals. At times, the border of involvement into privacy is hard to gauge.

## ***STAGE 2. PARTNERSHIP OF BROTHERS AND SISTERS***

After inheriting the ownership share, family members who have the same values and similar interests continue to cooperate, motivating other successors to sell their shares and leave the family business. However, there is an endeavor for the family to buy off the company shares in order to retain majority management rights.

The members who remain in the family business invest jointly in business but also family members. Investment activities start to appear within the community, as the family and enterprises support and help one another.

The family endeavors to ensure that the most competent family members are involved with the business. In order to reduce taxes and achieve significant results, owners start to hand over a part of their ownership to their children and grandchildren. FCs are, with the enlarging of wealth, significant philanthropists, donating significant funds to social and humanitarian causes within their community (Family Firm Institute Inc., 2014).

With the aging of the second generation of successors, the educating of the following generation begins. Parents introduce them to enterprises early on in order to motivate them to acquire formal as well as practical experience. However, they do not exert any pressure on their heirs to commit themselves to continue the family business.

The family makes sure that its members in the early years have ‘rainy day’ funds and retirement. This in a certain way is also accomplished by the FC “reserve financial fund”. Siblings make agreements regarding further investing into good opportunities.

Families carefully instruct their spouses, which are not blood relations, in the areas such as family values, culture, the nature of work, family agreements and conflicts, etc. Thus there is acquired support of the spouses and their eventual tutoring of the children until they become independent and until they start to manage the family business on their own.

The values fostered by the family are from the beginning installed into the successors and enterprises, as a part of the organizational culture. In order to centralize the decision-making system, the family sets up a central personality, which has the greatest trust of the majority of family members. Such a person is viewed as a leader of the entire family, taking care of the interests of all the family members. Except for the role of the central figure or the pillar of the family, this person also plays an important emotional role for the family. The central figure has certain commitments, such as maintaining contact with relatives which are not blood relations, the media, the community and others. This is a respected person who represents the family and its interests to the world but the family as well. In the case of family conflicts, this person should be the reconciler for the conflicted parties and a possible arbiter.

### ***STAGE 3. COOPERATION BETWEEN RELATIVES***

Even though they are not blood relations nor do they belong to the cultural milieu of the family, relatives may alter the culture of the family and the enterprise and thus they contribute to the family and the family enterprises to become more flexible. Their influence can to a large extent contribute to strategic changes in business.

If these changes are accepted, they can inspire family members to deal with new jobs and turn to new entrepreneurial ideas. This in turn stimulates new endeavors, useful in the commercial as well as social sense, which helps to integrate new family members and create a feeling of unity and dedication to family. The changes incurred and a new common dedication to work creates the success of the family, which in turn creates the conditions for a further increase of wealth and social respect from the community members. A feeling is created that “this company will last forever.” All the family members do not fare equally well but the family helps to learn about business and capital management within the family.

The family enables a free sale of shares to all the family members equally, under certain conditions and at fair prices. With the growth of the business and separating ownership from the management, the capital owners experience the family business less as a profit-making vehicle and increasingly endeavor to develop an entire family business system.

Family meetings are organized on a regular basis, in the interest of the family. New members are from an early age taught about ownership responsibilities, from knowing the business, finances and reporting to management. Spouses are often included in these programs.

Family members try not to get involved in the operational managing of the FC, as they support the adopted strategy and act as cultural ambassadors. They support their management in the function of managing the FC.

Family members are trained in three basic areas:

- Communication skills, necessary for managing the growing business.
- Personal growth and development, through formal education.
- Family culture and tradition.

Family and relatives experience the role of the family leader as being very significant. The family leader can be a respected member of the group of family members (larger families). His role remains more or less the same, to take care of all the family members as well as the family business. His role is also to offer help to family members who are in trouble, the causes of which can be purely personal reasons or some special needs (illness, addiction and similar). The politics which the family leader takes up is conveyed to all the family members, and must be adhered to. Each family member is considered equally significant and valuable.

The family devotes increasingly more time to humanitarian work, and family members not in the FC structure are also included in these activities, as family cohesion is thus maintained and the power and status of the family is demonstrated to the world.

Relatives understand that occasional rivalries and conflicts are less valuable than the advantages and power which is enabled by the unity of the family and its support, and

thus they contribute to reducing the tension among the conflicted sides in the family. This helps to placate the conflicts among blood relatives and increases family cohesion.

Family members attempt to define the family mission separately from the FC. This enables the family members to strengthen their dedication to the family and the FC, also enabling the family and the FC to review various options of further development. Family values are conveyed to the institutions established by the family, as a result of their social and humanitarian work, such as foundations, endowments, and similar.

The conviction of family members that the company is a means for achieving the common good increases which serves to further increase dedication to the family and its values.

The process of maintaining continuity becomes especially significant, as it helps to coordinate personal attitudes and interests with long-term family attitudes. An individual learns how to work and think as a member of the team (group). In this way, every family member matures through the process of continuity and decision-making, learning how to become a respected family member.

Respected and appreciated families start to share their enthusiasm and knowledge about the family business with other families and its members.

#### ***STAGE 4. A LONG-TERM PERSPECTIVE***

Families which understand and embrace the challenges posed by time increase the chance to increase the continuity of the family and the family business. This need for change and adapting is characteristic for all families which endeavor to preserve the essential values of the family. Furthermore, each family experiences values in their own special way.

Even though there is trust among family members which originates from childhood, it is also necessary to take into consideration the opinion of experts, who view the situations from different angles. All families have problems which are more or less the same and thus predictable. Consequently the help of expert consultants is essential and can help to overcome problems more quickly. It is equally important that there are different views and perspectives of viewing the problem and solution, as is the fact that family members need to rise above their personal opinion and bring a decision which is in the long-term is acceptable for all members.

Two things are relevant in this process: communication and the decision-making method. Communication is essential for the exchange of information on the attitudes of the other side and the possibility of presenting the personal attitudes of the other members. The possibility of understanding and accepting other perspectives and attitudes is the second part of this problem. If the participants in decision-making are prepared to accept other attitudes as well and not just their own, there is a possibility to arrive at a sustainable solution which is acceptable for everyone. Furthermore, the final solution does not necessarily have to seem like the solution which all the parties had at the beginning of the negotiations.

Key for long-term planning is sustaining continuity. Planning in this stage is carried out on the following levels:

1. A business strategic plan.
2. A plan on inheriting, leading and ownership in the family.
3. Personal financial plans of family members.
4. Plan of family continuity.

### ***KEY SUCCESS FACTORS OF OWNERSHIP TRANSFERS***

According to Srisomburanant (2004) many consider that an FC depends on the competence of family members, their dedication and hard work, which is only partly true. For the family, it is important to maintain its business in the long term. Reducing the impact of all the external and internal factors which can disable a successful transfer can be achieved by three approaches:

-The existing of awareness about negative feedback and corrective activities. A negative feedback is made up of three significant dynamic forces:

- The ability of managing a FC by family members. During time, the possibility of the family to efficiently manage and control the business is continuously falling. As a result of the limitations which occur with the possibilities of the family to manage complex work demands, there occurs a tendency of stagnation which reduces the work volume and raises it to a level which family members can manage.
- Organic forces. The negative impact is reflected through loss of flexibility due to an increase of bureaucracy which ensues from the growth of the organization. The more an organization works to raise its efficiency, the more grow the needs to define the work method, which has the negative consequence of reducing organization flexibility.
- Work complexity. The growth of the FC also impacts the growth of the business of the enterprise. Work diversification leads to an increase of its complexity. This opens the issue of the efficiency of the entire organization.

- Corporate management.

- Professionalism.

The same source claims that for a successful ownership transfer, the following should be prepared successfully:

- The next generation of successors, for taking over the family business.
- Securing a large dedication to family tradition, values, loyalty and hard work of all the family members and especially the successors.
- A successful business transformation. It secures the adapting of the FC to changes in the environment. One of the main causes of the disappearing of FC enterprises may be organizational inertia which is deeply ingrained in the processes and organizational culture of families.

## ***CONCLUSION***

The development of FCs makes up a great part of the total number of SMEs with their specific features. The research conducted points to the large significance of FCs for the economy and development of the entire society. In spite of this probable fact, the state fails to adequately follow the problems of FC development.

With every ownership transfer, the number of FCs is reduced by about 50%. Thus, every third generation of successors has only 25% of the total number of SMEs, which is why the number of FCs in the world is relatively low, even though their success and impact on business trends is significant. Sustaining a family business through the generations is considered to be a large challenge.

One of the key issues linked with the managing of FCs is the separating of ownership and the managing function during a life cycle. In the families where there is a strong combination of family and ownership relations, traditional family values can be a big burden for the necessary changes in business and managing a FC. The traditional values are confirmed by business results from the past and are used as an adequate way of thinking about the future.

Viewing matters in the long term, the family with their values represent a force which directs the family and its business in the same direction. On the other side, changes in the size of the organization and the business environment of the enterprise demand other changes. Coordinating these three antagonistic forces can be achieved by a successful preparing of successors which will accept the basic interests of the family but at the same time seek new work methods and businesses which will correspond to the demands of the new age.

According to Miloš Švarc, a consultant at the Center for Developing Family Companies ASEE (2014), the owner can save his/her FC by long-term planning the development of the enterprise, whereupon the issue of ownership transfer to the next generation of owners is one of the most important issues. In order to realize this successfully, it is necessary to plan the following for the ownership transfer process:

- The company for future changes.
- The successors for taking over the FC management.
- Oneself, as the owner, for the future ownership transfer. Every owner has a difficult time, emotionally speaking, with ownership transfer.
- The family, for the new owners which will take over the managing of the family and the FC, introducing the necessary changes.

## ***PROPOSALS FOR APPLYING RESULTS AND FURTHER RESEARCH***

Due to an obvious large economic and social significance which FCs have for the development of society, it is necessary, from the standpoint of various interest groups, to carry out the following activities:

1. To be carried out by state institutions and the local self-government:

- Recording and statistical following of the growth and development of family enterprises.
- Periodically carry out research of the problems faced by the family enterprises.

2. To be carried out by educational institutions and entrepreneurial associations:

- Promote family enterprises.
- Train entrepreneurs for ownership transfers.
- Stimulate long-term planning of enterprise development.

3. To be carried out by entrepreneurs in family enterprises:

- Attend courses on the methods of ownership transfers in family enterprises.
- Plan the activities of long-term development of enterprises and ownership transfers.
- Carry out specific activities according to plan.

Perhaps the most important advice which can be given to entrepreneurs is related to the fact that they should acquaint their successors as children with the values and attitudes of the family and the business. By getting to know the work of FCs, the new generations can assimilate the knowledge of the previous generations and acquire their own knowledge.

Medelsheim, in his thesis (reprint of the 1929 issue) gives advice for FCs which deal with trade. As the advice is of a universal character, it can be applied to all FCs regardless of activity. Some of the activities which can be applied to entrepreneurs for preparing the new generations of successors are the following:

- If your children show any interest in business, let them work for others. This is the way for them to learn about discipline and work. Also, they will see other work methods as well, different from yours.
- Allow your children from their young years to be present in your business space, shops, workshops, offices. Ask them if they are interested in seeing anything or having something explained to them other than what they have seen or heard. It may be the case that they will be in the way but this is the best way to stimulate your children's interest for the work you do.
- Teach your children to respect your vocation and be proud of their parents. In this way you can stimulate their ambition to take your place one day.

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# **THOUGHTS ON ENTREPRENEURSHIP AND ITS LINKAGE WITH INTRAPRENEURSHIP: IMPLICATIONS FOR ECONOMIC DEVELOPMENT**

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## **ABSTRACT**

*An entrepreneur is someone who is willing to bear the risk of a business venture where there is a significant chance for making profit (Chell, Ozkan, 2010). This is particularly where the opportunity comes from outside of the enterprise. Entrepreneurship is basically the practice of starting a business in order to earn profit on new found opportunities (Ercan Ekmekcioglu). Generally, “entrepreneurship represents a wide area for various business moves where the entrepreneurial activities take place. How entrepreneurial activities would develop and whether their result would be positive or negative depends on many factors that determine the development of those activities” (M. Radović-Marković, Muhammad Omolaja, 2010). Alternatively, new businesses that are developed within a company under the influence of permanent efforts of entrepreneurs for changes in existing organizational structures are called intrapreneurship. In other words, intrapreneurship represents restructuring of existing enterprises. Accordingly, it can be said that there are two ways of developing entrepreneurship; that is, establishing a new one and restructuring an existing enterprise in a process known as intrapreneurship. However, what are the alternative views on the theory of entrepreneurship? Is there a linkage between entrepreneurship and intrapreneurship? How does this linkage affect economic development? Provision of answers to this kind of questions is the core of this paper.*

**Key words:** *Entrepreneurship, Intrapreneurship, Economic Development, Innovation, Business Ideas*

**JEL Classification:** *L26, G34, O31*

**UDK:** *005.591.1 005.346 005.961:005.914.3*

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## ***INTRODUCTION***

Entrepreneurship and intrapreneurship have many uncertainties especially when new products are created for which there is no existing market. Both collectively affect economic development in many ways. It is through both entrepreneurship and intrapreneurship that important innovations enter the market leading to new products or production processes which eventually increases efficiency or productivity through bringing competition in the market places. This paper discourses the nature, types and forms of entrepreneurship and intrapreneurship as well as their linkage and their impacts on economic development. It also illuminates the ideas and concepts that emerge from entrepreneurs increasing our knowledge and what consumers may prefer through introduction of variations of existing products and services in the market. This speeds up innovations pertaining to introduction of new products in the market as a result of longer working hours and more efficient nature of entrepreneurs as their income is directly linked with their working input. Entrepreneurship and intrapreneurship lead to introduction of new goods with new quality and value. Their innovativeness introduces new ways of production and new markets that have not been exploited. It is through entrepreneurship that new source of supply are discovered and influences creation of new business organisations that directly affect the economy. Creation of new business opportunities through entrepreneurship, intrapreneurship, productivity and innovation leads to economic development. This therefore means that when there is more entrepreneurship and intrapreneurship innovation in an economy, it will be accompanied by high rate of economic development.

## ***DEFINITION OF ENTREPRENEURSHIP***

The first attempts at defining the basic meaning of entrepreneurship go back to 16<sup>th</sup> and 17<sup>th</sup> century. It was not until the 18<sup>th</sup> century (specifically, 1725) did Scottish economist, Cantillon (1725) gave the first significant contribution to understanding what it means to be an entrepreneur. *Cantillon*, in his definition, however, described the functions of entrepreneur, rather than his personality. In those days, the classic entrepreneur was a farmer, who was willing to take on business risk despite uncertain climatic conditions and other variable business circumstances. Later on, this concept began to expand to independent traders, where more and more, the role of entrepreneur as a leader and a promoter of “everything new” in the business were recognized.

Adam Smith considered a case of capitalist who lent his money to other people and so recognized the special function of people who take on the use and risk of capital. The famous economist John Stewart Mill also noticed that taking risks should be a part of entrepreneurial function. Say in 19<sup>th</sup> century (specifically, 1803) in his book "Tractate of Political Economy", emphasized the importance of entrepreneurs. He defined an entrepreneur as "a person who moves economic resources from the area of lower to the area of higher productivity and greater profit". Namely, Say defined the function of entrepreneur independently of a social framework and did not include risk taking in the definition. On the other hand, Knight in 1921, established his definition of entrepreneurship on the basis of risk and insecurity. In his opinion, goods are primarily manufactured according to personal motivations, and not according to manufacturers' wishes; the manufacturer takes the responsibility of anticipating the buyers' wishes. This definition was heavily criticized by the Austrian economic school, lead by the famous scientist Schumpeter.

However, the first universal definition of entrepreneurship was developed in the 20<sup>th</sup> century. It was given by Schumpeter (1934), and it emphasized the role of innovation and creativity in entrepreneurship. In Schumpeter's interpretation of entrepreneurship, all firms, which tend to innovate, introduce one of the following new combinations: new products or services, new production methods, new markets, new resources, and new industrial organization. Unlike Schumpeter's definition, there is a group of definitions which assume that entrepreneurship is related to the decision-making process and the development of profitable businesses. This conceptual description of the essence of entrepreneurship is more precise than Schumpeter's definition and is regarded more acceptable. Despite that fact, this definition has certain weaknesses, primarily because it does not include the basic indicators for determining how and under what conditions a business activity should be started.

Huge number of entrepreneurial theorists tried to present economic theory based upon "rational postulates of human behavior" after Schumpeter and to synthesize selected theoretical contributions in this area. Scientist Casson is especially distinguished among these. He criticized the neoclassical economic school for the fact that it has demonstrated extreme subjectivism, which has been transferred to entrepreneurs and does not enable them to realistically anticipate the future. According to Casson, Schumpeter's, Kirzner's, Knight's and Hayek's theories are, although different in some aspects, are very much alike. Casson believes that "entrepreneurs have more relevant information than other people and are always motivated by personal interests".

In order to simplify his theory, Casson (1982) focused on entrepreneurs sincere intentions to gravitate towards maximizing profit at given a amount of effort by conducting their business. Namely, the amount of entrepreneurial activity is closely related to amount of possibilities for making profit. Casson believes that an entrepreneur needs to have great number of specific personal qualities in order to make a successful business decision. He states some of the qualities (knowledge, imagination, analytical capabilities, researching capabilities and communication

skills). Some of these attributes he explains in detail, except for imagination to which he does not give enough emphasis. Beside those outlined by Casson, other scientists have added some other entrepreneurial attributes which are regarded as desirable. Brockhaus (1982), Gartner (1989), Aldrich, Zimmer (1986), Carson (1995) and Delmar (1996) have determined that key psychological characteristics of successful entrepreneurs are, readiness for risk-taking, ambition, optimism, willingness for independence and the need for power. Besides describing the attributes which may contribute to an entrepreneur's success, none of those mentioned any universal or common attributes of successful entrepreneurs.

## ***THEORIES OF ENTREPRENEURSHIP***

By reviewing the great number of theories and approaches, it is crystal clear that it is not simple to answer the question of what entrepreneurship is and how to distinguish one definition as the most universal. Perhaps one of the most universal and, accordingly, the most acceptable definitions is the one given by the American economist R. Hisrich (1985). According to him, entrepreneurship is "a process which consists of creating something new which needs time and huge effort, while psychological, financial and other types of risks are taken, and material satisfaction is returned". Beside the Hisrich's definition, there are also a number of contemporary approaches that have contributed to the theory of entrepreneurship. Stevenson and Stahlman have systematized these theories from the last two hundred years in an excellent manner. In 1987, they systematized these theories in three basic groups; that is, theories that regard entrepreneurship as an economic function, theories that define entrepreneurship from an individual aspect, and theories that define entrepreneurship from a behavior aspect.

So, while some theories are based upon economic functions, others are based upon researching the individual characteristics of entrepreneurs in trying to understand and explain entrepreneurship. The other theories stress those personal attributes that only entrepreneurial people possess. The scientists' challenge from those theories is therefore to identify personal attributes that are unique to entrepreneurs, and to determine those attributes that play a key role in a successful entrepreneur. This approach includes the psychological, sociological and anthropological aspects of entrepreneurship. In the newer theoretical considerations of entrepreneurship, Delmar's (1996) theory stressed that earlier behaviorist approaches are incomplete because they mainly focus on those entrepreneurs' attributes that are stable and are not subject to frequent changes. He gave his contribution to the contemporary theory of entrepreneurship, trying to integrate economic-psychological models of entrepreneurial behavior, by developing a model which is based on understanding the entrepreneurial behavior and environment, as well as determining their influence on entrepreneurial performances (the development of business and finances). "Entrepreneurial behavior is determined by individual differences like intellectual capabilities,

motivation and business characteristics". For those reasons, he represents the view that interpersonal and organizational approaches are very important to the understanding of entrepreneurship.

Some of contemporary entrepreneurship scientists have tried to explain small differences between entrepreneurship and marketing. Scientist Gartner stated his opinion that the development of entrepreneurship will greatly influence the development of marketing theory and practice. Also, in 1992, this scientist tried to demonstrate a difference between entrepreneurial and organizational behavior. For an organization, to be an entrepreneur means relating personal capabilities to the needs of the organization itself.

Meanwhile, despite the differences in definitions of the essence of entrepreneurship, the common theme in the majority of definitions is that entrepreneurship has creative functionality in the creation of new values by an individual or group of business partners. In addition, in most agree that there is a special kind of behavior which includes taking the initiative, taking the business risk, business creativity, and organizing and innovating in all aspects of the business where needed. A conceptual definition of entrepreneurship should consider that differences in the interpretations arose primarily because economists have different approaches to the matter than psychologists, sociologists or anthropologists. Consequently, the dominating approaches are economic, cognitive and behaviorist to entrepreneurship. Recently, organizational, marketing and financial approaches have also been added.

However, all of these approaches should be as integrated as possible in order to provide a complete understanding of entrepreneurship. Also, a conceptual determination and definition of entrepreneurship should study the way organizing and conducting entrepreneurial activities change over time. It should follow the changes in the roles and tasks of entrepreneurs as the main conductors of these activities, influenced by new flows of economic operation. These changes have occurred not only in the "new economy" on firm level, but also on the global level.

## ***TYPES AND FORMS OF ENTREPRENEURSHIP***

According to Carree and Thurik (2002), entrepreneurs in history have often been represented in many faces and assumed different roles. As identified by scholars such as Schumpeter, Kirzner and Knight, entrepreneurs can be termed as innovators, profit opportunists and uncertainties and risk takers respectively. Schumpeter drew his attention to understanding an entrepreneur as an innovator. As an innovator, the entrepreneur performs new combinations which Schumpeter called enterprises (Karlsson et al, 2004). An entrepreneur according to Kirzner perceived profit opportunities. This role is what was labeled Kirznerian entrepreneurship. The last role of an entrepreneur is that of assuming the several risks and uncertainties which may be associated with running a business. This role is labeled Knightian entrepreneurship. As the individual introduces a new product

in the market or starts a new business, this entrepreneurial role can be described in terms of the three labels. As posted by Audretsch, Lehman (2005), the individual who launches a new firm or introduces new products can be termed as the innovator and he assumes that he has perceived a previously uncertain profit opportunity. The innovator also takes risks that the venture or the new product may eventually turn out to be a total failure (Todtling, Wanzanbock, 2003).

However, according to one of the classifications of entrepreneurship by professor Gartner (1986), we can distinguish eight different types of entrepreneurship:

- Presenting something new: here, the businesses are partially started and usually organized among family members and relatives with low degree of innovating;
- Business network development: businesses are connected through manufacturers, suppliers and distributors (different business aspects linking). Everything operates perfectly due to “the right” selection of all participants for business activities performing;
- Use of previous experiences, knowledge or business contacts: in this case, an individual has no long-term interest to start a new business, which relates to business risk. Therefore, individuals often start a business with little capital (usually their personal savings), spending very little time in sales analysis and marketing activities. Instead, they usually use previous experiences, knowledge or business.
- Buying a company: individuals may get interested in buying a developed company for running their own business. In this case individual’s attention is focused on finding business with the least business risk;
- Conducting expert investigation: when an individual is not able to estimate whether a business idea is good for the business or not, this is the approach. In this case, one should hire teams of experts for conducting an investigation, which should determine and present the validity of a new idea.
- Use of consulting companies services: an individual (small business owner) may use services of authorized consulting companies when employing and educating employees, giving expert advices related to various areas of business activities, etc.
- Paying special attention to one idea: in this case, the emphasis is only on the idea, which is not technically specified or is too complex to be implemented easily. Regarding the fact that it has special quality, it demands hiring experts and production of a report. Such expert opinion should be used as a basis for development of, usually, a long term business;
- Development of adequate methods for new business organizing: An individual (owner) is using various, well-known methods of business planning, with intention to use them as a basis for creating his own method. In addition, he is being acquainted with necessary details that are important for starting a new business.

In general, entrepreneurship represents wide area for various business moves where the entrepreneurial activities take place. How entrepreneurial activities would develop and whether their result would be positive or negative depends on many factors that determine the development of those activities. However, the most relevant factor are economic environment, political conditions, technical-technological level of development achieved and cultural environment. General social and personal context are closely related and therefore they have common influence on performing suitable entrepreneurial activities. While on one hand entrepreneurial activities change resources giving economical, political and social contribution on local, national and state level (products, services, export, etc.), on the other hand, economic conditions are especially important for development of new businesses, including available capital and high-risk investment.

Considering that the largest number of business is financed from entrepreneurs' personal resources (savings, loans, etc.), their family members or close friends, tax policy plays a significant role in starting and developing a new businesses (Birley, 1988), as well as economic conditions (country's economic stability, benefits when applying for credits, etc.). Availability of capital, resources, large goods and services markets, represent possibilities for gaining money and appear as significant variables, which include perception of market conditions, risk degree, unemployment rate, transporting costs, life standard, etc. The size of market is a variable that is directly related to industry and new businesses and it includes appropriate market structure – the number of vendors and customers, differentiation of products and the degree of vertical integration, as well as market development rate (Sandberg, 1986).

Social system, cultural environment, political and other conditions, under which an entrepreneur starts new business, influence whether the new business will be successful or not. Namely, the conditions for starting new businesses vary from national and geopolitical, to industrial, governmental and cultural factors. These differences may be considered when we explain difficulties, which encounter those who create policies for favoring the development of new business and entrepreneurial activities.

## ***DETERMINANTS OF ENTREPRENEURSHIP***

There has been a wealth of knowledge on the determinants of entrepreneurship over the last few decades. Although studies bringing forth this knowledge have rather been based on theoretical grounds, others have been drawn from empirical evidence. Scholars have also been keen in investigating the impact of entrepreneurship in relation to economic development which has further led to the explosion of extensive literature in this field (Van Stel, Carree, Thurik, 2005). It is important to note that a significant amount of existing literature has been based on the observation of firms, establishments and regions in terms of their economic performance, development and survival. The facts that can be derived from these studies link economic development with the size and age of the firm or an

establishment. According to Van Stel, Carree and Thurik (2005), newly established firms and very small firms experience systematically faster development compared to the already established larger firms.

These findings have been found to hold in the modern industrialized economies as well as across time periods (Karlsson et al., 2004, p.3). The connection between entrepreneurship and economic development measured in terms of performance of the firm has been extended even beyond observing the establishment to accommodate geographic regions. This paper discourses how entrepreneurship can be related directly economic development and how entrepreneurship is at the heart of economic development of any nation. Entrepreneurship is a challenging task as many businesses which start fail to take off

## ***THE CONCEPT OF INTREPRENEURSHIP***

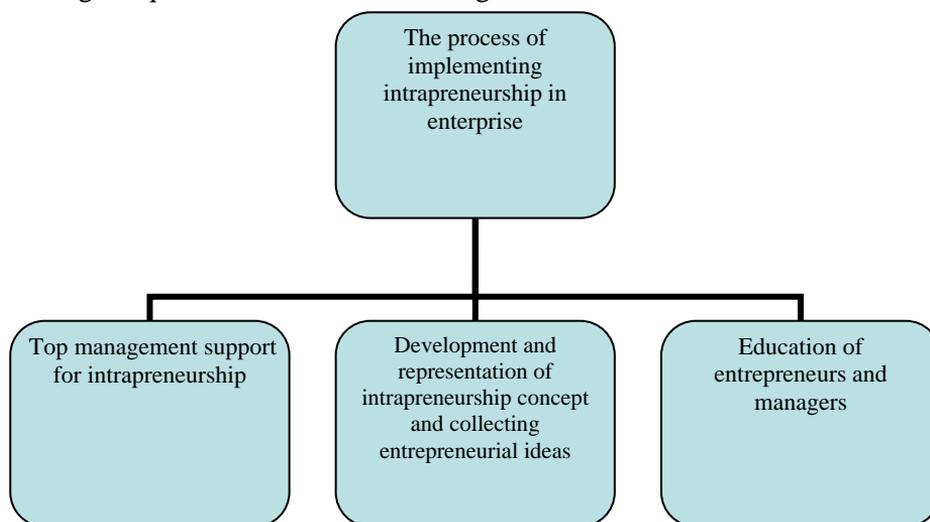
As a consequence of social and economic trends in many countries, which appear due to fast marketing changes, there has been increasing number of new businesses, both inside and out of existing organizational structures. New businesses that are developed in a company under the influence of permanent efforts of entrepreneurs for changes in existing organizational structures are called intrapreneurship. In other words, intrapreneurship represents restructuring of existing enterprises. Accordingly, it can be said that there are two ways of developing entrepreneurship; that is, establishing a new one and restructuring an existing enterprise in a process known as intrapreneurship.

Intrapreneurship is becoming the main component of existing enterprises' development, which rose as an efficient answer to new challenges and extremely competitive environment. Namely, for a company, in order to encourage entrepreneurial spirit and creativity, it is necessary to develop appropriate organizational structure. What it would be like or would it be able to change and adapt itself, largely depends on existing business climate in a company. In other words, where traditional management dominates, hierarchical structure will develop more strictly, with main goal to cut down the business risks. In this manner, good business results are achieved in shorter time. On the other hand, creativity and flexibility of a company are reduced. Due to that, most companies demonstrate the need for intrapreneurship development, in order to create good conditions for encouraging development of new ideas, elimination of bad and attractive jobs expansion, teamwork, long-term planning, adequate rewarding system and motivating the best individuals, as well as providing the support of the top management.

Introducing intrapreneurship has great benefits because of the use of existing technological base, developed marketing network as well as the employees who know one another well and who had developed good relations. Besides all these advantages of intrapreneurship, it demonstrates certain disadvantages, primarily concerning great dependence on environment and needs for all employees in organizations to be convinced in validity of new ideas and the need for their implementation.

## ***IMPLEMENTING INTRAPRENEURSHIP IN ENTERPRISES***

For implementation of intrapreneurship process in an enterprise, it is necessary to secure systematic realization of several phases of this process. As shown *Fig. 1*, the first step in the process of intrapreneurship implementation in modern day enterprises is providing support of the top management and mid-level management. Without it, organization will not be ready for all the changes related to inner transformation and restructuring of the company. One of the necessary initial frameworks of new business concepts, in order to identify, select and train the leaders of intrapreneurship, is development. This training should point out providing adequate human resources in organizations.



*Figure 1: The Process of Intrapreneurship Implementation Enterprises*

*Source: Adopted from M. Radović-Marković, Muhammad Omolaja (2010), Modern Entrepreneurship: Concepts, Practice and Innovations)*

During the training, it is necessary to develop mentor work, as well as to provide sponsors for it. Without sponsors, there is little hope that something will change, because the success or otherwise of introducing intrapreneurship greatly depends on providing adequate financial means. Parallel to training of potential entrepreneurs is the fact that it is necessary to train managers to enable them to pool and share their knowledge with other colleagues. The training is usually organized once a month and lasts for probably eight months.

## ***REQUIREMENTS FOR INTRAPRENEURSHIP***

To introduce intrapreneurial process in an enterprise, the following factors are of paramount significance: understanding of the environment, vision and creativity determination, flexibility in operations, creation of manager options, encouragement of team work, and encouragement of open discussions among colleagues at work whether senior or otherwise. Taking one after the other, these facts are explained as follows:

- Understanding the environment includes monitoring and analysis of internal and external company environments in order to have complete insight into possible weaknesses, advantages or internal abilities of the company,
- Visionary approach is needed for determining company position, prices, expenditures, planning of the informational technologies and demands for hardware and software in order to provide company's development and to improve business efficiency,
- Flexibility in operations assumes quick adaptation to changes; namely, if the organizational structure relies on flexibility of operation, it will be able to change at will within a short time,
- Creating managers' options means that managers should not only change their behavior, but also their opinions and to offer various solutions to problems of the moment. We should also keep in mind that managers are different in their approaches to changes. It is perfectly natural that many managers are usually afraid of changes and that they see them as stresses before they are able to see their advantages. Likewise, many assume that they cannot easily change their way of thinking and see the needs for changes in a different way,
- Encouraging teamwork is necessary, as well as information flow in order to keep managers' efforts constructive and resulting positively. Bad communication will hardly lead to positive changes,
- Open discussions among organizational members are necessary so that all employees as well as other organizational members will get to know the new ideas and possibilities of organizational change and to have a feedback. In this way, confidence is built among the employees and faster acceptance of changes will be assured, and
- Finally, we should point out that this kind of tasks are organized as integral part of the organization or system, and not as independent business units; so it is necessary to establish good cooperation and collaboration with different units of the enterprise.

## ***THE LINKAGE BETWEEN ENTREPRENEURSHIP AND INTRAPRENEURSHIP***

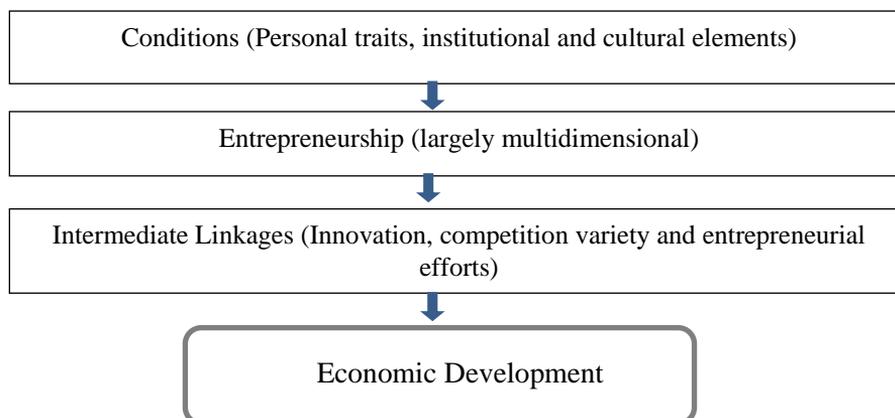
Going by the discussion so far in this paper, it would be crystal clear that entrepreneurship do occur mainly from the outside of an enterprise whereas intrapreneurship usually originate from, and operate within, a particular enterprise. All innovations and creativities aiming at generating and improving gains or profits within an enterprise are tantamount to intrapreneurial activities nowadays commonly termed internal reengineering or organisational restructuring in modern management. This approach to modern management in most cases lead to creation of new products (goods or services) or improving the existing ones but it must take place within a particular enterprise.

On the other hand, all efforts concerning new innovations and creativities with the ultimate aim of making profit or improving productivity from outside of the organisation as well as setting up of new business ventures are tantamount to entrepreneurship. Hence, Intrapreneurship and entrepreneurship are complements of each other. Both concepts in practice collectively lead to productivity improvement which, in turn, lead to profit by the entrepreneurs, and as a consequence, they play integral parts in economic development through creation of more jobs, making availble more facilities (amenities) as well as advancement in technology. In practice, however, not many people would differentiate between the concepts of entrepreneurship and intrapreneurship as they see them synonymously. Hence, from now onward, we will use the term entrepreneurship to refer to both of them for the ease of analyses and explanations.

## ***UNDERSTANDING ENTREPRENEURSHIP AND ECONOMIC DEVELOPMENT***

In terms of how entrepreneurship has been a stimulant in economic development, there exist enormous discussions and debates but it is however eminent to realize the importance of constant innovations and rivalry enhancement (Todtling, Wanzanbock, 2003). There has been a problem in defining and measuring entrepreneurial factors and this has further complicated the exact contributions to economic development. According to Carree and Thurik (2002), the concept of entrepreneurship is multidimensional and largely ill-defined. Understanding the role of entrepreneurship in the process of economic development will therefore require a framework because of the nature of intermediate variables and connections which exist (Bygrave, Minniti, 2000). The best examples of these intermediate variables include innovation, competition mainly characterized by exit and entry of firms, variety of supply and particular energy and efforts of invested by entrepreneurs. Other conditions of entrepreneurship also add up when it comes to their contributions to economic

growth (Robbins et al., 2000). These conditions according to Carree and Thurik (2002) include personal traits, cultural and institutional factors as shown in Figure 2 that follows:



*Figure 2: Appreciating Entrepreneurship*

### ***EXTENDED DEFINITION OF ENTREPRENEURSHIP IN RELATION TO ECONOMIC DEVELOPMENT***

While entrepreneurship is all about the activities carried out by individuals, the concept of economic growth has often been relevant at firm level, industrial, national and regional levels (Robbins et al., 2000). This implies that linking entrepreneurship to economic development will be to amalgamate individual to aggregate levels. Considering this linkage however requires revisiting the definition of entrepreneurship, whereby entrepreneurs, either as individuals or a team, manifest their willingness and abilities to create new opportunities in economy (Todtling, Wanzanbock, 2003). In this manner, novel products, production modalities, organizational schemes and product-market combinations are created. The entrepreneurs seek to introduce their newly crafted ideas in the existing market in the face of obstacles and uncertainties. They also make critical decisions in terms of business location, forms and the utilization of available resources and institutions. In a nutshell, entrepreneurship refers to the behavioral attributes of individuals and should not be confused with well-defined professional persons (Lloyd-Ellis, Bernhardt, 2000).

## ***ENTREPRENEURIAL EFFECTS IN THE DEVELOPMENT OF ECONOMY***

To sum up the contributions of entrepreneurship to economic development, Carree and Thurik (2002) have provided five strands of empirical evidence to show their involvement. The first evidence mainly deals with the turbulence effect of entrepreneurship on the development of economy. Turbulence can be viewed as the total entries and exits in regions or industries and can easily be interpreted as one of the powerful indicators of entrepreneurial activities. The effect of and changes in size distributions in regions represents the second strand of evidence as identified by the two researchers (Lloyd-Ellis, Bernhardt, 2000). It is believed that the change in size distribution and its ultimate effects can have a significant impact on the development of economy (Carree, Van Stel, Thurik, Wennekers, 2002). Thirdly, the number of market participants in any industry will finally have an important effect on economic development and this is recognized as another strand of evidence of the role of entrepreneurship in economy expansion (Chell, Ozkan, 2010).

Empirical literature has also identified the effect of the number of business owners and self-employed individuals in economic development. This is the fourth strand of evidence that seeks to appreciate the role of self-employment in the development of economy in any state. Lastly, the economic history of previously centralized and planned economies will also have an influence in economic development of countries (Carree et al., 2002). For instance, in Eastern Europe, small enterprise development served as the most vital part of the transitional process which has seen economic development in the area.

The turbulence effect of entrepreneurship on economic development refers to the entry and exist which however appears to have minimal contributions to the development of the economy in the short run (Bathelt, 2001). Nevertheless, the entry-exit turnover will make a significant contribution especially in service industry than in manufacturing industry in the long run as evidence by empirical research done by Bosma and Nieuwen-huijsen (Chang, 2011). The effect of size distribution changes of firms on development performances has also been recognized particularly when examining the share of small firms in the manufacturing industry in the European states. Competition among firms which is a commonplace for entrepreneurs has been shown to have a positive effect in the development of economy (Carree, 2002). The increased numbers of participants in the market compounded with entrepreneurial activity are some of the contributions of entrepreneurship in economic development (Chell, Ozkan, 2010). In particular, local competition which is measured in terms of the relative number of businesses in a region per worker encourages development of employment in industries thus economic development.

Entrepreneurship encourages self-employment and this has been found to have an impact in productivity development (Chang, 2011). This is however a much contested

observation whether countries should adopt the equilibrium or the self-employment model which has largely failed countries such as Italy. According to Chang (2011), the high levels of self-employment in the country have proved to be inefficient for economic development. Italy has in the past experienced large negative impacts on the development of its economy because of self-employment. Scandinavian countries represent cases of countries with relatively low rates of self-employment than the equilibrium and have often been characterized by extensive public sector and low rates of entry and exit. The contrary is seen when analyzing the business structure in West Germany where they have low rates of self-employment (Van Stel, Carree, Thurik, 2004a). In Germany, there is a total failure in the restructuring the economic policies as the United Kingdom has done. The industrial policy in German has repressed the structural changes by solely supporting large-scale industries with enormous subsidies (Van Stel et al., 2004b). This has led to the lack of a vibrant economic development made of new industries and firms in German and thus a serious barrier to innovative activity.

### ***FUTURE PERSPECTIVE IN ANALYSIS***

From various strands of literature, there have been many insights that have inspired a number of frameworks which should be embraced in the analysis of how entrepreneurship plays a critical role in economic development. Carree and Thurik (2002) found three different levels of analysis to be evident when associating entrepreneurship to economic development as this meant that the individual level could be linked to the macro-economic sphere. These levels include the individual, firm and the macro levels of analysis. According to Bruce, Deskins, Hill and Rork, (2009), entrepreneurial actions usually take place at the level of the firm and thus require a vehicle which can transform their individual ambitions and qualities into workable actions (Todtling, Wanzanbock, 2003). In small firms, the entrepreneur usually has the controlling stake which acts as the vehicle for transformations. Larger firms have also been found to mimic smaller firms in terms of business units, joint ventures and subsidiaries in order to introduced entrepreneurship or corporate entrepreneurship. The results of such entrepreneurial manifestations at the level of the firm must do with how novel processes, products, innovations, and entry to new markets or start-ups are (Tesreau, Gielazauska, n.d). At national, industrial and regional levels, entrepreneurial actions are all composed of new experiments.

## **CONCLUSION AND FURTHER RECOMMENDATIONS**

Entrepreneurship play a critical role in the development of the economy as this is the key contributor to innovativeness and product improvement. It is one of the important ingredients to the creation of new employments and in the building of communities in ways of offering them jobs. By contributing to local charities, taking part in local business, investing in projects in communities and creating and participating in different networks in entrepreneurship, they build up robust communities which contribute to the community development. Governments should develop policies which will enhance entrepreneurship by understanding the critical difference existing between small business owners and entrepreneurship. At the same time, a misconception about entrepreneurs and where entrepreneurs can be found can also help the local people to create the right picture of entrepreneurship and thus become aggressive and contribute to economic development.

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## ***JOURNEY OF A SMALL TOWN ENTREPRENEUR : AN INDIAN CASE STUDY***

*Reena Agrawal, PhD<sup>50</sup>*

### ***ABSTRACT***

*This case study showcases the vision and initiative of a small town entrepreneur who belonged to a business family and who inherited the legacy of entrepreneurial traits from his father. He always had a passion to establish and operate a business of his own and generate employment opportunities for others in the society. This case study showcases his exemplary work and discusses in detail the education acquired by the entrepreneur, his vision, how he became an entrepreneur, his entrepreneurial endeavours, the milestones achieved by him, major challenges faced by him, the growth enjoyed by him and his plans for future expansion and growth.*

**Key words:** *entrepreneurial traits, revival of sick unit, entrepreneurial initiatives, future growth*

**JEL Classification:** *L26, F43*

**UDK:** *005.961:005.914.3(540-77)*

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## ***INTRODUCTION***

As early as the 1950s, researchers began looking for personality factors that determine who is – and who is not – likely to become an entrepreneur. McClelland (1961) found that entrepreneurs had a higher need for achievement than non-entrepreneurs and were, contrary to the age old belief, moderate risk takers rather one can say they take calculated risk. A great deal of research on the personality characteristics and socio-cultural backgrounds of successful entrepreneurs was conducted in the 1980s and 1990s. Timmons (1994) in his analysis of more than fifty studies found a consensus around six common characteristics of entrepreneurs: (1) commitment and determination; (2) leadership; (3) opportunity obsession; (4) tolerance of risk, ambiguity and uncertainty; (5) creativity, self-reliance and ability to adapt; and (6) motivation to excel. A related stream of research examines how individual demographic and cultural backgrounds affect the chances that a person will become an entrepreneur and be successful at the task. For example, Bianchi's (1993) review indicated that factors such as: (1) being an offspring of self-employed parents; (2) being the oldest child in the family and (3) being a college graduate often etc often lead a person to take up entrepreneurship as a career. In the words of Timmons (1994) "Entrepreneurship is the process of creating or seizing an opportunity and pursuing it regardless of the resources currently controlled".

The present case study truly brings out that the Anil Singhal's choice to become an entrepreneur was not a sheer chance or pure luck but was the outcome of several other factors that closely touched his life his family background, family's financial condition, his role and responsibility towards his family, and above all the basic personality traits that he possessed.

## ***METHODOLOGY***

The methodology adopted includes the following: visiting the project site, conducting series of interviews of the entrepreneur and interacting with the other stakeholders. A questionnaire was drafted and then those questions were administered on the entrepreneur. A rough draft was prepared and then it was refined. The entrepreneur's endeavours, experiences, hardships, success and other nuances of business have been developed by way of a case and the vital learning's drawn have being illustrated by way of figures and diagrams.

## ABOUT THE ENTREPRENEUR

Mr. Anil Singhal is a resident of Bahraich district in Uttar Pradesh. He belonged to a business family and his father had an oil mill. He completed his education in arts stream from a government college. While he was still pursuing his education, his family was going through financial difficulties and he being the eldest child in the family was compelled to look out for opportunities to earn a livelihood and give financial support to his family. The only thought that struck him was Anil to start a business of his own. As he belonged to a business family he had seen life of a businessman very closely and had experienced all the shades of highs and lows. These had inbuilt in him several entrepreneurial traits such as self-motivation, courage, ability to take risk, hard work and patience. He had inherited several characteristics such as leadership, interpersonal skill and co-operative nature from my father. He was hardworking person, who was open to new ideas and who would pursue his work with great passion. He asserts that, the personality traits that assisted him in becoming a successful entrepreneur are his patience, hard work, capability of handling the complexities, an eye for opportunity and the ability to tap the opportunity on right time, self-motivation and positive attitude.

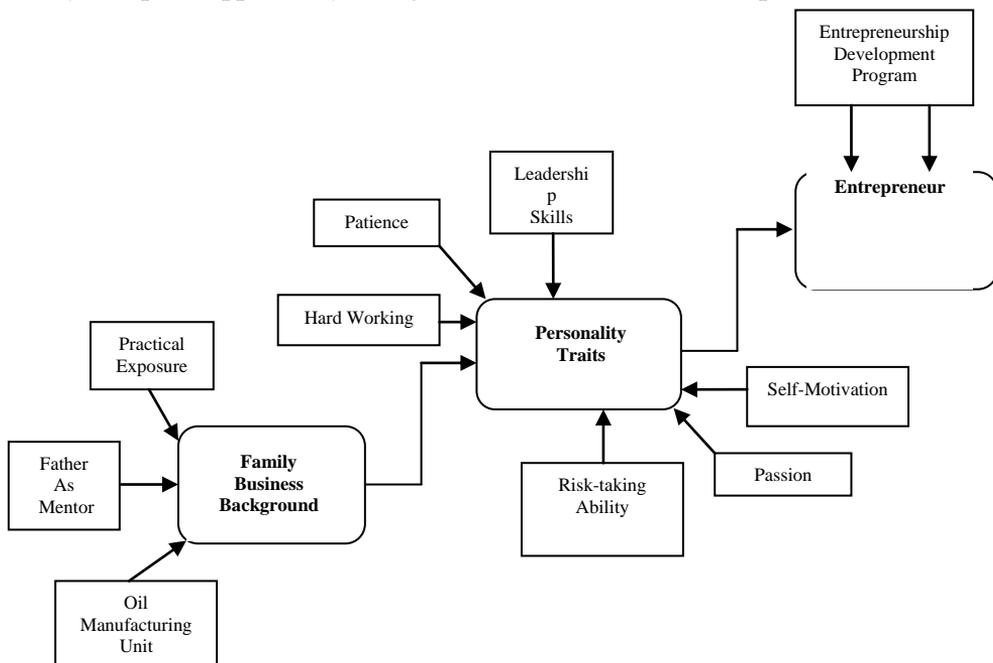
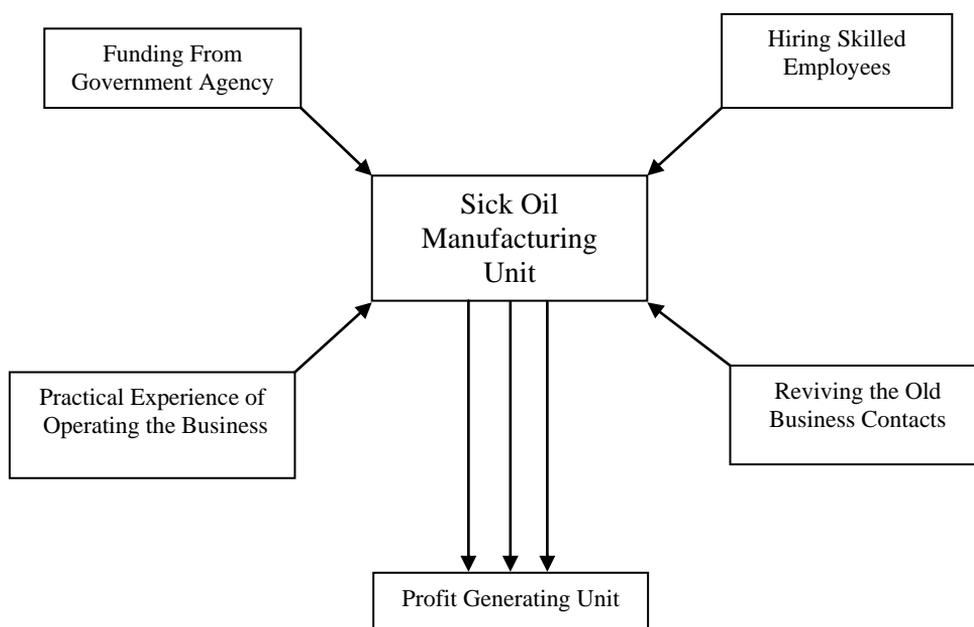


Figure 1: Factors that made Anil an Entrepreneur

## ***ENTREPRENEURIAL INITIATIVES***

Once Anil decided to start a business of his own he realized that establishment of a business required huge capital investment and at that point in time he was not in a position to arrange funds to initiate a venture. But he did not get disheartened, he looked for another alternative. The idea that crossed his mind was of re-starting his father's oil mill which was shut down due to unavoidable reasons. He knew he would need funds for the same. He had a small saving of INR 12,000/- which was not sufficient for the cause. He prepared a business plan for re-starting the sick oil mill and submitted the same to the Unemployed Yojna Samiti, a government agency, which provided financial support to the projects, which had financial viability. His business plan was appreciated by the agency and they sanctioned him a loan of INR 50,000/- with which he re-started his father's oil manufacturing unit. The reasons for re-starting the oil mill were: the capital investment was minimal as the machinery such as speller and filter was already installed; he as a child accompanied his father to his work place so he already had practical exposure in that business; he knew the experienced work force and had to make little effort to bring the back to work; there were existing business contact which he could soon revive.



*Figure 2 : Revival of a Sick Unit*

The process involved in manufacturing of edible oil was as follows: firstly, mustard was bought from the market and cleaned; second, the clean mustard was put into machines and oil was extracted and third it was filtered and stored in tanks;

fourth the packing was done in the tinned boxes of 15 kg and drums of 180 kg and lastly it was dispatched to market. The initial production capacity of the oil plant was 112,000 kg per annum but gradually he expanded the production capacity to 324,000 kg per annum. He could generate an annual income of INR 72,000/- from this business. He largely catered the local market and a few markets of the neighbouring cities. Although the amount was not big enough, but was enough to fulfill his family's basic needs. Till four-five years, his business was operated profitably but then it started experiencing a down ward trend, this was alarming but with his business acumen Anil managed to retain the stability. But he realized within that it was appropriate time to look out for new business opportunities

During this time he got an opportunity to join a seven days "Entrepreneurship Development Programme" conducted by National Alliance of Young Entrepreneur and sponsored by the Government of Uttar Pradesh. He stated that he greatly benefitted from that program. As he was an arts graduate he never acquired formal business education. The learning's drawn by him from that program included the following: how to identify new business opportunity, how to conduct a research before starting a venture, how to initiate a new venture, what are the different sources from where the funds could be arranged, how to arrange necessary resources, how to manage the day to day operations, how to tap a new market etc. He asserted that the training programme instilled in him courage and confidence and he passionately moved towards his goals and progressed in life.

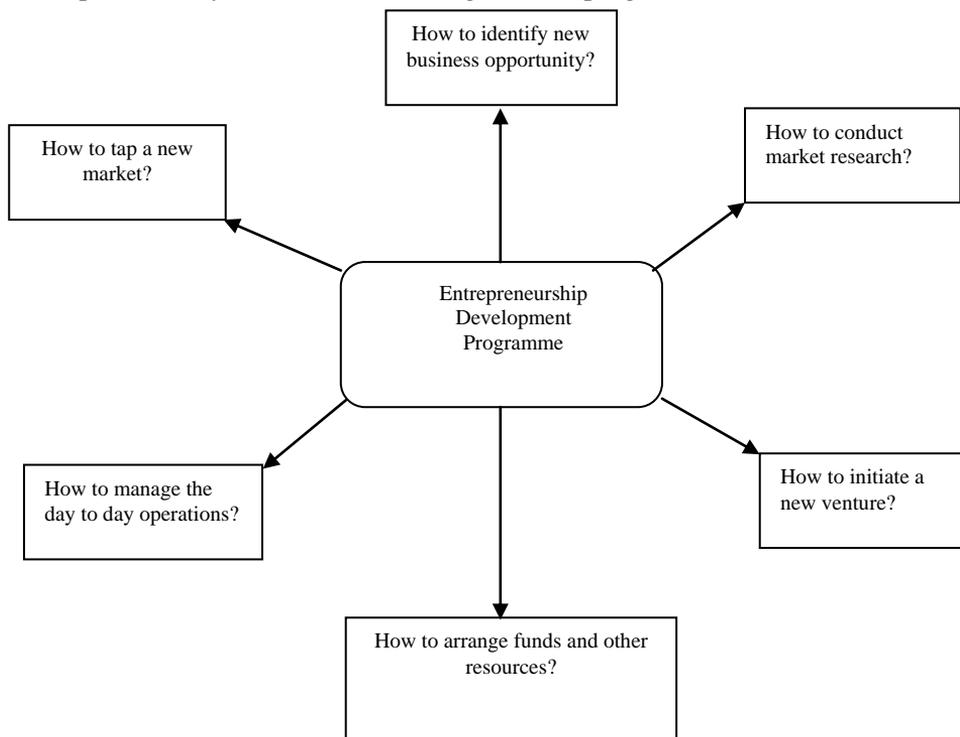
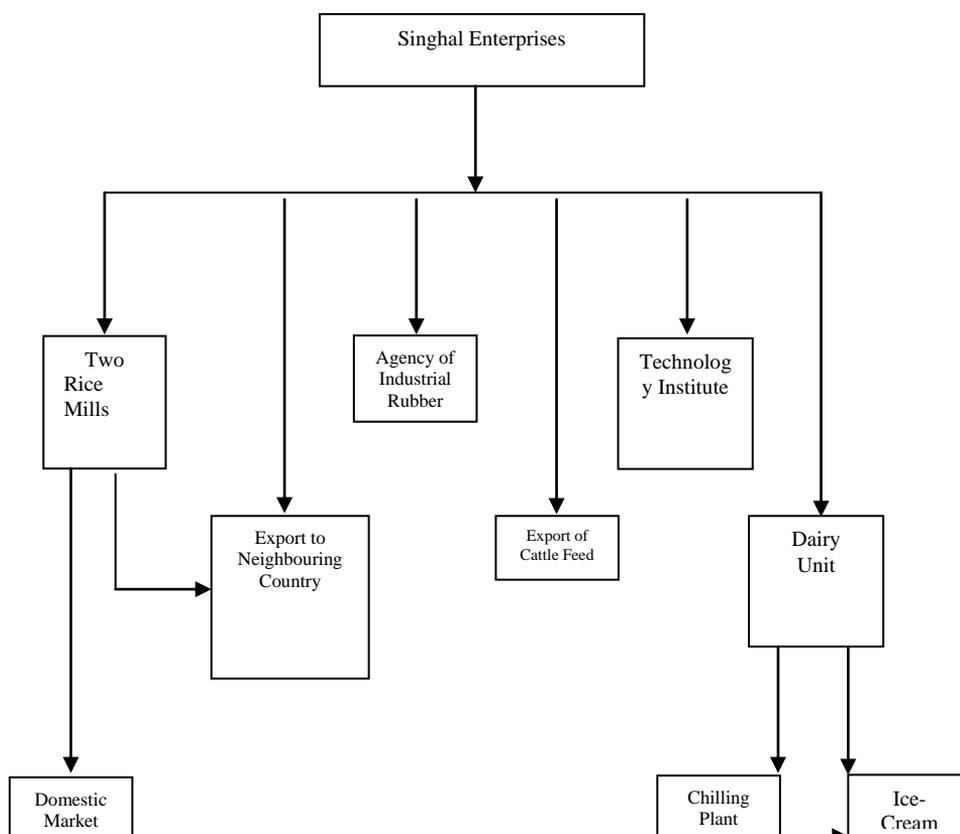


Figure 3: Learning Drawn from Entrepreneurship Development Program

As there no scope for further growth in the oil manufacturing business, he decided to venture out for some new product. He thought he should deal in such a product which enjoys constant demand in the market, he did some market research he analyzed that demand for rice never come down. He decided to establish a rice mill. He arranged the necessary resources and with a capital investment of INR 100,000 and on a land area 2,400 square feet he installed the machines such as de-husker and an imported polisher. It was a very risky decision for him as he was invested all that he had earned so far in his life. But his thinking was that, a person who takes risks succeeds in life, and high risk gives high returns. He strongly feels that every entrepreneur must have an ability to take risk. The production capacity of the rice mill was 5,184 tons per annum. The production process included the following steps: firstly paddy was cleaned, second clean paddy was dried, third it was put into de-husker in which rice and husk was separated, fourth the rice was polished, fifth it was packed and sixth it was dispatched. He majorly catered to the various markets within Uttar Pradesh. With this rice mill he was able to earn INR 20,000/- per month which was much higher than what he used to earn from oil manufacturing unit. This was a turning point in his life where he started getting progress in his business and the credit goes to his hard work and his never ending motivation towards his life. Till a few years, he was individually handling his business but he was facing some problem in the finance and accounting due to which he had to suffer a few losses as well. Anil had a number phobia since his childhood, so he engaged his brother to take care of the monetary aspects. Anil said an entrepreneur should be able to do self assessment and should not shy away from his weaknesses rather he should be able to design a proficient and trustworthy support system for all the missing expertise.



*Figure 4: Entrepreneurial Initiatives by Anil Singhal*

Successful execution of the rice mills boosted Anil's confidence and he started looking for another business opportunity. He then took an agency of Gold Mohur rubber roll, it is rice polisher rubbers used in machines used in rice mills. This rubber roll was the best quality rubber available in the Indian market and was manufactured by a company called in Delhi. Anil knew that there would always be a regular demand for such rubber rolls in the rice mills. This new business proposition generated additional revenue for him. Today he supplies the rubber rolls in all over Uttar Pradesh.

Anil wanted to expand the rice business even further and he desired to expand his reach in the foreign markets as well. So he decided to apply for a license to Agricultural and Processed Food Product Export Development Authority (APEDA) Ministry of Commerce, Government of India so that he could seek the necessary permission, to export rice outside India. He got the license and started exporting rice to Nepal. Today he exports almost 2,400 tons of rice annually to Nepal. This again resulted in substantial growth of the revenues. With this increase in market size Anil decided to set up one more rice mill to fill up the gap. Gradually he also started exporting cattle feed in Nepal which he bought from local market. He also supplied cattle feed some of the states in India as well.

Anil believes that “today there is a need for knowledge based society, having skilled youth who bring innovations and lead the world.” Therefore, technical and professional institute of global standards needs to be established all over the country. He observed that the Purvanchal region in Uttar Pradesh lacks behind in educational development. There was lack of good quality technical institutes in the region. The youth living in that region either moved to other cities, which are recognized as educational hubs, to seek education and those who could not afford the same had to forgo their dreams. So Anil decided to open an engineering institute in the Purvanchal region. He gathered support of some like minded people and together they established an institute named “Buddha Institute of Technology”, at Gida in district Gorakhpur, Uttar Pradesh (India). It is approved by All India Council for Technical Education, a statutory body and also the apex body of Government of India for technical education and affiliated to Uttar Pradesh Technical University, a state level affiliating body for technical education. The programme that is offered is B.tech. At present 5 branches engineering such as Civil engineering, Computer Science, Electronics and communication, Information Technology and Mechanical Engineering are being offered to the students. They have total of 300 seats. The institute has picked up well and serving the society in special manner.

Anil recently started a Dairy Unit which has milk chilling plant and an ice factory. The capital investment was of INR 4,000,000. The production capacity of this milk chilling plant is 30,000 liters per day. Milk is procured from local vendors, then cooling is done in the chilling plant, the milk is supplied to the ice-cream factory and a local milk powder manufacturing unit. The daily production is of 30,000 kg of ice creams per day.

## ***OPERATIONAL STRATEGY***

He stated that he has a policy of changing the machineries in every five years. This facilitates the use of latest technology; ensures superior quality production and also prevent undue wastage of money on repair and maintenance of the machineries.

Anil started with a workforce of six people and today he is providing livelihood to hundreds of people. He lays special emphasis on the training and development of the workforce. People are trained to handle the machines in safe and proper manner. This helps in avoiding undesirable mishaps at the work place. He arranges medical insurance for all his employees along with their families and gives bonus during the festival season.

The major challenges faced by him included cut throat competition, fast changing technology, climatic condition which affected the agricultural produce. These hardships helped him to learn that one must build long term relationship with the customers, to be always ready with the product when demanded by customers and the most important is to be confident and the ability to stand against the failure. Another important thing is to have goodwill in the market. A business should be known for its quality of production, timely supply and fair dealing. All these are important principles for enjoying sustainable growth.

Anil who started with an annual turnover of INR 200,000 per annum today approximately has an annual turnover of INR 70,000,000. Starting with a single manufacturing unit today Anil owns and pilots six different diversified projects. Today his product basket comprises of: agricultural products; industrial products; dairy product and education.

### ***AGENDA FOR FUTURE GROWTH***

Anil stated that he has come a big way but he feel he still has to go for mile. He would constantly be on a lookout for new business opportunities. He said that due to globalization and liberalization there are fast moving changes in the government policies, economy and society. There are new avenue which are opening up and people demand diversified products and services. So if he comes across any financially viable business preposition he would certainly love to venture into the same. As of now he has a dream to establish school to impart primary and secondary education to the kids living in his region. He plan is to create a state of art infra structure, employee highly qualified and trained faculty and deliver a contemporary curriculum which is at par with the world`s best schools. At the moment he is busy drafting a blueprint for his dream project.

### ***TEACHINGS FOR YOUTH***

One must work hard and be fully dedicated to whatever work they do. One must keep their eyes and ears open for any upcoming opportunities and grab them on time. One must be ready for failure, keep taking challenges, and don`t let the failure bring down the morale and self-belief. One should deliver his very best. Before plunging into any specific sector one must have in-depth knowledge of that sector, must gather necessary expertise in that field, work hard to arrange the necessary, work passionately the most important thing is have patience. Once a person has firm determination there is nothing in this world that cannot be achieved.

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# **THE APPLICATION OF THE EU PUBLIC SERVICES GUIDELINES IN SERBIAN PUBLIC ENTERPRISES**

*Daliborka Petrovic, PhD<sup>51</sup>*

*Tihomir Gligoric, PhD<sup>52</sup>*

## **ABSTRACT**

*The subject of the paper refers to the unique concept of public services at the level of European Union. The main principles of the management of these services are outlined and issued by the European Commission within the White paper of Services of General Economic Interest (SGEI) in the year 2004. The aim of this paper is to analyze the level at which the management of public enterprises in the Republic of Serbia is aligned with the new European Union's public services concept and management principles defined in the White Paper of SGEI. In order to achieve the aim of the paper, empirical research and collection of the primary data were necessary. The research method applied is qualitative by nature. The interview with in advanced prepared section of questions was used as the research instrument. Based on the results of the empirical research it could be concluded that there is enough place for making the adequate changes that would improve the market and consumer orientation of Serbian public enterprises, which would substantially contribute to alignment with the EU guide principles in this field.*

**Key words:** *Services of General Economic Interest, European Union, Public Service Management, Republic of Serbia*

**JEL classification:** *M20*

**UDK:** *005:351.076(497.11)      005:351.076(4-672EU)*

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## ***INTRODUCTION***

According to the new European Union concept of public services, all public services are divided into two groups- Services of General Interest (SGI) and Services of General Economic Interest (SGEI)- based on the (non)economic nature of their activities. The first group of services refers to the public services such as police, security, judicature and a like, where the active role of the state in their provision and delivering is indispensable. The second group of public services includes: electricity, public transport, postal services and telecommunication. When it comes to the services of general economic interest, new elements such as introducing market mechanisms, strengthening the competition, improving the consumer and market orientation and professionalization of public management are added. With the aim to give member states the framework for organizing the services of general economic interest at the national level, in the year 2004 the European Commission issued the White paper on SGEI outlining the basic principles of management of these services. Although public management in the European countries has undergone several changes since 1980 (England) and 1990 (Germany), this new EU framework for public services makes all European countries more interested in finding the ways to improve management of public enterprises especially in order to improve the quality of services, efficiency in their provision and citizens'-consumers' satisfaction. Putting the accent on the competition, market and consumers, new EU concept of services of general economic interest arises more interest in the professionalization of management in the process of public service provision and delivery.

## ***THE NEW CONCEPT OF PUBLIC SERVICES IN THE EUROPEAN UNION***

The main characteristic of the new concept of public services in the European Union refers to the unique combination of the two economic traditions- continental and Anglo-Saxons. In the field of public services, the traditional continental economic approach emphasizes the equality, social justice, universal access to services for all citizens, absence of discrimination, support for low income, vulnerable and marginalized social groups as well as the strong, active role of state in the provision and delivery of public services. On the other hand, the Anglo-Saxons economic approach put the accent, among the others, on the improvement of public service quality and efficiency in the process of their provision, on the availability of alternatives for citizens who should be seen primarily as consumers of the public services and the professionalization of public service management. The role of state is considered to be very important in the domain of planning, making adequate policies, monitoring and controlling rather than in the direct,

often monopolistic provision of public services. Instead of choosing only one way, European Union, from the year 2000, opted for the harmonious combination of continental and Anglo-Saxon economic approaches, respecting the elements of both. As a result of that, the idea of European citizens and socially balanced Europe has been enriched with the concept of consumerism, competition and market-oriented approach to the management of public services.

The new European concept of public services has two aims- modernization of public service system on the internal market while maintaining the fundamental European values in the domain of social politics where the state is perceived as their main guarantor. In other words, the European Union strives for balance between high level of social protection, fair national income redistribution and achievement of planned growth rate and the improvement of EU competitiveness (Maroto, Rubalcaba, 2002).

Modernization and competitiveness of European public services are supposed to be achieved by selective introduction of certain Anglo-Saxons economic elements, such as opening the market, introducing some form of competition, treating the citizens as consumers of public services offering them the chance to choose among different alternatives and have more influence by ensuring mechanisms for their potential complains and reclamations. In other words, the channels for two-way communication should be developed in order to encourage the citizens'-consumers' active involvement in the service provision process. Apart from that, Anglo-Saxons approach to public service management, known as the New Public Management, also stresses the importance of researches of consumers' real and actual needs, their attitudes, opinions as well as the level of their satisfaction with the various aspects of public services they use and pay for, either directly or through taxes. Additionally, elements such as evaluation of performances, inclusive management, better transparency and protection of consumer rights are also highly ranked in this system of public service management.

The possibility of the integration of more economic approaches into one, unique, European approach could be explained by the fact that social politics is perceived not as the burden but as the important prerequisite for sustainable economic growth in Europe (Clifton et al., 2007). Therefore, European tendency to competitive public services goes hand in hand with the project of socially balanced Europe which indisputably includes the guarantee of access to basic public services for all citizens and care for socially vulnerable groups. According to that specific mission, all enterprises providing and delivering the public services are obliged to accept and respect the rules defined by Universal Service Obligation.

In conclusion, the idea of implementing certain elements from Anglo-Saxons approach to public service policy and management should be understood in that specific context of European public services concept; not as the opposite, but more as the compatible additional elements that supports and strengthen current attitude of the European Union that all citizens should have rights to affordable, good quality public services which efficiently satisfy their actual needs.

## ***INTRODUCING THE NEW EU TERMINOLOGY IN THE FIELD OF PUBLIC SERVICES***

Respecting the traditional, continental economic approach as well as the mechanisms like competition, market-orientation and consumer right to choose, European Union opted for new, unique concept introducing even new terminology. All public services are divided into two groups according to the predominant nature (economic or noneconomic) of the activities of public services. Group of services with predominantly economic nature of activities are opened to the competition on the internal European market and named "Services of General Economic Interest-SGEI" (electricity and gas, telecommunication, postal services, public transport). The second group includes services which are non-economic by their very nature, where the role of state has always been essential for their provision, like the police, security, and judicature. This group of "Services of General Interest-SGI" is excluded from the competition on the internal European market. This categorization of public services in the European Union matches the orthodox economic dichotomy of public good- pure and non pure public good, by the criteria of non-rivalry and non-excludability (Gnjatović, 2005). So, the SGEI are non pure and SGI are pure public good.

## ***EUROPEAN REGULATORY FRAMEWORK FOR SERVICES OF GENERAL ECONOMIC INTEREST***

The process of forming the European regulatory framework of services of general economic interest (SGEI) has been going through a long and continuous process, which is characterized by the active involvement of the state members, the formulation and updating of the official documents of the European Commission. Although the process of creating regulations in the area of services of general economic interest is still subject to amendments and modifications, it is possible to distinguished basic legislative and regulatory documents governing the area of services of general economic interest. These are: Treaty of the European Community ECT, in particular the Articles 86 and 16, Green Paper on SGEI, White paper on SGEI. For the purpose of this paper, Green Paper on SGEI and specially White Paper on SGEI are accented.

In the year 2003 the European Commission published Green Paper on SGEI which is the first document at the supranational level dealing exclusively with the issues of SGEI. The goal of Green Paper on SGEI was to open the series of important questions in this area, and invite all member states, as well as other stakeholders, to actively participate in shaping the future of the European concept of public services. Hence, Green Paper on SGEI represents the first step toward the formulation of the official European regulatory framework for services of general economic interest. Green paper on SGEI is consisted of five main parts, in addition to the introduction and operational conclusions.

The first part refers to the new terminology and definitions, as well as the role of public authorities in the system of services of general economic interest. The second part deals with the objective that the Community wants to achieve through their engagement in the area of services of general economic interest. The third chapter deals with a number of elements that could potentially constitute a common concept of services of general economic interest. The common principles refer to: the universal access, continuity, quality of services, affordability, consumers' and users' rights protection. Additional principles had been later added as a result of member states' participation in the process of forming the final common European framework of SGEI. The fourth part covers issues relating to the organization, financing and evaluation of SGEI, while the fifth part is devoted to the international dimensions of services of general (economic) interest.

White Paper on SGEI is consisted of introduction as a first part of the document, Second part deals with the issue of common responsibility of public authorities in the EU and the member states. In the third part there are basic common principles for SGEI defined and outlined. These principles represent the EU guidelines for Services of General Economic Interest, and as such, are given special attention in the following part. The fourth part deals with the policy improvement with the aim to accomplish the higher degree of coherency in the area of services of general economic interest along with the respect of diversity. Hence, White paper on SGEI is final document regulating this field. But it has not nevertheless to be understood as a finite step in shaping the common regulatory framework for SGEI.

Common EU principles defined in the White paper on services of general economic interest are in line with the basic idea of linking up the elements from European continental and Anglo-Saxon economic traditions. Although the sharp line can not be underlined, still it is possible to note that the principles of cohesion and universal access to services for all citizens, respecting diversity of situations, maintaining safety and security, providing legal certainty reflect the traditional values of European continental economic approach. On the other hand, the principles such as achieving public service objectives within competitive open markets, highlighting the consumer rights, monitoring and evaluating the performance, increasing transparency are in line with the Anglo-Saxon economic tradition.

## ***EU GUIDELINES FOR SERVICES OF GENERAL ECONOMIC INTEREST***

In the year 2004 the European Commission published the White paper on Services of General Economic Interest, based on the suggestions and conclusions of member states that took part in the constructive dialog at supranational level. Despite the expected differences in opinions and attitudes of member states, consensus was reached that services of general economic interest should be organized with a harmonious combination of market mechanisms and the specific mission of public service.

In the third part of White paper on SGEI, nine guiding principles of the Commission's approach are outlined: enabling public authorities to operate close to the citizens, achieving public service objectives within competitive open markets, ensuring cohesion and universal access, maintaining a high level of quality, security and safety, ensuring consumer and user rights, monitoring and evaluating the performance, respecting diversity of services and situations, increasing transparency and providing legal certainty (Commission of the European Communities, 2004).

Very important new part of EU public services policy refers to the separation of the process of policy formation from the process of the direct delivery of the public services. Those who are involved in the defining the policy framework of public services are not included in the production or direct delivery of services of general economic interest. This part is done by the other subject or organization, which is engaged by public authorities. Between these two parties the conflict of interest must not exist and their mutual relationship is regulated through legal means and contract.

This kind of separation of production and delivery from policy making has already been done in several member states of the EU, specially in England and Germany. Based on these experiences, authority in charge of the policy making forms the policy framework but in order to organize production and direct delivery of services of general economic interest, this authority makes contracts with other parties-organizations and agencies, which on the behalf of the public authority and in line with the previously defined policy, have the responsibility for the quality and the efficiency of delivered services. The public authority, which chooses and makes the contract with other organizations or agencies, is accountable for monitoring and control of the delivery process. Apart from that, in the cases where some parts of public authority are included in the direct delivery, there has been a practice of making the semi-contracts with those parts. This kind of semi-contracts approach forms the internal quasi market where the relations are defined and based on the contractual principle. In addition to that, the local authorities also has the right to engage the other parties for public services delivery and improvement at the local level. In this case local authority enters into a contract with the chosen organization. Reasons for local cooperation in the domain of services of general economic interest can range from overall improvement in quality and efficiency of services up to the need for organizing tailor-made services' delivery for special or marginalized population groups. In all these cases, the organizations in charge of production, organization and direct delivery of services of general economic interest are run by professional managers.

The separation process of policy making from production and direct delivery of services resulted in the greater and clear distinction between the policy decision making and the professional management process. It is the relation known as principal agent relation, in which one party (agent) acts on behalf of the other party (principal). This kind of relations are well known in the private sector, but it is regarded as innovative in the field of public sector. For example, the companies' shareholders (as principals) choose management (agents) to act on their behalf. Precize conditions of the relation between the principal and agent is defined by contract. The separation of the policy makers from the professional management is considered to be crucial for the development of market mechanisms in the domain of services of general economic interest.

The new, contract - based relationship in the field of services of general economic interest led to the profound change of traditional hierarchical relations, which had generally dominated in the public sector for a long period of time. Instead of that, modern EU approach puts an accent to the relations based on contracts, with clearly defined responsibilities and accountability.

The party, which is responsible for direct delivery of public services, gets more freedom at the operational level but at the same time it is more accountable for the quality and efficiency of services delivered to the citizens. The party, which is responsible for policy making is also in charge of control and monitoring of the chosen organization's work and management. The innovative contract- based approach also changes the previous hierarchically structured control in the public sector towards the control based on the contract, where all the rights and obligations of both parties are defined and specified. Therefore, the cooperation becomes the standard in the domain of public services. By engaging the other parties, the public authorities enlarge their capacity to offer the better quality services to the citizens. Apart from the fact that cooperation has positive effects on the savings in public spending, main goal of including partners in the delivery of services to the citizens refers to the greater capabilities to offer services of better quality (Gray, 2003). The contractual principle in the domain of public services encourages institutional competition between the public enterprises, public-private and regulated enterprises, cooperants as well as social organizations.

New EU framework for services of general economic interest requires the definitions of the responsibilities for the performances of these services. Whether the public authorities enters into the contract with the private enterprises or the special agencies within the public authorities are formed, the clearly defined roles and responsibilities are necessary for the achievement of overall quality and efficiency improvements in the the process of public services' delivery to the citizens. Following the example of the private sector, public sector also turns towards professionalism, by strenghtening the role of and significance of management and employees who are directlz involved into the process of public services' delivery. Although the performance appraisal is new for public sector, and its effects are very specific, yet the general processes and techniques for the appraisal of organizational and individual performances are considered to be the solid foundation whcih can be appllied in several fields, regardless of whether the organizations belongs to the private or public domain (Daley, 1992).

Appraisal of performances entails also the need for precise definition of goals which have to be accomplished, as well as the clear criteria for appraisal of performances and responsibilities. The responsibility is closely associated with the evaluation of performances. If the professional managers are given the greater control over the resources in order to achieve certain defined results, then they are considered to be accountable for the performances of public services (Stewart, Walsh, 1992).

The price of services of general economic interest, method of payments and the labor cost in public secotr had long been regulated exclusively by government.

However, with the changes of relations among the parties and bigger responsibilities of professional management in engaged agencies and organizations, governmental approach of price and labor cost determination has often been seen as obstacle that limits the freedom of management's action and affects their capabilities for effective and efficient use of available resources. The requirement for competitive bidding, as an ingredient part of the new EU policy of services of general economic interest, is not compatible with the restrictive framework of labor cost and prices determination.

However, the more flexible approach to public services' prices and labor cost determination entails also the need for the profound changes in the human resource management in public sector. There is a need for creation of the new business culture, where employees are adequately motivated for more active involvement in the process of creation and delivery of services of general economic interest. In order to modernize the public services according to the EU guidelines, it is necessary to make the public sector more attractive for current as well as future professionals. Therefore, the new human resource management has to open more space for personal initiative fostering the entrepreneurial spirit and encouraging new ideas and team work. The role of employees is crucial because they are mostly in direct contact with the users-citizens and without their full engagement and initiative, the process of implementation private business like approach would hardly be done successfully. Modernization of services of general economic interest directly depends on the operational effectiveness and efficiency of all employees and management together. The employees should be offered stimulative environment, where they can have real chance for professional improvement, career development and promotion according to the achieved results and final outcomes. To make employees more motivated, there is also a need for delegation of more responsibility for tasks and operations, as well as for defining the encouraging system of rewards. Therefore, the careers of employees in public sector should be in line with their work performances and results achieved. In this regard, incentives for successful performances and the penalties for under average results have to be more precisely defined.

The public services market had long been consisted of only one or a few enterprises, mostly or entirely government-owned and managed. The consequence was that management decisions had been evaluated and made in accordance to political rather than economic criteria. In that case, enterprises involved in public services' delivery are monolithic because in one center there is a concentration of whole management, financial monitoring and budget control. With the new EU policy for services of general economic interest, the existence of more bidders is encouraged through the mechanism of public tenders. Local authorities are also suggested to turn to the alternative ways an resources of supply and delivery of services at the local level. This kind of change opens up the possibility of competition (or quasi-competition within the public bodies) between different bidders that have the capacity to cover the market and satisfy users' needs for public services.

Additionally, one of the major innovation in the EU public services' approach refers to the empowerment of the citizens' role since they represent the major users of public services. Treating the citizens as users of services or clients became known as the concept of consumerism, well known in the private sector but entirely new for public sector area. The concept of consumerism, instead of concept of citizenship, represents one of the main instruments for strengthening the market orientation in the field of services of general economic interest. Individual needs and right to choose between different alternatives are emphasized, which is significantly different from the previous collective, one-size-fits-all approach of public sector. Concept of consumerism opens up the possibility of marketing implementation in the public sector, which is also relatively new for this field (Kostić et al., 2013). New element of consumerism is underpinned by the fact that citizens pay for services of general economic interest, either directly or through taxation, which gives them the right to have better quality services, in line with their actual needs. Respecting the citizens as consumers of public services changes at the certain extent the nature of relationship between the state and its citizens. This relation is not only about obligations and responsibilities to pay taxes, but also about getting adequate level of quality and efficiency of public services the citizens pay for. Therefore, the state is more often understood as the guarantor of rights, and less as the active economic entity that has to be directly involved into the process of public services delivery.

Although the role of government in the direct delivery of services of general economic interest is reduced, its role in making adequate regulation and legislation, doing continuous monitoring and control of bidders has become bigger and more important. In the very developed economies, such as England, almost every privatization of public services had been followed by establishment of regulatory agency in charge of monitoring and control of the private enterprise bidder (Stewart, Walsh, 1992). The public authority bodies responsible for supervision and control of the work processes must be separated from the interests of the organizations/enterprises over which this control is exercised. So, the previous practice where the inspection, monitoring, control as well as the regulation had been done by the same organization is not compatible with the new EU market oriented approach to services of general economic interest. According to the EU guidelines, it is important to have independent entity in charge of supervision and control of those enterprises directly involved in public services' delivery, with their mutual interest strictly separated.

## ***TRANSFORMATION OF MANAGEMENT***

European Union concept of services of general economic interest has given the impetus for organizational and management changes in the field of public services at the level of member states. In spite of differences in extent and speed of changes, there is a clear tendency toward reducing the public sector inefficiency, which mostly results from organizational differences compared to private sector: soft budget constraint, lack of bankruptcy, the role of political factors, lack of competition, specific constraints in employment policy, procurement and budgeting, presence of principal-agent problem, strong emphasis on bureaucratic goals and risk avoidance, rigid procedures (Stiglitz, 2004).

Since public services have distinctive mission, purposes and tasks which private sector does not deal with, the process of introducing market mechanisms in the management processes must not undermine and jeopardize their fundamental components such as social justice and equity, public interest and socio-economic welfare of society. So, the public services should be treated differently than the private sector services (Van de Walle, 2008) even though some of private sector mechanisms would be useful for managing the public services. This means that, in spite of introducing market mechanisms and private sector approaches to public service management, respect of public interest, social responsibility and traditional European values remain vital components in the process of public services modernization.

European socio-economically balanced approach to reform of SGEI management is mostly focused on creation and implementation of business, private sector alike approach in managing scarce public resources, on defining clear responsibility and accountability for the results achieved and on performance management in line with the basic economic criteria of cost-effectiveness and efficiency (Doherty, Horne, 2002, pp. 16).

Although not limited to that, certain key themes reflecting the transformation of SGEI management can be identified (Steward, Walsh, 1992): the separation of the purchaser role from the provider role, the growth of contractual or semi-contractual arrangements, accountability for performance, flexibility of pay and conditions, the separation of the political process from the management process, the creation of market or quasi-market, an emphasis on the public as customer, the reconsideration of regulatory role, a change of culture.

## ***EMPIRICAL RESEARCH ABOUT MANAGEMENT OF SGEI IN THE REPUBLIC OF SERBIA***

Topic of the authors' empirical research refers to the question at what extent the principles defined at the level of European union are used in the management of public enterprises that provide services of general economic interest in the Republic of Serbia. Since the topic of professional management in the field of public services is relatively innovative at the national level, qualitative methodological approach is used.

The research sample is limited by European Union categorization of SGEI so that includes only those enterprises that provide SGEI at national level: Public Utility City Transport Company "Belgrade" (public transport), Company "Elektroprivreda Srbije-EPS" (electricity and gas), P.E. of PTT Communications "Srbija" (postal services) and Telekom Srbija (telecommunication). Although there is a certain difference between the management of the enterprises mentioned above, the aim of this paper is to try to make general conclusions summarizing the results of the interviews with all four enterprises (marketing departments) in order to get the average result about the level of EU principles implementation in the provision of SGEI in the Republic of Serbia.

The research instrument used is the interview, structured in two parts: the current use of activities which enhance consumers' orientation of public services, then the alignment of management with the principles of European framework of SGEI (defined in the White Paper of SGEI).

The research is conducted by the authors of this paper in the period from 01.07.2012 up to 15.07.2012, on the territory of city of Belgrade. The chosen enterprises provide SGEI at the national level.

Main limitations/problems in conducting the research relate to the in advance defined sample of only four enterprises (only SGEI as defined at supranational level), as well as the strong hierarchical structure of the duties and responsibilities in public enterprises and closed, "not easy available" way of internal functioning which make the access to the persons of charge more difficult. Respecting these rules, full anonymity of interviewees is accepted.

This research is dealing with the perspective of the public enterprises, in other words, the supply side whereas the opinions of the consumers of SGEI, albeit demand side, are still there to be enquired, analyzed and synthesized. Accordingly, suggestion for the future research refers to the consumers' perspective and their satisfaction with the access, quality, efficiency and affordability of the services of general economic interest in the Republic of Serbia.

## ***SUMMARIZING AND ANALYSIS OF THE EMPIRICAL RESEARCH RESULTS***

All of the four public enterprises analyzed have the active marketing department in the organizational structure, within which most of the activities concerning relationship with consumers of services are dealt with. In other words, awareness of consumers and customers exists at the operational level in each public enterprise. However, when it comes to the effective and efficient usage of marketing principles in practice, there are evident differences between the public enterprises. Nevertheless the aim of this research is to give the overall picture of the consumer orientation and professionalization of management in the analyzed public enterprises, so the comparisons between individual cases and their ranking are intentionally left out.

*Table 1: The level of consumer orientation in the analyzed public enterprises (providers of services of general economic interest in the Republic of Serbia)*

Activities enhancing the consumer orientation	Level of application
Dissemination of the relevant information to citizens-consumers	Full
Managing the system of feedback from the citizens-consumers	Partial
Managing the system of consumers' appeals and complaints	Partial
Managing the system of consumers' satisfaction	Nonexistent/low

*Source: Authors' analysis*

The main characteristic of SGEI providers in the Republic of Serbia refers to the nonexistence of competitive environment. Strong monopolistic ambience discourages the management of SGEI to apply and strengthen the market and consumer orientation in the process of delivering public services. Hence, in all four enterprises analyzed, only the mass marketing principles are being used (characterized for production firms more than the service sector). So, there is only one-way mass communication. However, from marketing perspective, the communication means the exchange of information and their flow from two sides-providers and consumers, supply and demand. The implementation and management of feedback system from consumers as well as the system of consumers' appeals and complaints are only partially developed and used often only as a way to satisfy the form, leaving the substance aside. Although there are some forms of collecting the information from consumers, the level of motivating consumers on active participation in information exchange is very low and in certain cases even the existent mechanism of appeal is quite complicated and

therefore discouraging for consumers. Therefore, both mechanisms for two-way communication with the consumers (feedback and system of managing the appeals, complaints) are not given the proper attention. Moreover, the almost nonexistent system of monitoring the consumers' satisfaction additionally justifies the absence of two-way communication with the service consumers indicating at the same time a very low level of market orientation in the field of services of general economic interest. To conclude, the weakest point of the providers of SGEI can be found in the relationship with the consumers and overall market orientation of the service providers. Hence, the development and management of organized, systematized and strategically focused channels of communication with the final users of the services of general economic interest should be improved.

*Table 2: The application of the European Union's principles of SGEI in the analyzed public enterprises (providers of services of general economic interest in the Republic of Serbia)*

<b>Guiding principles of SGEI</b>	<b>Level of application</b>
To operate close to citizens	Partial/Low
Ensuring cohesion and universal access	Full
Maintaining a high level of quality, security and safety	Full/Partial
Ensuring consumer and user rights	Full
Monitoring and evaluating the performance	Partial
Respecting diversity of services and situations	Partial /Low
Increasing transparency	Full/Partial

*Source: Authors' analysis*

The analyzed enterprises judge their operations as being close to citizens. In almost all cases this principle is predominantly understood as active, one-way of information dissemination through the mass media. However, to operate close to citizens means much more than mere use of mass media. It also means getting to know the consumer needs, demands and preferences as well as having more flexibility in creating the service offer. These elements cannot be found in the business strategy of the SGEI providers. The probable reason for enterprises equating this principle with the mass communication comes from the fact that modern, strategic reform of public sector has not been done yet at the macro level. Consequently, the providers of services of general economic interest still operate as a highly bureaucratic monopoly, under the influence of the government structures and political issues. Without the macro environment that foster competition, motivation for practicing marketing philosophy at the micro level (level of enterprises) is substantially reduced and often considered as unnecessary. Therefore, the public enterprises are still unfamiliar with the notion of real market orientation and management of their operations close to citizens.

When it comes to the principal of universal access and territorial coverage, the situation is quite satisfactory. Moreover, the improvement of the infrastructure in order to achieve better territorial coverage with SGEI and make them accessible for all citizens is one of the major business priorities in all analyzed enterprises.

The standard concerning the quality, security and safety is fully implemented in the management of analyzed public enterprises. Although static, technical and technological sides of quality are indeed very important, maintaining the full quality of services requires also the implementation and constant improvements of its dynamic elements- two-way communication, interpersonal relationships and orientation to the real needs and preferences of the consumers. So, regarding the dynamic dimension of service quality, there is enough space for development and additional improvements. All of the analyzed enterprises comply with the legal regulations and rules in the domain of consumer and user rights. The necessary information about every service of general economic interest (type of service, prices) is publicly available and users are not misled by incorrect, inaccessible, confusing or outdated information.

Principles of monitoring and evaluation of performances represent the important segment of management in all SGEI providers. The annual business and financial reports are regularly published and made publicly available. Nevertheless, the integral parts of this standard also include the clear definition of responsibility and accountability for performances and results achieved, the mechanism of independent, professional control over business performances and the strategy for timely corrections in case of unsatisfactory results. These elements are quite weak in the management of SGEI providers in the Republic of Serbia. So, the principle of monitoring and evaluation of performances is considered as half-done, and hence cannot lead to a conclusion that the analyzed enterprises are goal-oriented.

In respect of diversity of services and situations the performance vary between the analyzed enterprises (some of them are more flexible in differentiating their services than the others). However, in average the level of flexibility in customizing the services according to the actual needs and possibilities of the users should be improved. The philosophy of "one-size-fits-all" is still dominating in the management of SGEI providers. Marketing tools such as segmenting the market, targeting the certain groups of consumers and creating customized service offer are not systematically applied in the marketing strategy of these enterprises. Bearing in mind that services of general economic interest have unique public mission, special attention should be paid to the services designed for vulnerable and marginalizes groups of users.

Since the annual business and financial results are published regularly, the level of transparency is judged as quite positive. However, in order to increase the transparency this principle should include all aspects of service production and delivery. According to that, there are still enough places for certain improvements when it comes to transparency of finance management, human resource management, evaluation of service quality and efficiency, control systems and management of consumers' appeals and complaints.

## ***CONCLUSION***

Starting from the new concept of public services in the European Union, in the year 2004 the European Commission issued White paper on Services of General Economic Interest (SGEI) stressing the main guidelines for improvement and professionalization of public service management: enabling public authorities to operate close to the citizens, achieving public service objectives within competitive open markets, ensuring cohesion and universal access, maintaining a high level of quality, security and safety, ensuring consumer and user rights, monitoring and evaluating the performance, respecting diversity of services and situations, increasing transparency and providing legal certainty.

In order to see at what extent the public service enterprises in the Republic of Serbia are aligned with the new, market and consumer orientated EU concept of public services and at what extent the management practices are in line with the EU basic guidelines, the empirical research is conducted and primary data are collected in the four public enterprises at national level.

Based on the analysis of data collected, it can be concluded that lowest level of compliance with the EU concept can be found in the domain of market and consumer orientation of the analyzed enterprises. Development and maintaining of providers'-users' relationship and "win-win" profitable exchanges have not yet been applied systematically and seriously in the management of SGEI providers at the national level.

When it comes to the management principles, certain aspects of SGEI providers' management are well aligned with the EU principles (universal access, territorial coverage, technical quality and safety, respect of consumer rights defined by the law, system of continuous monitoring and evaluation of service performances and transparency of final business and financial results). On the other side, there are aspects where considerable changes could be made (conducting business as closer to citizens as possible, understanding quality management from broader perspective, expand the system of monitoring and evaluation by defining the clear responsibility for final results, the system of independent control and the plan for future improvements, increasing flexibility in service provision and delivery in order to be able to react on the diversity of situations, making all aspects of management more transparent).

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## ***NEW SYSTEM OF ASSOCIATION CORNER SHOP'S IN SERBIA***

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### ***ABSTRACT***

*Retail space has become a set of resource around which a number of entities are fighting to provide a position for their items on the shelves of Retail Alliances. Also, the retail space is becoming a new marketing ground with a very strong effect of advertising on consumers decisions during the buying process. Creating and maintaining competitive advantage requires that Retail Alliance has advantages that its rivals do not have on the target markets. Of particular importance is competitive advantage based on knowledge. Retail stores gathered in the alliance have the opportunity to make sure that "the competition by working" in association with providing benefits to all members. The work traces the future activities of Retail Alliances, the way in organizing, survival in the market in order to competition and efficient response to consumer demands. The main objective of this paper is to present a focus on the demands of final consumers, which represents a general approach to explore the new role of retail in overcoming the gap between procurement market and sales market. Finally, the goal of the paper is derived from the object itself, and refers to the tendency to establish a theoretical framework and adequate empirical platform on which will be generated opportunities for defining new strategies for positioning retailing subjects, valid for achieving business success. Method in the study will be consist in the fact that on the basis of theoretical assumptions and the available published data to construct a model that future alliance should operate on the basis of the author's practical experience.*

***Key words:*** Retail Alliance, A Partnership, Efficient Consumer Response, Flexibility, Suppliers.

***JELclassification:*** L81, D71

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## ***INTRODUCTION***

The main task of this work is to adequately shows the main directions in the way of gathered action for corner shops on the Serbian market. The main objectives of the action are: the fight against monopolies, competition in the market associations, better commercial terms, procurement centralization, greater purchasing power.

## ***MAIN CRITERIA FOR MEMBERSHIP AND DEVELOPMENT PHASE OF THE ASSOCIATION***

Retail Alliance in the market is represented as a solvent partner in trade. Management has to worry about the conditions of competition in the short-term (meet customer needs) and on the long-term effectiveness of Retail Alliances. So, strategic management must be oriented in a way that the long-term Retail Alliance was effective. Management has to prepare an alliance for a successful business in the future, to answer the questions of what it was before and how it should be developed in the future, in order to take competitive advantage in the market. Retail Alliance is a newly formed system which strengthens the competitive position of local retailers and local shops, and the survival of many small and independent participants in the trading process. Retail Alliance members should respect each other in order to progress and improve the operations of retail stores. Membership in the Retail Alliances allows them to overcome the weaknesses that exist in terms of competitiveness of some national retailers. Within members are exchanging a lot of knowledge and information, where the cooperation of members takes place in relation to joint contracting, strengthen purchasing power, cooperation in the promotion, logistics, marketing and lobbying. So, the task of Retail Alliance is daily strengthening.

The objectives of the association or Retail Alliances:

- strengthening and improving the position of the members;
- belong to the group of top leaders in the market in the sector of high-current products;
- cover the entire (large) market;
- creation of a single retail systems, ie. unique functional and visual identity of the alliance;
- advancement made partnerships with suppliers;
- more flexible and longer payment currency and define additional rebates;
- implementation of centrally coordinated marketing activities, sales promotion: action sales and promotional activities at point of sale;

- joint public relations;
- computerization of operations;
- opportunity to develop products with trademarks of Retail Alliances.

Retail Alliance mission is to provide consumers high-quality goods and services for daily use with prices lower than the competition. Also, mission is to win market share and defending against monopolies. Gathered in alliances members have the opportunity to see for themselves that "competition through cooperation" clubbing action provides benefits to all of them. Membership in this group overcome the weaknesses that exist in terms of competitiveness of some traders, because in alliance they share a lot of information and knowledge and achieve a number of advantages. Some of them are:

- advantages in terms of supply chain management and the purchase price through the definition of lower prices in order to achieve price competitiveness, as well as more flexible and longer payment currency;
- the possibility of prepayment;
- better meet the expectations of consumers and suppliers,
- reducing the total cost;
- develop their own brands and expanding its image;
- protection from takeovers;
- transparent dissemination of business knowledge, information and experience;
- the performance advantages of promotional and other marketing activities
- number of specific and short-term benefits (making action leaflets, secondary position).

Development stages of Retail Alliances can be defined as follows:

- Defining business strategies and criteria for membership
- conducting interviews with prospective members and presenting ideas of business alliances,
- Beginning of preliminary business discussions with suppliers,
- Defining of the accession treaty in the Alliance
- signing contract with the members and provide all necessary information on the business member
- continued negotiations with suppliers and the signing of new commercial contracts for the year,
- the beginning of the implementation of the defined strategy.

The main criteria for membership in the alliance is their liquidity. It is essential that the potential member is financially capable and that in the last two years he has not been blocked. Financial liquidity can be easily checked on the website of the National Bank of Serbia and sales through suppliers in the field. The most important thing is that each member has to pay its dues payable to the eventual tolerance, if it is defined in the agreement on business cooperation with

suppliers. Before joining and signing the contracts with Retail Alliance, each member must provide the information listed in the following table.

*Table 1: The pre-accession documents*

No	Name of retail outlet	Street	Municipality	Phone	Store manager	Annual turnover	Lease or ownership	Property size
1.								
2.								
3.								
...								

<b>Company Name:</b>	
Company location:	
Address:	
Authorized person:	
Tax number:	
ID number:	
Account number:	
Number of employees:	
Number of vehicles for goods transport:	

<b>Best-selling products in 2013.</b>	<b>The largest suppliers in 2013.</b>	<b>The vendor participation in sales as a percentage</b>

<b>Authorized person:</b>	
Phone number:	
Mobile phone:	
e-mail:	
Fax number:	

<b>Submit copies of the following</b>		
1.solution for the Serbian Business Registers Agency	3.certificate of registration to the tax	5.notarized signatures of authorized representatives
2.certificate of incorporation	4.list of signatures	6.ID copy

Data listed in the table may serve Retail Alliances to meet future member of the alliance, to form an idea of the financial power of the future item. With the signing of the contract and receipt of the above information, each member is required to submit within 7 days information about turnover for a period of two years. The information must have the following data: annual sales by product category, the financial market for products and suppliers, as well as sales volume. Retail Alliance thus can predict their potential, ie. purchase power and thus on meetings with suppliers negotiate new commercial terms for the new fiscal year.

### ***INTRODUCING PRIVATE BRAND PRODUCTS IN ASSOCIATION***

The process of introducing products under private brand is conducted in two phases (Barac, 1999., pp. 38-45):

- a concept phase and
- executive phase.

Private Label Department conducts their projects based on the business plan approved by the director of the retail chain where is specified start and date of implementation of each project as well as the responsible person. The basis for corrective measures is to analyze variations planned / realized and identify the causes. The process of introducing new products under private brands is kept in a computer program MS Project, which chronicles the phases of the project, when, how, deadlines, responsible, planned comparison - realized, deviation and everything else that is necessary for the information of the individual projects. After the completion of each phase (concept and executive) of each project Private Label Department informs service projects. At the beginning of the year, Private Brand Manager informs the Project Director and Sales Director about projects that are planned for that calendar year. At the regular monthly meetings, Private Brand Manager report to the Project Director and Sales Director about realized projects and the results of these projects.

### ***THIRD FINANCIAL FLEXIBILITY ASSOCIATION***

In this section, special attention will be paid to the association financial flexibility through contracting commercial conditions.

Retail Alliance at meetings with suppliers as the main argument for improving commercial conditions mentioned two things:

- Increased purchasing power,
- financial security,

- implementation of the agreed across the network alliance.

Goal of the meetings is to improve waged on commercial terms, which is the purpose of the alliance. Agreed commercial terms would apply to every member of the alliance, regardless of its fair game. Retail Alliance should be seen as one entity. We will list such commercial terms, if the maximum rebate from a supplier to any member of the alliance was 11%, with an increase in merger and acquisition of power, retail alliance will agree to a minimum of 12%, but the vendors are required to pay quarterly Alliance 1% to finance the operations and management of the alliance. This would give suppliers a total of 13%.

Price competition recording can easily determine the rebate with competitors. The purpose of the negotiations with suppliers is to provide similar commercial terms with other retail systems in the market to competition. Retail Alliance's strategic goals should be to set up in each fiscal year to sign contracts with suppliers who have a stake in a maximum of 70% of financial transactions. Why? This is the way it creates flexibility in payments due debts. If a member of the alliance is unable to make a payment to a supplier with whom the Retail Alliance has a signed contract, he has the ability to redirect the money that is intended for suppliers who make up 30% of the turnover to suppliers with which the contract was signed, in order to respect the agreed currency and term partnerships with suppliers.

Corollary of this theory is that the vendors with which the alliance has signed the priority for payment of overdue invoices. Through this flexibility alliance can survive for long without significant problems that threaten its business.

### ***CONCEPT OF COMPETITIVENESS AMONG SUPPLIERS IN ASSOCIATION***

Because of the financial flexibility as a key strategy for the alliance, which introduces competition among vendors, suppliers to the demands of the alliance will come out with positive thinking. For example, if there are five manufacturers of soft drinks on the market, the Retail Alliance will sign contracts with manufacturers that participate in the trade about 70%. Which vendors will sign contracts with Retail Alliance is depending on suppliers, their flexibility and acceptance of the fact for improving commercial terms.

Suppliers with which the alliance had signed agreements will have the following benefits:

- defined amount per annum,
- defined marketing,
- payment security,
- defined positions in retail stores,
- defined range,
- the increase in turnover,

- a strategic partnership through the production of products under private brands.

## ***COMPETITION IDENTIFICATION***

Create and maintain a competitive advantage in the retail demands form Alliance that has advantages that are not available to its rivals in the target markets. Particularly important competitive advantage is based on knowledge. Once you identify your main competitors, Retail Alliance must consider their strategy, goals, strengths and weaknesses. Group companies apply the same strategy in a given target market is called a strategic group. When Retail Alliance identifies its main competitors and their strategies, should ask the following questions: what each competitor in the market is looking for? What affects on the behavior of each competitor? Many factors influence the goals of competitors, among them: (Ristic, 2008. pp. 98-105)

- size,
- history,
- current management and
- financial situation.

If a competitor is one division of a larger company, it is important to know whether it uses the parent company for growth, profit and exploitation. One of the benefits of assumptions that competitors are striving for is to maximize profits. However, companies vary in how they bit short compared to the long-term profits. Another hypothesis could be that a competitor is trying to accomplish a number of objectives: (Ristic, 2008. pp. 98-105)

- current
- profitability,
- growth,
- market
- share,
- cash flow,
- technology leadership or
- leadership.

Finally, the Retail Alliance must be accompanied by expansion plans of competitors. The company needs to gather information about the strengths and weaknesses of each competitor. Generally, companies should monitor three variables when analyzing competitors: (Kotler, 2006. pp.222-231)

- Market share - share of competitors in the target market.

- Participation in awareness - the percentage of customers who indicated competitor when answering the question "Specify the first company that you can think of when it comes to this industry sector."
- Participation in the emotional attachment - the percentage of customers who indicated competitor when answering the question "Indicate the company from which you wish to purchase a product."

### ***LONG-TERM AND SHORT-TERM RELATIONSHIP INTERESTS BETWEEN ASSOCIATION AND SUPPLIERS***

Looking at the substance and the types of relationships with suppliers, retailers, the right question is the practical feasibility of defining and securing the common goals of both complementary to the strategic partnership. It is noticeable that there is a tendency and growth trend of development of strategic partnership in the channels, but with those entities and to the extent it is economically rational. Partnership and cooperation are not imposed by force, they are the result of the need for pooling and concentration of power. However, is a great number of suppliers with which retail cooperate and continuous trend is to increase this number, which indicates the inability to establish the same level of quality relationships with all stakeholders in the supply chain. On the contrary, retail achieves cooperative relations with various degrees of complexity, which produce significantly different interests and results of operations. At this point, the question is raised of defining the boundaries between long-term and short-term interests of interconnected entities in channels of distribution and quantification of the effects that are achieved. (Gullberg, 2003. pp. 122-125)

Subjects in the Retail Alliances channel will seek increasingly to establish long-term cooperation with suppliers due to demand for improving business performance, resisting competitive pressures, reduce uncertainty and gaining mutual trust. However, there will always be a certain number of entities in the chain with which will be reasonable to establish short-term relationships, especially given the current interest, as opposed to aligning business goals and strategies in the long run. This trend is present due to dynamic and volatile market conditions, which require a change in the balance of power, position and role of particular companies. Although partnership with suppliers is common practice in business of modern retailers there are some real dangers from unexpected flows that can cause. Partners and alliance members can become mutually dependent, that will certainly encourage deeper cooperation, but also can reduce the flexibility of the rapid growth of retail alliances. Because of pleasure of the existing supplier mix and long-term relationships it can be missed reactions to the changing market conditions and the emergence of new products that will achieve higher growth in sales and market share jeopardize existing suppliers. In this sense we can say that the retail alliance must constantly monitor changes in market supply and market sales in order to retain the dynamic range management and portfolio of suppliers in

the supply chain. If the agent is concentrated on the acquisition of existing partners, it can happen to overlook or ignore better deals from other sources of supply for the product category for which he is responsible. Therefore, it should be emphasized the importance of combining short-term and long-term interests to maximize profitability and maintain a competitive advantage in the specific organizational format - Alliance. In the case of a short-term interests between suppliers and Retail Alliance is when retail sales, developing private trade mark, trying to replicate the brand of suppliers who have already expressed market image. The main motive of Retail Alliances to achieve an additional source of profit is to quickly introduce products to the market under the assumption that conscious consumers will equate quality and characteristics of products with private label brand suppliers whose products are copied. In this case the partnership is not expected, but a priority of both parties can be given by short-term interests for the supplier - to take advantage of economies scale effects and unused production capacity, and for retailers to exchange views and experiences in organizing the production process. After that, both subjects are independently care for the success of their brands in the market, without pretending to define a coherent strategy. Finally, it can happen the deterioration of relations and mutual hostility in the case when Retail Alliance copy brand of the manufacturer's as an attempt to appropriate a certain amount of national brand goodwill. In extreme cases there might be a war by market vendors sometimes try to point to the ultimate retail consumer brands trying to copy the appropriate built a reputation and image producers. Manufacturers can point out that the production of similar products is used only to manipulate and mislead consumers in order to achieve placement with the image of the original brands. Also, in practice, retailers are really trying to identify the attributes and characteristics of private labels with attributes and characteristics of the national brands, without investing significant resources in advertising and promoting their brands as producers have in the process of building its image. Manufacturers, as brand owners, warn that this type of unfair competition in the long term lead to a narrowing of choices and less interest in the future the manufacturer for further innovation. In addition to accusations of unfair competition, the manufacturers claim that copying designs and even packaging retail products do not invest in research activities, development, planning and implementation of marketing campaigns, but also to account for the effects that are achieved manufacturers, investing in that purpose, developing and original building of national brands. Because of this situation producers are less interested in developing new products because there is a high probability that the copied products of retailers, directly threatening the planned profit of potential national brands. If Retail Alliance thus prevent producers, who will lose the sale directly by the production of a copy, they will not be able to invest enough money in the development of new products in the future. The occurrence of copies before achieving a certain level of profitability from sales of national brands hindering the reproduction manufacturers and permanently affects the decline of interest in investing in the development of new products. The answer is that the similarity of retail products to their quick and easy comparison,

encouraging positive competition in the interests of consumers. Retailers accept the claim that their products are similar as products under the brand manufacturers, but reject accusations of unfair copying and emphasize a commitment to fair competition. The next potential field of disagreement interests between suppliers and Retail Alliance is determining the final price of the product. Each of these parties wants the possibility of a certain type of control and influence on the price. Manufacturers often want to project a unique image in the market by attempting to provide unique price for their products, regardless of the chosen distribution channel. They even sacrificed their own part of the price difference covering both retailers lower efficiency compared to others in order to achieve a unique calculation of rates in all channels of distribution. Nevertheless, many retailers want to base prices on its image, goals and current business concept. Suppliers can control prices in the event of system use exclusive distribution, launching its own retail stores and discount retailers refusing delivery. On the other hand, the retailer may not have control over pricing in the event that the company is an important customer, it may inhibit the overall sales of the supplier in the event of termination of cooperation, that has a range of products under private label items within the same category or have the ability to sold on the gray market. Sometimes it happens that deliberately charge high retail margins achieved regardless of the purchase price in the negotiation process with suppliers, to be able to favor the sale of its private label products due to their price-competitiveness in relation to the supplier of the product we have on the shelf. This form of promote sales and create a more favorable position for its products may jeopardize long-term relationships among related entities and put the focus solely on short-term transactional relationships and interests. (Barac, 2008. pp. 89-94)

Next, highlight the advantages with respect to short-term interests are reflected in the situation when e.g. Retail Alliance requires suppliers to pay compensation for the involvement of its product in retail stores. As we have said, by requiring compensation for inclusion in range, Retail Alliance wants to protect itself from the potential risks of market failure of new products. Thus a source of additional revenue and profit from the use of force in the channel that was controlled retail space. Manufacturers, even though they are aware that the practice is widespread, not look favorably on such a relationship and to understand as unfair way of redistribution of profits among companies in the marketing channels for the benefit of retailers. Short-term stress refers precisely these forms quickly and easily make extra profit, long-term relationships stress the mutual goals of improving profitability on the basis of growth in sales. In today's market conditions undoubtedly prevail commitment to collaboration and co-operation in marketing channels and supply chain. The main areas of cooperation, which are manifested to a greater or lesser degree are: (Borota, 2006. pp. 145-152)

- Value chain (in the form of savings and optimization of logistic processes and increase inventory turnover ratio)
- Financial analysis (analysis of the efficacy of pricing policies, presentation, promotion and ABC cost analysis);

- strategic marketing (understanding of consumer habits and perceptions, creating demand and improving the image of the joint).

Cooperation can be achieved in three ways: an open long-term cooperation, "hot-cold" relationship and transactional type relationships "buy-sell". In any case, the importance of open collaboration means focusing on creating more customer value, that is multifunctional ie. team approach, a joint business plan to maximize mutual opportunities and coordinated development of strategic projects. Finally, the specific field of operational and strategic cooperation between suppliers and retail alliances are: (Borota, 2006. pp. 145-152)

- Promotion planning. Associated entities jointly plan the promotion; must first negotiate a mutual responsibilities, planned expenditures and revenues, plan execution, and evaluation method generated effects.
- Management of space, which can be seen as a set of common activities and the development of effective standards of visual merchandising plans, operational best use shelf space in retail outlets.
- Managing the development of new products, including an active role in the design, planning, manufacturing process, packaging and defining the basic functional characteristics of the product.
- The introduction of a new product. The main objective of the joint introduction of a new product is to reduce potential problems in entering the market and the costs related to that occurring. The process involves the choice of a specific product to be introduced in assortment, making the introduction of the operating plan and related promotion and development of a methodology for measuring the results achieved in relation to expectations.
- Relationship management costs and prices to ensure fulfillment of the turnover volume that generates the maximum profit (given the level of price elasticity and total costs).
- Manage orders include specific activities such as receiving orders, processing and delivery of goods, in order to meet the demand for certain goods in the right quantity, at the appropriate time and with the correct invoice for the goods.
- Transportation management planning process involves joint transportation, handling, transfer and payments by the manufacturers, distributors and retailers.
- Inventory management is aimed at improving the level of inventory control at all stages of the supply chain and the optimization of the costs thereof. Plan and complete inventory of retail stores for the next period depends on the historical sales data from the POS terminal and expected trends in the market.
- Management of unsold goods not only involves a process in which slow moving and obsolete inventories down goods, but also preventive actions to forestall the emergence of phenomena destroyed, damaged and substandard quality goods. This reduces the costs that are caused in this way, and reduces the number of cases of return purchased goods that consumers were not satisfied.

In this sense, ask questions of business ethics in the interaction and interrelationship between related entities in marketing channels. Respect codes of ethics and good business practice to the dominant position of power and do not use unfair for profiting in the distribution of some participants at the expense of others, whose market power is significantly lower. In the development of mutual relations and the competitive bidding during the evolution of the channel, reveals and new forms of pressure on other businesses, so that limits intrusion into the unethical issues become so thin that it is almost double the possibilities of interpretation, depending on the angle of observation and possible analyst bias. Notwithstanding the commitment to long-term or short-term interests, in all respects, to be honorable requirement to comply with business ethics. This is a necessary precondition for the further development of Retail Alliances and encourage fair and loyal competition.

### ***IMPROVING MARKET PARTICIPANTS IN COOPERATION WITH SUPPLIERS***

When the strategic partnership is established with the aim to improve market performance of joint operations, critical decisions are related to the selection of partners. Then you have to define clear criteria for evaluating the benefits and the final choice of partner. Election of the members in the planning phase of the strategic partnership is a two-way process. In fact, the producers should choose the traders, and the trade should choose suppliers. The main objective of the manufacturer when selecting retail is to ensure an adequate distribution channel for their products to the consumer and in this sense the new improved market performance of the power of partnerships. In assessing retailers, manufacturers often can use criteria such as market share, the number of retail outlets, the number of consumers who shop at these facilities, financial strength, purchasing and negotiating power, representation competitor in the retail portfolio and the level of cooperation with them, the future development retail network and the potential for new markets, the method of supply retailer prefer, geographic dispersion of retail stores and distribution center distance, reputation and image among consumers. It is therefore in the interest of retailers to join forces in order to increase the above criteria.

Retail Alliance when choosing manufacturers as a strategic partner wants to achieve the availability of products in the package, on the shelves of retail stores in accordance with the requirements and needs of the end consumers. In this sense, partner selection criteria can be:

- brand strength,
- quality and performance of products,
- market orientation and taking a global marketing campaign to support the sale,
- the willingness to accept the return of unsold products,

- reliable and the possibility of efficient and accurate processing of orders,
- timeliness of delivery,
- the presence of other products in the range of retail,
- supply conditions,
- complementarily with existing retail assortment,
- joint readiness development of new products,
- benefit from the standpoint of supporting private label projects etc.

There are many criteria for evaluating the potential benefits of establishing strategic partners, long-term relations of cooperation. Finally, we conclude that the importance of the selection criteria individually selected just depends on the area in which he wants to achieve the improvement of market performance. Final, Retail Alliance will be improving economic performance, reduce production costs, promotion of innovation and increased market orientation through diversification of economic activities are important for improving the quality of life and a better environment. (Ostojić, 2013.)

### ***FINANCIAL POWER OF STRATEGIC PARTNERSHIP ASSOCIATED***

Inevitable motive in establishing the strategic partnership of suppliers and Retail Alliance is to create a joint financial strength of suppliers members, especially the alliance. In developed market conditions integration and concentration of capital are growing and becoming a necessity and a critical factor in the survival of the market. The pooling of resources partners see opportunity to help overcome the barriers to entry into new markets that increasingly require large investments, and facilitate negotiations with a management and implementation of the agreed overall network alliance. Financial power can manifest itself in two ways: by increasing revenues and profitability on the one hand, and reducing administrative and other operating expenses, on the other. Associated investments can provide growth in sales and profits achieved, triggering a spiral of further growth of financial strength. Certain administrative and operating costs can be divided between partners or even reduced concerted activities and the exchange of professional opinion about a possible their optimization. Also, this should be considered as an advantage and share the burden of the investment risk due to the combined financial strength. There is no need to analyze individual growth effects of financial strength which in itself implies. There is a need to emphasize the possibility of using financial strength of associated members as a strong motive for entering certain entities in the partnership in alliance.

## ***DEVELOPMENT TECHNOLOGY AS A BASE FOR SUPPORT SERVICES***

Information technology is a necessary infrastructure for the functioning of modern strategic partnerships. This requires the exchange of information, and the improvement in this area can be strategic. Affiliate relationships may constitute a platform for continuous improvement and integration of technology as a support service to business-related subjects. We can summarize that information technology is an important factor supporting business concepts like retail alliances such as:

- quick and efficient response to consumer demand,
- integrated management
- inventory
- joint planning,
- forecasting and replenishment,
- Category Management,
- Customer Relationship Management,
- Shelf Management
- merchandising strategies etc.

## ***CONCLUSION***

The first and the most important task that needs to be addressed in the policy portfolio is to identify customer requirements in terms of quality and product properties. It is, in fact, determine the quality of the properties which will give consumers a priority. Product purchasing decisions involve choices between a number of functional, structural and aesthetic properties. Retail Alliance has to produce quality products on the market, or certain categories that consumers are looking for. Therefore, management of Retail Alliances must procure and sell quality products that meets their requirements. Gaps in structuring qualitative assortment are accompanied by frequent bargains, excessive inventories, and often permanently lost customers. On the other hand, unnecessarily tying funds for goods with a low turnover ratio equals disaster. Range policy of Retail Alliances should coordinate the interests of consumers and producers alliance. This means a balance between the needs and demands of consumers, on the one hand, and reality producers, on the other hand. The above equilibrium can not be achieved unless production and trading companies are not cooperating. Joint planning and production of the best selling range reflects to the unity of production and marketing of commercial enterprises. To stumbled upon receipt of the consumer products, retail assortment structure of the alliance to meet next looks, price and

consumer demands in terms of quality. Customer can perceive the value that it provides retail in several dimensions:

- Compliance with requirements;
- the possibility of a wide selection of products;
- the price level and brand image;
- services that add value;
- establishing relationships and creating experiences.

As with any business in general, there are certain risks associated with the operation of strategic alliances. The primary issue for Retail Alliance is to achieve the greatest possible value, while maintaining control, and how to choose members to achieve such a goal. There are two types of risks associated with strategic alliances:

- risk refers to the probability that the partner will appreciate the elements of a cooperation agreement,
- the risk environment is the amount of property that would be directly affected by changes in political, economic and competitive environment.

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